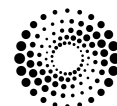


SELF-STUDY CONTINUING PROFESSIONAL EDUCATION

Companion to PPC's Guide to

Nontraditional Engagements



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Interactive Self-study CPE
Companion to PPC's Guide to
Nontraditional Engagements

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INTRODUCTION

Companion to PPC's Guide to Nontraditional Engagements consists of two interactive self-study CPE courses. These are companion courses to *PPC's Guide to Nontraditional Engagements* designed by our editors to enhance your understanding of the latest issues in the field. To obtain credit, you must complete the learning process by logging on to our Online Grading System at **cl.thomsonreuters.com** or by mailing or faxing your completed **Examination for CPE Credit Answer Sheet** for print grading by **December 31, 2011**. Complete instructions are included below and in the Test Instructions preceding the Examination for CPE Credit Answer Sheet.

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Each course is divided into lessons. Each lesson addresses an aspect of nontraditional engagements. You are asked to read the material and, during the course, to test your comprehension of each of the learning objectives by answering self-study quiz questions. After completing each quiz, you can evaluate your progress by comparing your answers to both the correct and incorrect answers and the reason for each. References are also cited so you can go back to the text where the topic is discussed in detail. Once you are satisfied that you understand the material, **answer the examination questions which follow each lesson**. You may either record your answer choices on the printed **Examination for CPE Credit Answer Sheet** or by logging on to our Online Grading System.

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COMPANION TO PPC'S GUIDE TO NONTRADITIONAL ENGAGEMENTS

COURSE 1

AN INTRODUCTION TO NONTRADITIONAL ENGAGEMENTS AND AGREED-UPON PROCEDURES ENGAGEMENTS (NTETG101)

OVERVIEW

COURSE DESCRIPTION: This interactive self-study course provides an overview of nontraditional engagements and describes the advantages and disadvantages of performing them. It also discusses the various types of nontraditional engagements that practitioners may perform. Further, this course describes the professional standards that apply to such engagements. In addition, this course discusses one type of nontraditional engagement in more detail: an agreed-upon procedures engagement.

PUBLICATION/REVISION DATE: December 2010

RECOMMENDED FOR: Users of *PPC's Guide to Nontraditional Engagements*

PREREQUISITE/ADVANCE PREPARATION: Basic knowledge of auditing

CPE CREDIT: 8 QAS Hours, 8 Registry Hours

Check with the state board of accountancy in the state in which you are licensed to determine if they participate in the QAS program and allow QAS CPE credit hours. This course is based on one CPE credit for each 50 minutes of study time in accordance with standards issued by NASBA. Note that some states require 100-minute contact hours for self study. You may also visit the NASBA website at www.nasba.org for a listing of states that accept QAS hours.

FIELD OF STUDY: Auditing

EXPIRATION DATE: Postmark by **December 31, 2011**

KNOWLEDGE LEVEL: Basic

Learning Objectives:

Lesson 1—Overview of Nontraditional Engagements

Completion of this lesson will enable you to:

- Recognize specific types of nontraditional engagements practitioners may perform.
- Identify professional standards that apply to nontraditional engagements.
- Recognize the effect of current developments in standard setting on nontraditional engagements.

Lesson 2—Overview of Agreed-upon Procedures Engagements

Completion of this lesson will enable you to:

- Identify the standards that apply to agreed-upon procedures engagements.

Lesson 3—Performing an Agreed-upon Procedures Engagement

Completion of this lesson will enable you to:

- Identify how to establish the terms of the engagement, as well as each element of the understanding with the client required by the attestation standards.
- Determine factors affecting engagement planning, including the responsibilities of the practitioner.

- Determine the purpose and basic requirements of workpapers and the representation letter in an agreed-upon procedures engagement.
- Recognize the elements of the practitioner's agreed-upon procedures report.
- Assess factors to consider when determining how to handle a change in the nature of the engagement and identify the quality control and peer review standards applying to agreed-upon procedures engagements.

TO COMPLETE THIS LEARNING PROCESS:

Send your completed **Examination for CPE Credit Answer Sheet, Course Evaluation**, and payment to:

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Lesson 1: Overview of Nontraditional Engagements

INTRODUCTION

Most clients and potential clients usually request typical accounting or audit services. Some, however, have specific needs that cannot be met by the traditional compilation, review, or audit of financial statements. In those cases, a nontraditional engagement will often provide the best alternative. This lesson provides an overview of nontraditional engagements. It discusses the pros and cons associated with performing them, as well as the professional standards that apply to them.

Learning Objectives:

Completion of this lesson will enable you to:

- Recognize the specific types of nontraditional engagements practitioners may perform.
- Identify professional standards that apply to nontraditional engagements.
- Recognize the effect of current developments in standard setting on nontraditional engagements.

WHAT ARE THEY?

In general terms, a nontraditional engagement is any engagement other than the traditional compilation, review, or audit of financial statements. Examples of nontraditional engagements include:

- Agreed-upon procedures.
- Audits, compilations, or reviews of specified elements of a financial statement.
- Audits, compilations, or reviews of special-purpose presentations.
- Other attestation engagements (such as reports on internal control, compliance, or nonfinancial information).
- Other assurance services (such as eldercare, risk assessment, and performance measurement).

Examples are discussed throughout this course.

When Do They Occur?

Most clients and potential clients request typical accounting or audit services. Some, however, have specific needs (for example, a demand by a potential lender, regulatory authority, stockholder, or absentee owner) that cannot be met by the traditional compilation, review, or audit of financial statements. In those cases, a nontraditional engagement will often provide the best alternative.

In some cases, nontraditional engagements occur when clients have a specific objective in mind (providing needed information for their use or someone else's), but not a specific type of service. They will often accept any engagement that results in a report on the information requested. Thus, the practitioner can often provide advice as to the most appropriate type of service in the circumstances.

Other times, a request for a *traditional* engagement may be an opportunity to provide a *nontraditional* engagement that better meets the client's needs. For example, a bank might ask for an audit of the financial statements when it really only needs assurance on the client's receivables and inventory that serve as collateral for a loan. In that case, a report on those specified financial statement elements might be of more benefit to the banker, less costly to the client, and involve less risk for the practitioner (since there is less of an *expectation gap* between what the bank desires and what it is getting). Also, a small-business owner might request an *audit* of the business's internal control when he or she really only wants specific procedures applied. In that case, an agreed-upon procedures engagement may be a better alternative.

What Are Their Advantages?

The primary advantage of nontraditional engagements is that they give practitioners added flexibility in meeting the needs of their clients. If practitioners are able to meet specific client needs in a cost-effective manner, this reduces the chance that clients may go elsewhere for the service. Nontraditional engagements can also provide opportunities for practitioners to establish relationships with potential new clients, thus opening up new practice development opportunities.

Another advantage of nontraditional engagements is their potential profitability. Whereas the traditional compilation, review, or audit of financial statements has come to be viewed, in many cases, as a commodity, nontraditional engagements are often viewed by clients as value-added services. Consequently, they can be more profitable than traditional engagements.

What Are Their Disadvantages?

The primary disadvantage of nontraditional engagements is a lack of familiarity with them on the part of practitioners and users. Financial statement compilations, reviews, and audits are generally more structured engagements. They require certain standard procedures and result in standard reports. Although they provide less opportunity to customize the engagement or report for the needs of the user, they may be more widely understood services, and practitioners may have more experience in providing them. Thus, there may be a higher comfort level in compiling, reviewing, or auditing financial statements than in providing other services.

How Does This Course Help?

Many CPA firms experience frustration when faced with obtaining a new nontraditional engagement. Although they relish the idea of expanding their practice, they are often unsure how to fulfill the client's request. They are faced with the question "What should we do now?"

This course is intended to answer that question. Its purpose is to assist practitioners when they are faced with something other than the traditional compilation, review, or audit of financial statements. In most cases, a client's request for a nontraditional engagement can be met, but the practitioner is faced with trying to identify the alternative services that can be provided and the standards that apply. This course provides guidance for choosing among those alternatives while complying with professional standards.

A brief description of some nontraditional engagements follows to assist you in identifying the type of engagement that best meets your client's needs.

Agreed-upon Procedures

An agreed-upon procedures engagement is one in which a practitioner is engaged by a client to perform specific procedures and report findings. The practitioner does not perform an audit or provide an opinion relating to the subject matter or assertion about the subject matter. Rather, the practitioner performs only those procedures that have been agreed to and reports findings.

The service is very responsive to the user's needs, since the practitioner does whatever procedures the user calls for. It is less expensive than standardized services because the practitioner is not required to apply procedures other than those requested. The practitioner's report provides no overall assurance—it only reports the findings resulting from the specified procedures. Accordingly, these engagements can reduce litigation risk, since the practitioner generally makes no judgments as to the scope of work or the appropriateness of the presentation. The value of an agreed-upon procedures engagement is that it enhances the credibility of the information to which the procedures are applied. But the client (or other users) are responsible for the adequacy of the procedures, not the practitioner.

Performance Measurement Services

Businesses have historically measured performance based on financial results. Since profit is the lifeblood of any business, financial measures are critical. However, many business managers now believe that long-term profitabil-

ity is better achieved by focusing on a balanced set of financial and nonfinancial measures. Performance measurement is basically a process of considering whether a client's performance measures are consistent with its overall business strategy.

Performance measurement services essentially involve the practitioner working with the client to—

- Define the organization's strategy.
- Develop performance measures.
- Implement a performance measurement system.
- Monitor the results of the performance measurement system.

Lease Agreements

Another engagement that is common for many local and regional firms is reporting in connection with a lease agreement. One of the more common of these engagements is reporting sales to a landlord for purposes of determining percentage rent. These engagements generally involve a schedule of sales, which is a specified financial statement element. Reporting on such schedules can consist of an audit, review, compilation, or agreed-upon procedures, and the relevant literature is as follows:

- Audit—SAS No. 62 (AU 623), *Special Reports*.
- Review—SSAE No. 10 (AT 101, *Attest Engagements*), as amended.
- Compilation—SSARS No. 13 (AR 110), *Compilation of Specified Elements, Accounts, or Items of a Financial Statement*.
- Agreed-upon Procedures—SSAE No. 10 (AT 201, *Agreed-upon Procedures Engagements*), as amended.

Specified Financial Statement Elements

Reporting on any specified element (other than a schedule of sales in connection with a lease agreement) might be applied to—

- A schedule of accounts receivable.
- A schedule of cash balances.
- A summary of PP&E.
- A statement of construction costs.
- A schedule of profit plan contributions.

Contracts

Engagements related to a contractual agreement such as a loan agreement, partnership agreement, profit sharing agreement, or licensing agreement are another type of nontraditional engagements. These engagements consist of such things as—

- Reporting, *in conjunction with an audit of the financial statements*, on the client's compliance with a contract (such as compliance with loan covenants).
- Reporting on special-purpose presentations prepared in accordance with a contract (such as financial statements that are neither GAAP nor OCBOA, and incomplete presentations that otherwise are in compliance with GAAP or OCBOA).

Compliance

Compliance engagements report on compliance with laws, regulations, or contractual agreements.

SSAE No. 10 (AT 601, *Compliance Attestation*), specifies the types of compliance-related services that practitioners can and cannot provide. Engagements subject to AT 601 include the following:

- Examining compliance with specific requirements (for example, with laws, regulations, or contractual agreements).
- Applying agreed-upon procedures regarding compliance with specific requirements.
- Applying agreed-upon procedures regarding the effectiveness of its internal control over compliance with specific requirements.

AT 601 prohibits review engagements. It also prohibits any other form of negative assurance regarding compliance (other than when provided in conjunction with an audit of the financial statements).

Pro Forma Information

Pro forma presentations are essentially recast historical financial statements. Their purpose is to show what the effects on historical information might have been had a transaction or event occurred at an earlier date. Engagements include the following:

- Examining, reviewing, or compiling pro forma information.
- Compiling pro forma information as supplementary information to compiled or reviewed historical financial statements.
- Reporting when pro forma information is treated as one of the assumptions for a prospective presentation.
- Assembling pro forma information, either with a report or as a plain paper service.
- Reporting on financial statements that disclose certain pro forma information required by GAAP.

Attestation Engagements

Attestation engagements are those engagements covered by Statements on Standards for Attestation Engagements. They include examination, review, and agreed-upon procedures engagements.

Attestation engagements occur whenever a practitioner is engaged to issue or does issue an examination, review, or agreed-upon procedures report on subject matter (or an assertion about the subject matter) that is the responsibility of another party. Attestation engagements provide the practitioner with flexibility in meeting a client's needs, primarily because the service can be applied to matters more varied than financial statements. Examples of matters that practitioners have provided attestation reports on include computer software, enrollment statistics, political contributions, the oxygen content of gasoline, and whether golfers hit Wilson Ultra golf balls farther than competitors' golf balls.

Internal Control

Another nontraditional engagement is to examine a client's internal controls (that is, to examine the effectiveness of its internal control over financial reporting) in conjunction with an audit of the entity's financial statements. Such engagements for nonpublic companies should be performed under SSAE No. 15 (AT 501, *An Examination of an Entity's Internal Control Over Financial Reporting That Is Integrated With an Audit of Its Financial Statements*).

Other internal control engagements include the following:

- Stand-alone examination of internal control effectiveness.
- Examinations on the design of internal controls.

- Reports issued in conjunction with financial statement audits (that is, communication of significant deficiencies and material weaknesses, management letters, etc.).
- Providing internal audit services.
- Reports on the internal controls of a service organization (SAS 70/SSAE No. 16 engagements).

Ownership Changes

There are engagements that arise when a practitioner is involved with the acquisition of one company by another. The specific type of engagement is acquisition assistance engagements.

Acquisition Assistance Engagements. Acquisition assistance is a term used to describe engagements in which a practitioner is asked to assist a client in *looking over* a prospective target. Other terms used for such services include *due diligence assistance*, *businessman's reviews*, *acquisition reviews*, and *acquisition analyses*. In these engagements, the practitioner simply applies general business and financial knowledge in looking over selected information and attempting to identify any critical areas that the client should be aware of.

Acquisition assistance engagements are often considered the domain of large firms whose clients are involved in large, complex acquisitions or mergers. However, local and regional firms, as well as sole practitioners, are sometimes requested to provide such services in their roles as business advisors to their clients. Some firms prefer performing these engagements as consulting engagements and others prefer to structure them as agreed-upon procedures engagements.

Other Nontraditional Engagements

Other engagements, include the following:

- Reports on the application of accounting principles.
- Services performed for financial institutions.
- Litigation support services.
- Fraud audits.
- Services performed for trusts and estates.
- Ballot-counting services.
- Trust Services (previously WebTrust and SysTrust services).
- Other requests in connection with an audit.
- Outsourced internal audit and controllership services.
- Attestation engagements performed under the Yellow Book.
- Engagements related to XBRL-tagged data.
- Other specialized attestation engagements.

Consulting engagements, as well as examinations, compilations, or assemblies of prospective information, could also be considered nontraditional engagements.

Eldercare Services

Because of their familiarity with a client's financial and personal affairs, CPAs are sometimes in a unique position to advise clients in matters relating to the care of older relatives and to help them administer their affairs. Services a practitioner might provide in this capacity include the following:

- Coordinating and overseeing periodic or full-time health care, including assistance in selecting care providers and establishing a system to monitor the quality of care provided.
- Handling routine financial transactions, including paying bills and ensuring that expected revenues are received and deposited.
- Arranging for transportation, yard maintenance, and other personal services.
- Determining whether investments are being managed per the elderly person's instructions.
- Making recommendations for funding health care expenses.
- Ensuring that all health care and retirement benefits are being received.
- Preparing payroll tax returns for in-home care providers.
- Ensuring that legal documents such as powers of attorney and living wills are in place.
- Reporting to family members about the quality of care being provided (based on criteria they establish) and other matters.

Other services practitioners could offer are limited only by their imagination and expertise.

Risk Assessment Services

An engagement could be helping a client identify and manage business risk. Business risk is the risk that an action or event will adversely affect an organization's ability to successfully achieve its objectives and execute its strategies. In order to be successful, a business must be able to effectively monitor and control its business risks.

Assessing and controlling business risks has become increasingly important in recent years due to changes in information technology and other developments. Because of their experience in assessing financial statement risk and designing internal control, and because of their knowledge of business practices, CPAs can provide valuable assistance to clients by helping them to identify and monitor risks.

Services that a CPA might perform related to risk assessment include the following:

- Helping a client identify and assess its business risks.
- Assessing risks that have been identified by a client.
- Evaluating a client's system for monitoring and controlling risks.

OVERVIEW OF THE APPLICABLE STANDARDS

Virtually all services a practitioner provides are subject to professional standards. With the proliferation of both services and standards, however, it is sometimes difficult to identify the right service and the standard that governs it. In general, the standards include:

- *AICPA Code of Professional Conduct.*
- Statements on Auditing Standards (SASs).

- Statements on Standards for Accounting and Review Services (SSARs).
- Statements on Standards for Attestation Engagements (SSAEs).
- Statements on Standards for Consulting Services (SSCSs).
- Statement on Standards for Valuation Services (SSVS).
- Statement on Quality Control Standards (SQCS).

This lesson provides an overview of the various standards. A discussion of current developments in standard setting for nonpublic entity engagements and recently issued AICPA standards is included as well.

SELF-STUDY QUIZ

Determine the best answer for each question below. Then check your answers against the correct answers in the following section.

1. Which of the following is a type of nontraditional engagement?
 - a. A compilation of financial statements.
 - b. An audit of financial statements.
 - c. An audit of a specified element.
 - d. A review of financial statements.
2. Which of the following is **not** an advantage of performing a nontraditional engagement?
 - a. Practitioners who perform nontraditional engagements have added flexibility in meeting the needs of their clients.
 - b. Nontraditional engagements often provide opportunities for practitioners to establish relationships with potential new clients.
 - c. One advantage of nontraditional engagements is their potential profitability.
 - d. Practitioners generally are as familiar with nontraditional engagements as they are with traditional engagements.
3. Which of the following best describes an agreed-upon procedures engagement?
 - a. In an agreed-upon procedures engagement, the practitioner provides an opinion relating to the subject matter or assertion about the subject matter.
 - b. In an agreed-upon procedures engagement, the practitioner performs only those procedures that have been agreed to with the user and reports findings.
 - c. An agreed-upon procedures engagement often is not responsive to a user's needs since the practitioner must perform procedures specified by standards.
4. When engaged to report on a schedule of sales to a landlord for purposes of determining percentage rent in connection with a lease agreement, a practitioner can provide **all but which** of the following services?
 - a. An audit in accordance with SAS No. 62 (AU 623), *Special Reports*.
 - b. A compilation in accordance with SSARS No. 13 (AR 110), *Compilation of Specified Elements, Accounts, or Items of a Financial Statement*.
 - c. A review in accordance with SSARS No. 19, *Compilation and Review of Financial Statements*.
5. Wilson Enterprises is completing a sale of its business to a competitor, Beacham, Inc. The president of Beacham has hired Kara, an auditor with Brown & Briddle to confirm the recent year-end financial statements of Wilson Enterprises. What type of nontraditional engagement has Kara been hired to complete?
 - a. An engagement to confirm the pro forma information of Wilson Enterprises.
 - b. An acquisition assistance engagement for Beacham.
 - c. A risk assessment engagement for Beacham.
 - d. An engagement to audit the contract between the two parties.

6. Which of the following types of nontraditional engagements provide internal audit services?
- a. Consulting.
 - b. Attestation.
 - c. Internal control.
 - d. Compliance.

SELF-STUDY ANSWERS

This section provides the correct answers to the self-study quiz. If you answered a question incorrectly, reread the appropriate material. **(References are in parentheses.)**

1. Which of the following is a type of nontraditional engagement? **(Page 3)**
 - a. A compilation of financial statements. [This answer is incorrect. A compilation of financial statements is a traditional engagement performed under the Statements on Standards for Accounting and Review Services.]
 - b. An audit of financial statements. [This answer is incorrect. An audit of financial statements is a traditional engagement performed under the Statements on Auditing Standards.]
 - c. **An audit of a specified element. [This answer is correct. An audit of a specified element is a nontraditional engagement. Generally, it is performed in accordance with SAS No. 62 (AU623), Special Reports.]**
 - d. A review of financial statements. [This answer is incorrect. A review of financial statements is a traditional engagement performed under the Statements on Standards for Accounting and Review Services.]
2. Which of the following is **not** an advantage of performing a nontraditional engagement? **(Page 4)**
 - a. Practitioners who perform nontraditional engagements have added flexibility in meeting the needs of their clients. [This answer is incorrect. Generally, because clients consider a nontraditional engagement to be cost effective, practitioners who provide such services are better able to meet the client's needs.]
 - b. Nontraditional engagements often provide opportunities for practitioners to establish relationships with potential new clients. [This answer is incorrect. Generally, providing nontraditional services offers unique opportunities for servicing clients and opening up new practice development opportunities.]
 - c. One advantage of nontraditional engagements is their potential profitability. [This answer is incorrect. Practitioners often have more flexibility over the amount to charge for nontraditional engagements since many clients view them as value-added services. In addition, most clients do not consider them commodities as they do audits, compilations and reviews of financial statements.]
 - d. **Practitioners generally are as familiar with nontraditional engagements as they are with traditional engagements. [This answer is correct. One disadvantage to performing nontraditional engagements is that many practitioners are not as familiar with them; therefore, they may have a higher comfort level in compiling, reviewing, or auditing financial statements than in providing other nontraditional services.]**
3. Which of the following best describes an agreed-upon procedures engagement? **(Page 4)**
 - a. In an agreed-upon procedures engagement, the practitioner provides an opinion relating to the subject matter or assertion about the subject matter. [This answer is the incorrect. The practitioner only reports findings in an agreed-upon procedures engagement; the practitioner does not opine on the subject matter of the engagement.]
 - b. **In an agreed-upon procedures engagement, the practitioner performs only those procedures that have been agreed to with the user and reports findings. [This answer is correct. In an agreed-upon procedures engagement, the practitioner and user agree on the procedures to be performed; the practitioner then issues a report on the results (findings) of those procedures, per the SSAE guidance.]**
 - c. An agreed-upon procedures engagement often is not responsive to a user's needs since the practitioner must perform procedures specified by standards. [This answer is incorrect. According to SSAE guidance, an agreed-upon procedures engagement generally is very responsive to a client's needs since the practitioner only has to perform procedures agreed to with the user.]

4. When engaged to report on a schedule of sales to a landlord for purposes of determining percentage rent in connection with a lease agreement, a practitioner can provide **all but which** of the following services? **(Page 5)**
- a. An audit in accordance with SAS No. 62 (AU 623), *Special Reports*. [This answer is incorrect. A practitioner *may* audit and report on a schedule of sales in accordance with SAS No. 62.]
 - b. A compilation in accordance with SSARS No. 13 (AR 110), *Compilation of Specified Elements, Accounts, or Items of a Financial Statement*. [This answer is incorrect. A practitioner *may* compile and report on a schedule of sales in accordance with SSARS No. 13.]
 - c. **A review in accordance with SSARS No. 19 (AR 100), *Compilation and Review of Financial Statements*. [This answer is correct. A practitioner would not follow the guidance in SSARS No. 19 when reviewing a schedule of sales, since SSARS No. 19 applies only to a complete set of financial statements. Instead, the practitioner could review the schedule of sales in accordance with SSAE No. 10 (AT 101, *Attest Engagements*).]**
5. Wilson Enterprises is completing a sale of its business to a competitor, Beacham, Inc. The president of Beacham has hired Kara, an auditor with Brown & Briddle to confirm the recent year-end financial statements of Wilson Enterprises. What type of nontraditional engagement has Kara been hired to complete? **(Page 7)**
- a. An engagement to confirm the pro forma information of Wilson Enterprises. [This answer is incorrect. Pro forma presentations are essentially recast historical financial statements. Their purpose is to show what the effects on historical information might have been had a transaction or event occurred at an earlier date. This is not what Kara has been engaged to complete. Beacham is asking for a confirmation of the most recent actual results.]
 - b. **An acquisition assistance engagement for Beacham. [This answer is correct. Acquisition assistance is a term used to describe engagements in which a practitioner is asked to assist a client in looking over a prospective target. The particular type of acquisition assistance engagement would be one of ownership changes. This type of engagement arises when a practitioner is involved with the acquisition of one company by another.]**
 - c. A risk assessment engagement for Beacham. [This answer is incorrect. A risk assessment engagement helps a client identify and manage business risk. Business risk is the risk that an action or event will adversely affect an organization's ability to successfully achieve its objectives and execute its strategies.]
 - d. An engagement to audit the contract between the two parties. [This answer is incorrect. While a contractual agreement audit is a form of a nontraditional engagement, it is an engagement related to the contractual agreement between the buyer and seller. Beacham, Inc. has asked Kara to confirm the financial statements of Wilson Enterprises, not the contract for the purchase of the company.]
6. Which of the following types of nontraditional engagements provide internal audit services? **(Page 6)**
- a. Consulting. [This answer is incorrect. Consulting is not a type of a nontraditional engagement.]
 - b. Attestation. [This answer is incorrect. Attestation engagements occur whenever a practitioner is engaged to issue or does issue an examination, review, or agreed-upon procedures report on subject matter (or an assertion about the subject matter) that is the responsibility of another party.]
 - c. **Internal control. [This answer is correct. Internal control is a nontraditional engagement performed to examine a client's internal control. Two examples of internal control include examining the design of internal controls and internal audit services.]**
 - d. Compliance. [This answer is incorrect. Compliance engagements report on compliance with law, regulations, or contractual agreements.]

Code of Professional Conduct

When It Applies. The *Code of Professional Conduct*, which was once called the code of ethics, applies to all professional services the practitioner provides. The *Code*, at ET 91.02 and ET 92.11, says that it applies to all services performed by a practitioner while *holding out* as a CPA, except for very limited exceptions (those called for by specific rules and certain services done by CPAs while practicing in other countries). According to ET 92.11, a practitioner *holds out* as a CPA if he or she informs others of his or her status as a CPA or AICPA-accredited specialist. This includes, for example:

- Oral or written representation to another regarding CPA status.
- Use of CPA designation on business cards or letterhead.
- The display of a certificate evidencing the CPA designation.
- Listing as a CPA in local telephone directories.

The *Code* also applies to other people in the practitioner's firm. ET 91.02, *Interpretation Addressing the Applicability of the AICPA Code of Professional Conduct*, states—

A member shall not knowingly permit a person, whom the member has the authority or capacity to control, to carry out on his or her behalf, either with or without compensation, acts which, if carried out by the member, would place the member in violation of the rules. Further, a member may be held responsible for the acts of all persons associated with him or her in the practice of public accounting whom the member has the authority or capacity to control.

Thus, a practitioner cannot avoid the rules by having an uncertified member of the firm perform acts the practitioner would be barred from performing.

All practitioners should follow the rules in the *Code*. When specific types of standards have been established to address specific types of services, the practitioner should also refer to those standards, but the code of conduct still applies. No specific standards conflict with the *Code*, but they generally are more restrictive and call for specific types of procedures or reports.

Form and Content. The *Code* consists of four parts: principles of professional conduct, rules of conduct, interpretations, and rulings.

Principles of professional conduct provide the framework for the *Code's* specific rules. They are found in the front of the *Code of Conduct*, ET sections 51–57.

Rules of conduct govern the performance of professional services. The AICPA Council establishes the rules and can designate bodies to establish technical standards under the rules. The rules consist of the following:

- Rule 101—Independence.
- Rule 102—Integrity and objectivity.
- Rule 201—General standards.
- Rule 202—Compliance with standards.
- Rule 203—Accounting principles.
- Rule 301—Confidential client information.
- Rule 302—Contingent fees.
- Rule 501—Acts discreditable.

- Rule 502—Advertising and other forms of solicitation.
- Rule 503—Commissions and referral fees.
- Rule 505—Form of organization and name. (Rule 504 has been deleted.)

Interpretations explain the rules. They are established by the AICPA Professional Ethics Executive Committee. A practitioner who departs from an interpretation has the burden of justifying the departure in any disciplinary hearing.

Rulings summarize the application of the rules and interpretations to a specific set of facts and circumstances. Practitioners who depart from the rulings in similar circumstances will be asked to justify those departures.

Ethics interpretations and rulings are exposed before they are established. They are published in the *Journal of Accountancy* and codified in the ET section of *Professional Standards*, volume 2. They are generally effective on the last day of the month in which the pronouncement is published in the *Journal*.

Independence Considerations. The primary rules governing independence are found in the AICPA *Code of Professional Conduct*. Exhibit 1-1 presents a listing of common independence considerations along with their applicable reference to the AICPA Professional Standards. This listing is not intended to be all-inclusive, but rather to assist accountants in finding information about the most common independence considerations.

Conceptual Framework for AICPA Independence Standards. ET Section 100.10, *Conceptual Framework for AICPA Independence Standards*, was adopted by the AICPA's Professional Ethics Executive Committee (PEEC) in January 2006 to be used by practitioners when making decisions on independence matters that are not explicitly addressed by the AICPA *Code of Professional Conduct*. The Conceptual Framework describes the risk-based approach to analyzing independence matters that is used by the PEEC when it develops standards. Under that approach, the practitioner's relationship with a client is evaluated to determine whether it poses an unacceptable risk to the practitioner's independence. Risk is unacceptable if the relationship would compromise (or would be perceived as compromising by an informed third party having knowledge of all relevant information) the practitioner's professional judgment when rendering an attest service to the client. Under the risk-based approach, steps are taken to prevent circumstances that threaten independence from compromising the professional judgments required in the performance of an attest engagement.

Exhibit 1-1

Independence Rules

Independence Consideration	AICPA Ref.
Another CPA Firm's Participation	ET 191.142–.143
Cooperative Arrangement with a Client	ET 101.14
Employment with a Client	ET 101.04
Business, Employment, and Family Relationships	ET 101.02
Fee Issues	ET 101.04, ET 191.103–.104
Financial Institution Clients	ET 191.075–.076, ET 191.081–.082, ET 191.150–.151, ET 191.170–.171
Gifts or Entertainment	ET 191.226–.229
Governmental Clients	ET 101.12
Indemnification of a Client	ET 191.204–.205
Investments	ET 101.02, ET 101.10, ET 101.17, ET 191.138–.139, ET 191.162–.163, ET 191.184–.185
Lease Property	ET 101.02, ET 191.182–.183
Litigation	ET 101.08, ET 102.03, ET 191.192–.193
Loans	ET 101.02, ET 101.07, ET 191.134–.135, ET 191.196–.197, ET 191.220–.221

Nonprofit Organization Clients	ET 101.06, ET 191.027–.028, ET 191.031–.034, ET 191.061–.062, ET 191.128–.129, ET 191.186–.187
Referral	ET 102.03
Retirement, Savings, Health and Welfare, or Similar Plan	ET 101.17, ET 191.041–.042, ET 191.119–.120, ET 191.214–.215, ET 191.222–.223
Services to Clients	ET 101.02, ET 101.05, ET 102.03, ET 191.003–.004, ET 191.017–.018, ET 191.021–.024, ET 191.031–.032, ET 191.037–.038, ET 191.144–.145, ET 191.164–.165, ET 191.198–.199, ET 191.206–.297, ET 191.222–.225
Significant Influence	ET 191.212–.213

* * *

The risk-based approach involves the following steps:

- Identifying and evaluating threats to independence. If identified threats are not considered to be at an acceptable level, safeguards should be considered.
- Determining whether safeguards already eliminate or sufficiently mitigate identified threats and whether threats that have not yet been mitigated can be eliminated or sufficiently mitigated by safeguards. A threat has been sufficiently mitigated by safeguards if, after application of the safeguards, it is not reasonable to expect that the threat would compromise professional judgment.
- If no safeguards are available to eliminate an unacceptable threat or reduce it to an acceptable level, independence would be considered impaired.

The Conceptual Framework also provides examples of threats to independence and of safeguards that may eliminate threats or reduce them to acceptable levels. Threats to independence are circumstances that could impair independence. Some examples of threats discussed in the framework include the self-review threat, the advocacy threat, the adverse interest threat, the familiarity threat, the undue influence threat, the financial self-interest threat, and the management participation threat. *Safeguards* are controls that mitigate or eliminate threats to independence. To be effective, safeguards must eliminate the threat or reduce to an acceptable level the threat's potential to impair independence. The three broad categories of safeguards discussed in the framework are:

- Safeguards created by the profession, legislation, or regulation.
- Safeguards implemented by the attest client.
- Safeguards implemented by the firm.

In instances where threats to independence are not at an acceptable level, safeguards should be applied and the following should be documented:

- The threats identified.
- The safeguards applied to eliminate the threats or reduce them to an acceptable level.

In conjunction with adopting the Conceptual Framework, PEEC also revised Interpretation 101-1, "Other Considerations," as follows, which requires AICPA members to consider the Conceptual Framework in making independence decisions:

It is impossible to enumerate all circumstances in which the appearance of independence might be questioned. In the absence of an independence interpretation or ruling under Rule 101 that

addresses a particular circumstance, a member should evaluate whether that circumstance would lead a reasonable person aware of all the relevant facts to conclude that there is an unacceptable threat to the member's and the firm's independence. When making that evaluation, members should refer to the risk-based approach described in the Conceptual Framework for AICPA Independence Standards [see ET Section 100.01]. If the threats to independence are not at an acceptable level, safeguards should be applied to eliminate the threats or reduce them to an acceptable level. In cases where threats to independence are not at an acceptable level, thereby requiring the application of safeguards, the threats identified and the safeguards applied to eliminate the threats or reduce them to an acceptable level should be documented.

Revised Interpretation 101-1 contains a footnote indicating that a failure to document would be a violation of Rule 202, *Compliance with Standards*. Independence would not be impaired if the member can demonstrate that he or she applied safeguards to eliminate unacceptable threats or reduce them to an acceptable level.

Independence and the Performance of Nonattest Services. Rule 101 of the AICPA *Code of Professional Conduct* requires independence for members in public practice. Practitioners should read Rule 101 of the *Code*, the interpretations of Rule 101, and the independence rulings for thorough guidance concerning independence.

For many nontraditional engagements, a frequent concern about meeting independence requirements is the effect of providing nonattest and attest services to the client. For many attest clients, the practitioner serves as a primary business consultant and may also provide consulting, tax, or other services to them.

Interpretation 101-3. Interpretation 101-3 (ET 101.05) states that the following requirements must be met in order for the performance of nonattest services for an attest client not to impair independence:

- *The Member Should Not Perform Management Functions.* Independence is considered to be impaired if a practitioner (or his or her firm) performs management functions or makes management decisions for a client. For example, determining which recommendations of the member should be implemented or reporting to the board of directors on behalf of management would impair independence. However, the practitioner may assist management in those functions or decisions. The Interpretation exempts from its scope certain routine activities, such as providing advice and responding to the client's technical questions as part of the normal client-practitioner relationship.

Certain activities performed as part of a nonattest service are considered to be management functions and, therefore, impair independence regardless of whether the auditor complies with the other requirements of Interpretation 101-3. The interpretation specifically states that performance of the following general activities would impair an auditor's independence (that is, they would preclude the auditor from being independent):

- Exercising authority on behalf of a client, such as authorizing, executing, or consummating a transaction, or having the authority to do so.
- Preparing source documents, in electronic or other form, that evidence the occurrence of a transaction.
- Having custody of client assets.
- Supervising client employees performing their normal recurring activities.
- Determining which of the auditor's recommendations should be implemented.
- Reporting to the board of directors on behalf of management.
- Serving as a client's stock transfer or escrow agent, registrar, or general counsel.
- Establishing or maintaining internal controls, including performing ongoing monitoring activities for a client.

An exhibit in the Interpretation looks at various other services, including bookkeeping, payroll, and other disbursements; benefit plan administration; investment advisory or management services; corporate finance consulting or advisory services; executive or employee search; business risk consulting; and certain information systems services. For each of these services, the exhibit looks first at characteristics of the service that would not be considered to impair independence and then looks at characteristics that would be considered to impair independence. The Interpretation also addresses appraisal, valuation, and actuarial services; internal audit assistance services; and how the characteristics of those services affect the practitioner's independence.

- *The Attest Client Must Agree to Perform Certain Functions.* The practitioner should be sure that the client is in a position to make an informed judgment on the results of the nonattest services and that the client understands its responsibilities to do the following:
 - Designate an individual with suitable skill, knowledge, and/or experience, preferably within senior management, to oversee the services to be performed.
 - Evaluate the adequacy and results of the services performed.
 - Make all management decisions and perform all management functions.
 - Accept responsibility for the results of the services.

In cases where the client is unable or unwilling to assume all of these responsibilities, the practitioner's performance of the nonattest services would impair independence.

When assessing whether a client's designated employee possesses suitable skill, knowledge, or experience as required by the Interpretation, it is not intended that the client's employee possess a level of technical expertise equal to the practitioner's. The client's employee need only understand the nonattest services enough to be able to provide general direction for the services; understand the key issues the practitioner identifies; make any required management decisions; and evaluate the adequacy of, and accept responsibility for, the results of the practitioner's work. This may mean the practitioner will need to educate the client in order to allow him or her to assume these responsibilities. For example, if the practitioner performs routine bookkeeping services for an attest client, he or she could ensure compliance with the requirements of the Interpretation by reviewing the proposed journal entries with the client and explaining in general terms how each entry affects the financial statements. The client should then be in a position to approve the journal entries and accept responsibility for the financial statements.

In addition, Interpretation 101-3 requires that the understanding between the member and the client must be documented in writing. To help prevent any type of misunderstanding with the client, the Interpretation states that, before performing the nonattest services for an attest client, the practitioner must document in writing his or her understanding with the client regarding the following:

- a. Objectives of the engagement (i.e., the nonattest services).
- b. Services to be performed.
- c. Client's acceptance of its responsibilities.
- d. Practitioner's responsibilities.
- e. Any limitations of the engagement.

Although failure to obtain the required understanding would impair independence, failure to comply with the Interpretation's requirement to document that understanding would not impair independence. Instead, such failure would be a violation of Rule 202, *Compliance with Standards*, of the AICPA's *Code of Professional Conduct*. A violation under Rule 202 is much less severe than a violation under Rule 101. A violation under Rule 202 may only generate an item for discussion, whereas a Rule 101 violation could result in a modified opinion in peer review.

The Interpretation does not specify how the written understanding is to be documented, so the practitioner has flexibility. For example, the understanding might be documented in a separate engagement letter, the workpapers, an internal memo, or the engagement letter obtained in conjunction with an attest engagement. The notes to the sample engagement letters throughout this course contain suggested language for instances when nonattest services are performed in conjunction with attestation engagements. The practitioner can choose to document the understanding with the client about the performance of nonattest services other than in the engagement letter.

The documentation requirement does not apply to nonattest services performed prior to the client becoming an attest client. The member would be permitted to prepare the required documentation upon acceptance of an attest engagement, provided the member is able to demonstrate his or her compliance with the other general requirements during the period covered by the subject matter, including the requirement to establish an understanding with the client. As a practical matter, practitioners who are initially engaged to only provide nonattest services but expect to subsequently be engaged to also provide attest services should consider structuring the engagement so that performance of the nonattest services will not impair independence for the attest services.

Interpretation 101-3 (ET 101.05) also addresses tax compliance services. Preparing a tax return (including informational tax forms) and transmitting the tax return and related payment, either electronically or in paper form, to a taxing authority does not impair independence as long as the practitioner does not have custody or control of the client's funds and the individual overseeing the tax services (a) reviews and approves the return and payment and (b) signs the return prior to transmittal, if required for the filing. The Interpretation states that making electronic payments under a taxing authority's specified criteria or remitting a check payable to the taxing authority signed by the client is not considered to be having custody or control of the client's funds. Signing and filing a tax return on behalf of client management impairs independence unless the practitioner has legal authority to do so and—

- The taxing authority has prescribed procedures, allowing the taxpayer to permit the practitioner to sign and file a return on the taxpayer's behalf, that meet the standards for electronic return originators and officers outlined in IRS Form 8879; or
- An individual in client management who is authorized to sign and file the tax return provides the practitioner with a signed statement that indicates—
 - The return being filed.
 - That the individual is authorized to sign and file the return.
 - That the individual has reviewed the return, including accompanying schedules, and it is true, correct, and complete to the best of their knowledge and belief.
 - That the individual authorizes the practitioner (or another named member in the practitioner's firm) to sign and file the return on behalf of the client.

The Interpretation also indicates that the practitioner's representation of the client in an administrative proceeding before a taxing authority does not impair independence, providing that practitioner obtains the client's agreement prior to committing the client to a specific resolution with the taxing authority. Independence is impaired if the practitioner represents the client in court to resolve a tax dispute.

A court encompasses a tax court, district court, or federal court of claims and equivalent state, local, or foreign forums. In addition, representation before forums that are equivalent to a court would impair independence. PEEC has determined that the following criteria would be indicative that the forum is equivalent to a court: (a) The forum is presided over by a trier of fact who is independent of the taxing authority and is empowered to render a determination that is binding (absent appeal); (b) The forum conducts formal proceedings governed by a set of procedural rules dealing with matters such as evidence and testimony; (c) The forum is the last opportunity for the parties to present new factual evidence so that any appeal of the forum's decisions would involve only a review of the forum's records, including its factual or legal findings, and not an evidentiary hearing.

In addition, under Interpretation 101-3, certain appraisal, valuation, or actuarial services are considered to impair independence. Performing appraisal, valuation, or actuarial services impairs independence if the results are

material to the financial statements and the service involves significant subjectivity. For example, a material asset appraisal or business valuation generally involves significant subjectivity and, therefore, would impair independence if performed for financial statement purposes. However, an actuarial valuation of a client's pension liabilities ordinarily does not require significant subjectivity and, therefore, would not impair independence even if the amount was material.

Under Interpretation 101-3, certain types of forensic accounting services may impair independence. Independence is impaired if an accountant conditionally or unconditionally agrees to provide expert witness testimony for a client. However, under certain defined conditions, independence is not impaired if the accountant provides expert witness testimony for a large group of plaintiffs or defendants that includes the accountant's client. If the accountant provides litigation services where he or she is a trier of fact, special master, court-appointed expert, or arbitrator in a matter involving a client, independence is impaired.

In some cases, the practitioner may assist with the client's internal audit function. Interpretation 101-3 also addresses the impact of those services on the practitioner's independence. According to the Interpretation, performance of internal audit assistance services does not impair the practitioner's independence as long as the practitioner is not an employee of the client or does not act in the capacity of management (for example, determining the scope, risk, and frequency of internal audit activities). The practitioner should be satisfied that the client understands its responsibility for directing the internal audit function. The general requirements of the Interpretation discussed previously also must be met. With respect to providing assistance with the internal audit function, the practitioner should be satisfied that the board of directors, audit committee, or other governing body is fully informed of the engagement.

Finally, the Interpretation incorporates by reference the independence requirements of other authoritative bodies. It states that failure to meet more restrictive independence requirements of any regulatory bodies (such as the SEC, GAO, DOL, and state boards of accountancy) relevant to the engagement constitutes a violation of the interpretation.

The practitioner must carefully consider the requirements of Interpretation 101-3 when performing nontraditional engagements. A nontraditional engagement can be structured as an attest engagement, a nonattest engagement, or a combination of both. For example, a buyer acquisition engagement can be structured as an agreed-upon procedures engagement (an attest service) or a consulting engagement (a nonattest service). Dual engagements can involve both consulting and attest services. Practitioners must be careful to meet the requirements of Interpretation 101-3.

In certain circumstances, practitioners may not be sure whether the performance of certain services are nonattest services that would fall under the requirements of Interpretation 101-3. Nothing precludes the practitioner from following the Interpretation's requirements when in doubt.

Informing Clients of Outsourcing Arrangements. Ethics Ruling 112 (ET 191.224–.225) under Rule 102, *Integrity and Objectivity*, requires that clients be informed, preferably in writing, if the practitioner's firm will outsource professional services to third-party service providers. If the practitioner intends to use third-party service providers (that is, entities not controlled or individuals not employed by the firm), the client must be informed before confidential client information is shared with the service provider. Also, revised Ethics Ruling No. 1 (ET 391.001–.002) under rule 301, *Confidential Client Information*, states that, if the accounting firm does not enter into a contractual agreement with the third-party service provider requiring the third party to (a) maintain the confidentiality of the client's information and (b) have procedures in place to prevent unauthorized release of confidential information, the accounting firm must obtain the client's consent to disclose the client's confidential information to the third-party service provider. Examples of the use of such services might be use of a specialist, having a third party observe inventory, using contract employees, or having another firm audit a specified element as part of an audit engagement. The client is not required to be informed when a third party is used only for administrative support services, such as record storage or software application hosting.

In cases where the practitioner chooses to provide written disclosure that a third-party service provider will be used, the following paragraph may be included in the engagement letter:

We may, from time to time and depending on the circumstances, use third-party service providers in serving your account. We may share your confidential information about you with these service providers, but remain committed to maintaining the confidentiality and security of your information. Accordingly, we maintain internal policies, procedures, and safeguards to protect the confidentiality of your personal information. In addition, we will secure confidentiality agreements with all service providers to maintain the confidentiality of your information, and we will take reasonable precautions to determine that they have appropriate procedures in place to prevent the unauthorized release of your confidential information to others. In the event that we are unable to secure an appropriate confidentiality agreement, you will be asked to provide your consent prior to the sharing of your confidential information with the third-party service provider. Furthermore, we will remain responsible for the work provided by any such third-party service providers.

Statements on Auditing Standards (SASs)

When They Apply. SASs apply to audits of financial statements for nonpublic entities. In addition, certain specific SASs apply to the following other situations:

- Filings under federal securities statutes.
- Condensed financial statements and selected financial data.
- Reports on the application of accounting principles.
- Reports on compliance with aspects of contractual agreements issued in conjunction with an audit.
- Special-purpose financial presentations to comply with contractual agreements or regulatory requirements.
- Reports on processing of transactions by service organizations.
- Letters for underwriters.
- Compliance auditing for recipients of government funds.

The practitioner is required to follow the procedure and reporting guidance in SASs whenever they apply. The requirement comes from two sources:

- Rule 202 of the *Code of Professional Conduct* requires adherence to them.
- Many state accountancy laws define the provisions of the SASs as GAAS, and require adherence to them as well.

Form and Content. SASs are issued by the AICPA Auditing Standards Board, which exposes the standards before issuance. When they are issued, the standards are published in the *Journal of Accountancy*, and free-standing copies can be purchased from the AICPA. Each new standard carries an effective date, which is based on the Board's assessment of the lead time practitioners require to implement the standard. The standards are codified in the AU Section of *Professional Standards*, volume 1. There were 120 SASs included in the AICPA's *Codification of Auditing Standards* as of the date of this course.

The auditing standards division also issues auditing interpretations. These pronouncements explain sections of standards that are ambiguous or the standards' application in situations not envisioned when they were originally issued. They are not enforceable under the code of conduct, but practitioners should be prepared to justify departing from them if their work is challenged. Interpretations are not exposed before issuance. They are published in the *Journal of Accountancy* and usually on the AICPA's website at www.aicpa.org when issued, and they are codified in the AU Section of *Professional Standards* immediately following the standards they interpret.

Statements on Standards for Accounting and Review Services (SSARSs)

When They Apply. SSARS apply to services on unaudited financial statements or financial information of nonpublic entities. They establish the two services practitioners can apply to such financial statements—compilation and review.

When the practitioner submits unaudited financial statements of a nonpublic entity, he or she is required to either compile or review them in accordance with the SSARS. The SSARS define the term *financial statement* generally as something that looks like a financial statement, but is not a tax return. It defines *submitting financial statements* as presenting to a client financial statements that the practitioner has prepared either manually or through the use of computer software.

The practitioner is required to follow the procedure and reporting guidance in SSARS whenever they apply. Rule 202 of the *Code of Professional Conduct* requires it, and many state accountancy laws require adherence to them as well.

Form and Content. SSARS are issued by the AICPA Accounting and Review Services Committee. ARSC exposes the standards before issuing them. When they are issued, the standards are published in the *Journal of Accountancy*. Free-standing copies of the new standard can also be purchased from the AICPA. Each new standard carries an effective date, which varies based on ARSC's assessment of the lead time practitioners require to implement the standard. The standards are codified in the AR section of *Professional Standards*.

SSARS interpretations are issued to explain sections of standards that are ambiguous or the standards' application in situations not envisioned when they were originally issued. They are not enforceable under the code of conduct, but practitioners should be prepared to justify departing from them if the quality of their work is challenged. Interpretations are not exposed before issuance. They are published in the *Journal of Accountancy* and usually on the AICPA's website at www.aicpa.org when issued, and they are codified in the AR Section of *Professional Standards* immediately following the standards they interpret.

There have been 19 SSARS issued to date. They are:

- SSARS No. 1 (AR 100), *Compilation and Review of Financial Statements* (December 1978). (SSARS No. 1 will be superseded when SSARS No. 19 becomes effective on December 15, 2010.)
- SSARS No. 2 (AR 200), *Reporting on Comparative Financial Statements* (October 1979).
- SSARS No. 3 (AR 300), *Compilation Reports on Financial Statements Included in Certain Prescribed Forms* (December 1981).
- SSARS No. 4 (AR 400), *Communications Between Predecessor and Successor Accountants* (December 1981).
- SSARS No. 5, *Reporting on Compiled Financial Statements* (July 1982) (Superseded November 1992 by the issuance of SSARS No. 7).
- SSARS No. 6 (AR 600), *Reporting on Personal Financial Statements Included in Written Personal Financial Plans* (September 1986).
- SSARS No. 7, *Omnibus Statement on Standards for Accounting and Review Services—1992* (November 1992) (Not published as a stand-alone section). (Portions of this SSARS amended SSARS No. 1. SSARS No. 1, as amended, will be superseded when SSARS No. 19 becomes effective on December 15, 2010.)
- SSARS No. 8, *Amendment to Statement on Standards for Accounting and Review Services No. 1, Compilation and Review of Financial Statements* (October 2000) (Not published as a stand-alone section). (This SSARS amended SSARS No. 1. SSARS No. 1, as amended, will be superseded when SSARS No. 19 becomes effective on December 15, 2010.)

- SSARS No. 9, *Omnibus Statement on Standards for Accounting and Review Services—2002* (November 2002) (Not published as a stand-alone section). (Portions of this SSARS amended SSARS No. 1. SSARS No. 1, as amended, will be superseded when SSARS No. 19 becomes effective on December 15, 2010.)
- SSARS No. 10, *Performance of Review Engagements* (May 2004) (Not published as a stand-alone section). (This SSARS amended SSARS No. 1. SSARS No. 1, as amended, will be superseded when SSARS No. 19 becomes effective on December 15, 2010.)
- SSARS No. 11 (AR 50), *Standards for Accounting and Review Services* (May 2004). (This SSARS created AR section 50 in the codification and amended SSARS No. 2. AR 50 will be superseded when SSARS No. 19 becomes effective on December 15, 2010.)
- SSARS No. 12, *Omnibus Statement on Standards for Accounting and Review Services—2005* (July 2005) (Not published as a stand-alone section). (Portions of this SSARS amended SSARS No. 1. SSARS No. 1, as amended, will be superseded when SSARS No. 19 becomes effective on December 15, 2010.)
- SSARS No. 13 (AR 110), *Compilation of Specified Elements, Accounts, or Items of a Financial Statement* (July 2005).
- SSARS No. 14 (AR 120), *Compilation of Pro Forma Financial Information* (July 2005).
- SSARS No. 15, *Elimination of Certain References to Statements on Auditing Standards and Incorporation of Appropriate Guidance Into Statements on Standards for Accounting and Review Services* (July 2007) (Not published as a stand-alone section). (Portions of this SSARS amended SSARS No. 1. SSARS No. 1, as amended, will be superseded when SSARS No. 19 becomes effective on December 15, 2010.)
- SSARS No. 16 (AR 20), *Defining Professional Requirements in Statements on Standards for Accounting and Review Services* (December 2007). (This SSARS will be superseded when SSARS No. 19 becomes effective on December 15, 2010.)
- SSARS No. 17, *Omnibus Statement on Standards for Accounting and Review Services—2008* (February 2008) (not published as a stand-alone section). (Portions of this SSARS amended SSARS No. 1. SSARS No. 1, as amended, will be superseded when SSARS No. 19 becomes effective on December 15, 2010.)
- SSARS No. 18, *Applicability of Statements on Standards for Accounting and Review Services* (February 2009). (This SSARS amended SSARS No. 1. SSARS No. 1, as amended, will be superseded when SSARS No. 19 becomes effective on December 15, 2010.)
- SSARS No. 19, *Compilation and Review Engagements* (December 2009).

Approach to Inclusion of SSARS No. 19 in This Course. In December 2009, ARSC issued Statement on Standards for Accounting and Review Services No. 19, *Compilation and Review Engagements*. SSARS No. 19 is the most significant change to the compilation and review standards since their inception in 1978. It supersedes SSARS No. 16 (AR 20), SSARS No. 11 (AR 50), and SSARS No. 1, as amended by SSARS Nos. 7, 9, 10, 12, 15, 17, and 18 (AR 100), and is generally effective for compilations and reviews of financial statements for periods ending on or after December 15, 2010. Early implementation is permitted only for the optional disclosure in the compilation report of the reasons for an independence impairment.

As of the date of this course, the AICPA was in the process of making conforming changes to the remaining SSARS and Interpretative Publications. Those changes are expected to be made by December 15, 2010, the effective date of SSARS No. 19. Conforming changes have been made throughout this course for the issuance of SSARS No. 19.

In addition, the course has been thoroughly updated for SSARS No. 19, and all SSARS No. 1, SSARS No. 16, and SSARS No. 11 references have been replaced with the applicable references to SSARS No. 19. SSARS No. 19 is effective for periods that end on or after December 15, 2010. Early implementation is not permitted except for the optional disclosure in the compilation report for the reasons for an independence impairment.

As of the date of this course, the numbering and placement of the SSARS No. 1 Interpretations in the SSARS Codification have not yet been determined. Consequently, throughout this course, the SSARS No. 1 Interpretation references have been retained. However, those interpretations have been referred to as SSARS No. 19 interpretations instead. The AICPA is currently considering the SSARS No. 1 Interpretations in light of SSARS No. 19. Practitioners should be alert to final changes to those interpretations.

The numbering and placement of the SSARS No. 1 Interpretations in the SSARS Codification have not yet been determined. Consequently, throughout this course, the SSARS No. 1 interpretation numbers have been retained. However, these interpretations have been referred to as SSARS No. 19 interpretations instead.

Statements on Standards for Attestation Engagements (SSAEs)

When They Apply. SSAEs apply whenever the practitioner is engaged to issue or does issue an examination, review, or agreed-upon procedures report on subject matter (or an assertion about the subject matter) that is the responsibility of another party. Technically, this definition includes services such as audits and reviews of financial statements, but the SSAEs say that they do not supersede any guidance in the SASs or SSARSs. So, the practitioner should refer to the latter standards for the services that they cover. The SSAEs provide for three levels of services: examination, review, and application of agreed-upon procedures.

Practitioners are required by Rule 202 of the *Code of Professional Conduct* to follow the procedure and reporting guidance in SSAEs when they apply.

Form and Content. SSAEs may be issued by any of three AICPA senior technical committees—the Auditing Standards Board, Accounting and Review Services Committee, or Consulting Services Executive Committee. The issuing committee exposes the standards before issuance. When they are issued, the standards are published in the *Journal of Accountancy*. Free-standing copies of the new standard can also be purchased from the AICPA. Each new standard carries an effective date, which is based on the committee's assessment of the lead time practitioners require to implement the standard. The standards are codified in the AT section of *Professional Standards*.

As of the date of this course, the following standards have been issued:

- SSAE No. 10, *Attestation Standards: Revision and Recodification*—SSAE No. 10 is organized in the following sections:
 - AT 101—*Attest Engagements*. (This is the umbrella standard that governs all types of attestation engagements.)
 - AT 201—*Agreed-upon Procedures Engagements*.
 - AT 301—*Financial Forecasts and Projections*.
 - AT 401—*Reporting on Pro Forma Financial Information*.
 - AT 601—*Compliance Attestation*.
 - AT 701—*Management's Discussion and Analysis*.
- SSAE No. 11, *Attest Documentation*—SSAE No. 11 was issued in January 2002 and amends the documentation requirements of SSAE No. 10.
- SSAE No. 12, *Amendment to Statement on Standards for Attestation Engagements No. 10*, *Attestation Standards: Revision and Recodification*—SSAE No. 12 was issued in September 2002 and also amends SSAE No. 10 to clarify the relationship of the SSAEs to the Statement on Quality Control Standards. The amendment clarifies that although an effective quality control system is conducive to compliance with SSARS, deficiencies in or noncompliance with a firm's quality control system do not, in and of themselves, indicate that an engagement was not performed in accordance with the attestation standards.

- SSAE No. 13 (AT 20), *Defining Professional Requirements in Statements on Standards for Attestation Engagements*. SSAE No.13 defines terms used in the SSAEs to impose professional requirements.
- SSAE No. 14 (AT 50), *SSAE Hierarchy*. This standard identifies the body of attestation literature and clarifies the authority of attestation publications.
- SSAE No. 15 (AT 501), *An Examination of an Entity's Internal Control Over Financial Reporting That Is Integrated With an Audit of Its Financial Statements*, establishes standards and provides guidance to practitioners performing an examination of a nonissuer's internal control over financial reporting (internal control) that is performed as an integrated audit (an audit of an entity's financial statements and an examination of its internal control).
- SSAE No. 16, *Reporting on Controls at a Service Organization*, provides guidance relating to reporting on the internal controls of a service organization and supersedes the service auditor portion of SAS No. 70. It is effective for service auditors' reports for periods ending on or after June 15, 2011.

The Institute also issues SSAE interpretations. These pronouncements explain sections of standards that are ambiguous or the standards' application in situations not envisioned when they were originally issued. They are not enforceable under the code of conduct, but practitioners should be prepared to justify departing from them if their work is challenged. Interpretations are not exposed before issuance. They are published in the *Journal of Accountancy* and usually on the AICPA's website at www.aicpa.org when issued, and they are codified in the AT section of *Professional Standards* following the section they interpret.

SSAE Hierarchy. SSAE No. 14, *SSAE Hierarchy*, identifies the body of attest literature and clarifies the authority of attest publications issued by the AICPA and others. It specifies the attest publications that the practitioner must comply with and those that the practitioner should be aware of when performing an engagement. The standard also amends the 11 attestation standards to conform them to the terms used in SSAE No. 13.

SSAE No. 14 establishes three levels in the SSAE hierarchy:

- Attestation Standards.** Attestation standards consist of the 11 general, field work, and reporting standards and Statements on Standards for Attestation Engagements (SSAEs) issued by the AICPA's Auditing Standards Board (ASB). SSAEs are codified within the framework of the eleven standards. The *AICPA Code of Professional Conduct* requires members to comply with SSAEs.
- Attestation Interpretations.** Attestation interpretations are not attestation standards, but rather recommendations on applying the SSAEs in specific circumstances. Attestation interpretations include Interpretations of the SSAEs, appendixes to the SSAEs, and attestation guidance in AICPA Audit and Accounting Guides and AICPA Attestation Statements of Position. SSAE No. 14 states that practitioners should be aware of and consider applicable attestation interpretations. If the practitioner does not apply an attestation interpretation, the practitioner should be prepared to explain how he or she complied with the underlying SSAE provisions.
- Other Attestation Publications.** Other attestation publications have no authoritative status but may help practitioners understand and apply the SSAEs. Other attestation publications include AICPA publications not referred to in item b, attestation articles in professional journals and the *AICPA CPA Letter*, continuing professional education programs and other instructional materials, textbooks, guide books, attest programs and checklists, and attestation literature published by state CPA societies, other organizations, and individuals (for example, PPC guides). If practitioners apply the guidance in other attestation publications, they should satisfy themselves that the guidance is both appropriate and relevant. Appropriateness refers to whether the guidance is technically sound. Relevance refers to whether the guidance is applicable to the circumstances of a particular engagement. Indicators of appropriateness include the extent to which the publication is recognized as being helpful and the professional qualifications of its author or issuer. There is a presumption that other auditing publications reviewed by the AICPA Audit and Attest Standards staff are appropriate.

SSAE No. 14 also amended the 11 general, fieldwork, and reporting attestation standards to conform them to the terms used in SSAE No. 13. Under SSAE No. 14, all 11 attestation standards use the word *must* and are therefore unconditional requirements.

Statements on Standards for Consulting Services (SSCSs)

When They Apply. SSCSs apply to engagements in which the practitioner develops the findings, conclusions, and recommendations presented. The practitioner does not attest to someone else's assertions, but is the one who develops the final presentation.

Consulting services include the following: consultations, advisory services, implementation services, transaction services, staff and other support services, and product services. They do not include any of the services described in SASs, SSARSs, or SSAEs. Nor do they include tax return preparation, tax planning or advice, tax representation, personal financial planning, or bookkeeping services. They also do not apply to recommendations or comments prepared during an excluded service (such as an audit) as a direct result of that service.

Practitioners are required by Rule 202 of the *Code of Professional Conduct* to follow the procedure and reporting guidance in SSCSs when they apply.

Form and Content. SSCSs are issued by the Consulting Services Executive Committee. It has issued only one SSCS to date: *Consulting Services: Definitions and Standards*.

The Consulting Services Executive Committee exposes the standards before issuance. When they are issued, the standards are published in the *Journal of Accountancy*. Free-standing copies of the new standard can also be purchased from the Institute. Each new standard carries an effective date, which is based on the committee's assessment of the lead time practitioners require to implement the standard. The standards are codified in the CS section of *Professional Standards*. No interpretations of the standard have been issued.

Statements on Standards for Valuation Services (SSVSs)

When They Apply. Statement on Standards for Valuation Services (SSVS) No. 1, *Valuation of a Business, Business Ownership Interest, Security, or Intangible Asset*, applies to any AICPA member who accepts an engagement to estimate the value of a business, business interest, security, or intangible asset. For the purposes of applying SSVS No. 1, the definition of a *business* includes not-for-profit entities or activities. SSVS No. 1 provides certain exceptions, such as when:

- An employer asks a CPA employee who is not in the practice of public accounting to prepare a valuation for internal use purposes.
- The value of a business or business interest is provided by the client or a third party, and the CPA does not report on the value or perform any procedures to estimate the value.
- The engagement is specifically to determine the economic damages, such as lost profits. However, if the engagement also includes determining the value of a business or business interest, SSVS No. 1 would apply to that engagement.
- The engagement is limited strictly to performing a mechanical computation of value, such as determining the value of 100 shares of a publicly-traded stock based on the most recent selling price.

Practitioners are required by Rule 202 of the *Code of Professional Conduct* to follow the procedure and reporting guidance in SSVS No. 1 when it applies. SSVS No. 1 points out that practitioners engaged to estimate value should be aware of any governmental regulations and other professional standards that apply to the engagement, including the AICPA *Code of Professional Conduct* and the SSCS No. 1, and the extent to which those standards apply to engagements to estimate value.

Form and Content. SSVSs are issued by the AICPA's Consulting Services Executive Committee. The Committee issued the first standard, SSVS No. 1, *Valuation of a Business, Business Ownership Interest, Security, or Intangible Asset*, in June 2007.

The Consulting Services Executive Committee exposed the standard before issuance. When issued, the SSVS was published in the Journal of Accountancy. Free-standing copies of the new standard can also be purchased from the Institute. The standard carries an effective date, which is based on the committee's assessment of the lead time practitioners require to implement the standard.

Statements on Quality Control Standards (SQCS)

Statement on Quality Control Standard No. 7 (SQCS No. 7), *A Firm's System of Quality Control*, establishes standards and provides guidance for a CPA firm's responsibilities for its system of quality control for its accounting and auditing practice. As part of its clarity initiative, the AICPA has redrafted SQCS No. 7. At its July, 2010 meeting, the Auditing Standards Board agreed to ballot on the issuance of a final SQCS No. 7, *A Firm's System of Quality Control (Redrafted)*, that, when effective, will supersede SQCS No. 7 of the same name.

SELF-STUDY QUIZ

Determine the best answer for each question below. Then check your answers against the correct answers in the following section.

7. Which of the following best describes the practitioner's responsibilities under the AICPA's *Code of Professional Conduct*?
 - a. The *Code of Professional Conduct* applies only to services a practitioner provides under the statements on auditing standards (SASs) and statements on standards for attestation engagements (SSAEs).
 - b. The *Code of Professional Conduct* generally applies to all services performed by a practitioner while holding out as a CPA.
 - c. The *Code of Professional Conduct* does not apply to other people in the practitioner's firm.
 - d. When specific types of standards have been established to address specific types of services, the practitioner need not follow the code of conduct.
8. Which of the following best describes the *Conceptual Framework for AICPA Independence Standards*?
 - a. Under the conceptual framework, the practitioner evaluates his or her relationship with a client to determine whether it poses an unacceptable risk to the practitioner's independence.
 - b. Even if identified threats are considered to be at an acceptable level, the practitioner should consider safeguards that could further mitigate such threats.
 - c. If no safeguards are available to eliminate an unacceptable threat or reduce it to an acceptable level, the practitioner would have to obtain a representation letter from the client that acknowledges the risk to the practitioner's independence in the performance of the engagement.
 - d. If neither party to the relationship (that is, the practitioner and client) believe that the practitioner's professional judgment would be impaired when rendering an attest service to the client, there is no risk to the practitioner's independence.
9. Interpretation 101-3 (ET 101), Performance of Non-attest Services, states that **all but which** of the following requirements must be met in order for the performance of nonattest services for an attest client not to impair independence?
 - a. The client must agree to perform certain functions.
 - b. The practitioner cannot perform routine activities, such as providing advice and responding to the client's technical questions.
 - c. The practitioner should not perform management functions or make management decisions for a client.
10. Interpretation 101-3 (ET 101) requires that the understanding between the practitioner and the client must be documented in writing. Which of the following best describes this required understanding?
 - a. The practitioner can document the understanding with the client at any time during the performance of the nonattest services.
 - b. The required understanding should include the objectives of the engagement, the services to be performed, and the responsibilities of both the client and the practitioner, among others.
 - c. Failure to comply with the Interpretation's requirement to document the understanding would result in the impairment of the practitioner's independence.
 - d. The Interpretation specifies how the written understanding is to be documented, so the practitioner has little flexibility in meeting this requirement.

11. In which of the following situations would the CPA have impaired their independence with the client when completing the tax return?
- a. Patricia completed Premier's tax return and filed the return, including a check to pay the taxes due, that was provided to Patricia by the company.
 - b. Steven filed Watson's tax return electronically for the company after management reviewed and signed the final document.
 - c. Kody has had power of attorney for Freeman Buick for the last two years. Kody completes Freeman's tax return, signs it, files the return and then drafts the funds out of Freeman's account to pay the bill.
12. If the practitioner's firm will outsource professional services to third-party service providers, Ethics Ruling 112 under Rule 102, *Integrity and Objectivity*, requires that clients be informed *before confidential client information is shared with the service provider*. In which of the following situations would Ethics Ruling 112 **not** apply?
- a. Use of a specialist.
 - b. Audit of a specified element of the financial statements.
 - c. Software application hosting.
 - d. Using contract employees.
13. Which of the following statements about the issuance of the Statements on Auditing Standards (SASs) is correct?
- a. SASs are issued by the AICPA Attestation Board.
 - b. SASs are published in the CPA Journal when issued.
 - c. SASs are not exposed prior to issuance.
 - d. The effective date of a new SAS is based on the Auditing Standards Board's assessment of the lead time practitioners require to implement the standard.
14. Which of the following best describes the requirements of the Statements on Standards for Accounting and Review Services?
- a. SSARS establish the two services practitioners can apply to unaudited financial statements—compilation and assembly.
 - b. SSARS defines *submitting financial statements* as presenting to a client financial statements that the practitioner has prepared either manually or through the use of computer software.
15. According to SSAE No. 14, *Attestation Hierarchy*, the category labeled *other attestation publications* includes **all but which** of the following types of literature?
- a. Appendixes to the SSAEs.
 - b. Attestation articles in professional journals and the AICPA *CPA Letter*.
 - c. Continuing professional education programs.
 - d. Attestation literature published by state CPA societies, other organizations, and individuals (for example, PPC guides).

16. Which of the following best describes the Statements on Standards for Consulting Services (SSCSs)?
- a. SSCSs apply to engagements in which the practitioner attests to someone else's assertions and develops the final presentation.
 - b. Consulting services to which SSCSs apply include tax return preparation, tax planning or advice, tax representation, personal financial planning, or bookkeeping services.
 - c. SSCSs apply to engagements in which the practitioner develops the findings, conclusions, and recommendations presented.
 - d. SSCSs apply to recommendations or comments prepared as a direct result of an audit service.

SELF-STUDY ANSWERS

This section provides the correct answers to the self-study quiz. If you answered a question incorrectly, reread the appropriate material. **(References are in parentheses.)**

7. Which of the following best describes the practitioner's responsibilities under the AICPA's *Code of Professional Conduct*? **(Page 15)**
- a. The *Code of Professional Conduct* applies only to services a practitioner provides under the statements on auditing standards (SASs) and statements on standards for attestation engagements (SSAEs). [This answer is incorrect. According to the Code at ET 91.02 and 92.11, the code of conduct applies to more services that a practitioner performs.]
 - b. The *Code of Professional Conduct* generally applies to all services performed by a practitioner while holding out as a CPA. [This answer is correct. The code of conduct applies to all services performed by a practitioner while holding out as a CPA, except for very limited exceptions (those called for by specific rules and certain services done by CPAs while practicing in other countries).]**
 - c. The *Code of Professional Conduct* does not apply to other people in the practitioner's firm. [This answer is incorrect. The Code also applies to other people in the practitioner's firm. Thus, a practitioner cannot avoid the rules by having an uncertified member of the firm perform acts the practitioner would be barred from performing.]
 - d. When specific types of standards have been established to address specific types of services, the practitioner need not follow the code of conduct. [This answer is incorrect. When specific types of standards have been established to address specific types of services, the practitioner should also refer to those standards, but the code of conduct still applies. No specific standards conflict with the Code, but they generally are more restrictive and call for specific types of procedures or reports.]
8. Which of the following best describes the *Conceptual Framework for AICPA Independence Standards*? **(Page 16)**
- a. Under the conceptual framework, the practitioner evaluates his or her relationship with a client to determine whether it poses an unacceptable risk to the practitioner's independence. [This answer is correct. According to this standard, risk would be considered unacceptable if the relationship would compromise (or would be perceived as compromising by an informed third party having knowledge of all relevant information) the practitioner's professional judgment when rendering an attest service to the client. Under the risk-based approach, steps are taken to prevent circumstances that threaten independence from compromising the professional judgments required in the performance of an attest engagement.]**
 - b. Even if identified threats are considered to be at an acceptable level, the practitioner should consider safeguards that could further mitigate such threats. [This answer is incorrect. The practitioner is required to consider safeguards only when the identified threats are considered to be at an unacceptable level.]
 - c. If no safeguards are available to eliminate an unacceptable threat or reduce it to an acceptable level, the practitioner would have to obtain a representation letter from the client that acknowledges the risk to the practitioner's independence in the performance of the engagement. [This answer is incorrect. If there are no available safeguards, the practitioner's independence would be considered to be impaired; therefore, the practitioner would not be able to perform an engagement requiring independence.]
 - d. If neither party to the relationship (that is, the practitioner and client) believe that the practitioner's professional judgment would be impaired when rendering an attest service to the client, there is no risk to the practitioner's independence. [This answer is incorrect. The practitioner's independence can also be impaired if an informed third-party having knowledge of all relevant information believes the relationship between the practitioner and the client would compromise the practitioner's professional judgment when rendering an attest service to the client.]

9. Interpretation 101-3 (ET 101), *Performance of Non-attest Services*, states that **all but which** of the following requirements must be met in order for the performance of nonattest services for an attest client not to impair independence? **(Page 18)**
- a. The client must agree to perform certain functions. [This answer is incorrect. Interpretation 101-3 requires that the client agree to perform certain functions that will indicate that the client is able to make an informed judgment about the results of the nonattest services, including evaluating the adequacy and results of the services performed and accepting responsibility for the results of the services, among other things.]
 - b. The practitioner cannot perform routine activities, such as providing advice and responding to the client's technical questions. [This answer is correct. Interpretation 101-3 exempts from its scope certain routine activities, such as providing advice and responding to the client's technical questions as part of the normal client-practitioner relationship. Therefore, a practitioner can perform these services without impairing his or her independence.]**
 - c. The practitioner should not perform management functions or make management decisions for a client. [This answer is incorrect. According to Interpretation 101-3, independence is considered to be impaired if a practitioner (or his or her firm) performs management functions or makes management decisions for a client.]
10. Interpretation 101-3 (ET 101.05) requires that the understanding between the practitioner and the client must be documented in writing. Which of the following best describes this required understanding? **(Page 19)**
- a. The practitioner can document the understanding with the client at any time during the performance of the nonattest services. [This answer is incorrect. To help prevent any type of misunderstanding with the client, the Interpretation states that, *before* performing the nonattest services for an attest client, the practitioner must document in writing his or her understanding with the client.]
 - b. The required understanding should include the objectives of the engagement, the services to be performed, and the responsibilities of both the client and the practitioner, among others. [This statement is correct. In addition to these matters, Interpretation 101-3 states that the required understanding also should include any limitations of the engagement. This is to help prevent any type of misunderstanding with the client.]**
 - c. Failure to comply with the Interpretation's requirement to document the understanding would result in the impairment of the practitioner's independence. [This answer is incorrect. Although failure to obtain the required understanding would impair independence, failure to comply with the Interpretation's requirement to document that understanding would not impair independence. Instead, such failure would be a violation of Rule 202, *Compliance with Standards*, of the AICPA's *Code of Professional Conduct*.]
 - d. The Interpretation specifies how the written understanding is to be documented, so the practitioner has little flexibility in meeting this requirement. [This answer is incorrect. The Interpretation does not specify how the practitioner should document the understanding with the client. Therefore, the practitioner can choose whether to document the understanding in a separate engagement letter, the workpapers, an internal memo, or the engagement letter obtained in conjunction with an attest engagement.]
11. In which of the following situations would the CPA have impaired their independence with the client when completing the tax return? **(Page 20)**
- a. Patricia completed Premier's tax return and filed the return, including a check to pay the taxes due, that was provided to Patricia by the company. [This answer is incorrect. Interpretation 101-3 states that making electronic payments under a taxing authority's specified criteria or remitting a check payable to the taxing authority signed by the client is not considered to be having custody or control of the client's funds and would not impair Patricia's independence.]
 - b. Steven filed Watson's tax return electronically for the company after management reviewed and signed the final document. [This answer is incorrect. Interpretation 101-3 allows preparing and filing an electronic

tax return for a client as long as practitioner does not have custody or control of the client's funds and the individual overseeing the tax services reviews and approves the return and payment and signs the return prior to transmittal.]

- c. **Kody has had power of attorney for Freeman Buick for the last two years. Kody completes Freeman's tax return, signs it, files the return and then drafts the funds out of Freeman's account to pay the bill. [This answer is correct. Signing and filing a tax return on behalf of client management impairs independence unless the practitioner has legal authority to do so and other requirements are met. Kody has a power of attorney for Freeman Buick, so Freeman Buick has authorized Kody to complete this action for them.]**
12. If the practitioner's firm will outsource professional services to third-party service providers, Ethics Ruling 112 under Rule 102, *Integrity and Objectivity*, requires that clients be informed *before confidential client information is shared with the service provider*. In which of the following situations would Ethics Ruling 112 **not** apply? **(Page 21)**
 - a. Use of a specialist. [This answer is incorrect. Ethics Ruling No. 1 would apply if the third-party provider is to be used as a specialist.]
 - b. Audit of a specified element of the financial statements. [This answer is incorrect. Ethics Ruling No. 1 would apply if the third-party provider is to be used to audit a specified element of the financial statements.]
 - c. **Software application hosting. [This answer is correct. The ethics ruling does not require the client to be informed when a third party is used only for administrative support services, such as record storage or software application hosting.]**
 - d. Using contract employees. [This answer is incorrect. Ethics Ruling No. 1 would apply if the third-party provider is to provide contract employees.]
13. Which of the following statements about the issuance of the Statements on Auditing Standards (SASs) is correct? **(Page 22)**
 - a. SASs are issued by the AICPA Attestation Board. [This answer is incorrect. SASs are issued by the AICPA Auditing Standards Board.]
 - b. SASs are published in the CPA Journal when issued. [This answer is incorrect. SASs are published in the Journal of Accountancy when issued by the Auditing Standards Board.]
 - c. SASs are not exposed prior to issuance. [This answer is incorrect. SASs always are exposed prior to issuance to allow practitioners to furnish their comments on the proposed standard to the Auditing Standards Board. Interpretations are not exposed before issuance.]
 - d. **The effective date of a new SAS is based on the Auditing Standards Board's assessment of the lead time practitioners require to implement the standard. [This answer is correct. The ASB determines the effective date of a new SAS by considering how much time practitioners will need to implement the new requirements.]**
14. Which of the following best describes the requirements of the Statements on Standards for Accounting and Review Services? **(Page 23)**
 - a. SSARS establish the two services practitioners can apply to unaudited financial statements—compilation and assembly. [This answer is incorrect. The two services practitioners can apply to the unaudited financial statements of a nonpublic company is a compilation and a review.]
 - b. **SSARS defines *submitting financial statements* as presenting to a client financial statements that the practitioner has prepared either manually or through the use of computer software. [This answer is correct. This definition is important because it is the key to determining whether the practitioner must apply SSARS or whether he or she can perform a plain-paper service.]**

15. According to SSAE No. 14, *Attestation Hierarchy*, the category labeled *other attestation publications* includes **all but which** of the following types of literature? **(Page 26)**
- a. **Appendixes to the SSAEs. [This answer is correct. Appendixes to the SSAEs are not *other attestation publications*; they are all under the category labeled *attestation interpretations*. That category precedes *other attestation publications* in the SSAE hierarchy.]**
 - b. Attestation articles in professional journals and the AICPA *CPA Letter*. [This answer is incorrect. Attestation articles in professional journals and the AICPA *CPA Letter* are included in the category labeled *other attestation publications*, per the SSAE.]
 - c. Continuing professional education programs. [This answer is incorrect. Continuing professional education programs are included in the category labeled *other attestation publications*, per the SSAE.]
 - d. Attestation literature published by state CPA societies, other organizations, and individuals (for example, PPC guides). [This answer is incorrect. Attestation literature published by state CPA societies, other organizations, and individuals are included in the category labeled *other attestation publications*, per the SSAE.]
16. Which of the following best describes the Statements on Standards for Consulting Services (SSCSs)? **(Page 27)**
- a. SSCSs apply to engagements in which the practitioner attests to someone else's assertions and develops the final presentation. [This answer is incorrect. An engagement to attest to someone else's assertions is an attestation engagement. Depending on the type of service to be performed, it is either governed by the Statements on Standards for Attestation Engagements or the Statements on Auditing Standards.]
 - b. Consulting services to which SSCSs apply include tax return preparation, tax planning or advice, tax representation, personal financial planning, or bookkeeping services. [This answer is incorrect. Per the IRS, such services are not included as consulting services. Accordingly, the SSCSs do not apply to them.]
 - c. **SSCSs apply to engagements in which the practitioner develops the findings, conclusions, and recommendations presented. [This answer is correct. An engagement in which the practitioner develops the findings, conclusions and recommendations presented is a consulting engagement; therefore, the SSCSs do apply to them.]**
 - d. SSCSs apply to recommendations or comments prepared as a direct result of an audit service. [This answer is incorrect. Per the Standards For Consulting Services, the SSCSs do not apply to recommendations or comments prepared during an excluded service (such as an audit) as a direct result of that service.]

Current Developments in Standard Setting for Audits of Nonpublic Entities

Standard-setting for Nonpublic Entities. The AICPA's Auditing Standards Board (ASB) oversees the standard-setting process for nonpublic entities.

SAS No. 117. SAS No. 117, *Compliance Audits*, was issued in December 2009 and supersedes SAS No. 74, *Compliance Auditing Considerations in Audits of Governmental Entities and Recipients of Governmental Financial Assistance*. SAS No. 117 applies when an auditor is engaged, or required by law or regulation, to perform a compliance audit of certain governmental and other entities receiving governmental financial assistance, including engagements to report on internal control over compliance with laws, regulations, contracts, and grant requirements. SAS No. 117 is effective for periods ending on or after June 15, 2010, with earlier application permitted.

SAS No. 118 to SAS 120. In February 2010, the AICPA's Auditing Standards Board issued the following Statements on Auditing Standards that amend existing authoritative literature for supplementary information:

- SAS No. 118 (AU 550), *Other Information in Documents Containing Audited Financial Statements*, which supersedes SAS No. 8, *Other Information in Documents Containing Audited Financial Statements*.
- SAS No. 119 (AU 551), *Supplementary Information in Relation to the Financial Statements as a Whole*, which, along with SAS No. 118, supersedes SAS No. 29 *Reporting on Information Accompanying the Basic Financial Statements in Auditor-Submitted Documents*.
- SAS No. 120 (AU 558), *Required Supplementary Information*, which supersedes the portions of SAS Nos. 52 and 98 that address reporting on supplementary information required by GAAP.

These standards define the types of information accompanying the basic financial statements and provide guidance on the auditors' related responsibilities, including reporting responsibilities. In addition, the SASs eliminate the distinction between auditor-submitted documents and client-prepared documents. All three Statements are effective for audits of financial statements for periods beginning on or after December 15, 2010, with early application permitted. This *Guide* has been updated for the new standards.

Clarity Project of the Auditing Standards Board. In response to growing concerns regarding the complexity of auditing standards and to harmonize U.S. generally accepted auditing standards with International Standards on Auditing (ISAs) issued by the International Auditing and Assurance Standards Board (IAASB), the Auditing Standards Board began a large-scale project known as the Clarity Project, to revise all existing auditing standards and to design a format under which all new standards will be issued. In March 2007, the ASB issued a discussion paper, *Improving the Clarity of Auditing Standards*, similar to a clarity project undertaken by the IAASB. The Discussion Paper asked for comment about potential changes related to the structure, format, and style of auditing standards, including the following:

- Establishing objectives for each of the standards that provide a conceptual framework for the application of professional judgment and the obligation related to the objective.
- Making structural and drafting improvements to make the standards easier to read and understand.
- Including special considerations in the audits of public sector entities and small entities in the explanatory material of a Statement on Auditing Standard.
- Establishing a glossary of terms that would be presented in a separate section of the Codification of Statements on Auditing Standards.

In response to comments received on the discussion paper and subsequent discussions, the ASB has decided on drafting conventions. Accordingly, the redrafted standards will include the following sections:

- Introduction (scope and effective date)
- Objective

- Definitions
- Requirements
- Application and other explanatory material

Generally, items that are *must* statements in existing standards will become objectives in the redrafted standards. Items that are *should* statements will become requirements. All of the guidance and suggested procedures from existing standards that assist in meeting the requirements will be included in the application and other explanatory material. Explanatory material will tie directly to the requirements; that is, for each requirement, there will be related explanatory material. The explanatory material will also include an exhibit comparing requirements of the SAS to the corresponding international requirements.

At the date of this course, the Auditing Standards Board has issued a number of final standards and exposure drafts of proposed standards under the clarity and convergence project. Exhibit 1-2 provides a current listing of all final and proposed standards (including those that have been voted to ballot for final issuance). The ASB is working towards completing the project in 2011.

Exhibit 1-2

List of Final and Proposed Clarified Auditing Standards Issued to Date^a

Clarified Standard	Existing Standards to Be Superseded	
Title	AU	Title
Final Clarified Standards^b		
Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance With GAAS	110	Responsibilities and Functions of the Independent Auditor
	120	Defining Professional Requirements in Statements on Auditing Standards
	150	Generally Accepted Auditing Standards
	201	Nature of the General Standards
	201	Training and Proficiency of the Independent Auditor
	220	Independence
	230	Due Professional Care in the Performance of Work
Quality Control for Engagements Conducted in Accordance with Generally Accepted Auditing Standards	161	The Relationship of Generally Accepted Auditing Standards to Quality Control Standards
Planning an Audit	311	Planning and Supervision
Materiality in Planning and Performing an Audit	312	Audit Risk and Materiality in Conducting an Audit
Evaluation of Misstatements Identified During an Audit		
Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement	314	Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement
Initial Audit Engagements, Including Reaudits—Opening Balances	315	Communications Between Predecessor and Successor Auditors
Terms of Engagement		

Clarified Standard	Existing Standards to Be Superseded	
Title	AU	Title
Consideration of Fraud in an Audit of Financial Statements	316	Consideration of Fraud in a Financial Statement Audit
Consideration of Laws and Regulations in an Audit of Financial Statements	317	Illegal Acts by Clients
Performing Audit Procedures in Response to Assessed Risks and Evaluating the Audit Evidence Obtained	318	Performing Audit Procedures in Response to Assessed Risks and Evaluating the Audit Evidence Obtained
Audit Considerations Relating to an Entity Using a Service Organization	324	Service Organizations
SSAE, Reporting on Controls at a Service Organization ^c		
Communicating Internal Control Related Matters Identified in an Audit	325	Communicating Internal Control Related Matters Identified in an Audit
Audit Evidence	326	Audit Evidence
Analytical Procedures	329	Analytical Procedures
Auditing Accounting Estimates, Including Fair Value Accounting Measurements and Related Disclosures	328	Auditing Fair Value Measurements and Disclosures
	342	Auditing Accounting Estimates
External Confirmations	330	The Confirmation Process
Written Representations	333	Management Representations
Related Parties	334	Related Parties
Using the Work of an Auditor's Specialist	336	Using the Work of a Specialist
Audit Sampling	350	Audit Sampling
Audit Documentation	339	Audit Documentation
The Auditor's Communication With Those Charged With Governance	380	The Auditor's Communication With Those Charged With Governance
Consideration of Omitted Procedures After the Report Date	390	Consideration of Omitted Procedures After the Report Date
Forming an Opinion and Reporting on Financial Statements	410	Adherence to Generally Accepted Accounting Principles
	508 ^d	Reports on Audited Financial Statements
Evaluating Consistency of Financial Statements	420	Consistency of Application of Generally Accepted Accounting Principles
Modifications to the Opinion in the Independent Auditor's Report	431	Adequacy of Disclosure in Financial Statements
	508 ^d	Reports on Audited Financial Statements
Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report	508 ^d	Reports on Audited Financial Statements
Subsequent Events and Subsequently Discovered Facts	508 ^d	Reports on Audited Financial Statements
	530	Date of the Auditor's Report
	560	Subsequent Events

Clarified Standard	Existing Standards to Be Superseded	
Title	AU	Title
	561	Subsequent Discovery of Facts Existing at the Date of the Auditor's Report
Audits of Group Financial Statements (Including the Work of Component Auditors)	543	Part of Audit Performed by Other Independent Auditors
Special Considerations—Audits of Financial Statements Prepared in Accordance with Special Purpose Frameworks	544	Lack of Conformity With Generally Accepted Accounting Principles
	623 ^d	Special Reports
Other Information in Documents Containing Audited Financial Statements ^e	550	Other Information in Documents Containing Audited Financial Statements
Other Information in Relation to the Financial Statements as a Whole ^e	551	Reporting on Information Accompanying the Basic Financial Statements in Auditor-Submitted Documents
Engagements to Report on Summary Financial Statements	552	Reporting on Condensed Financial Statements and Selected Financial Data
Required Supplementary Information ^e	558	Required Supplementary Information
Special Considerations—Audits of Single Financial Statements and Specific Elements, Accounts, or Items of a Financial Statement	623 ^d	Special Reports
Reports on Application of Requirements of an Applicable Financial Reporting Framework	625	Reports on the Application of Accounting Principles
Exposure Drafts		
Audit Evidence—Specific Considerations of Selected Items	331	Inventories
	332	Auditing Derivative Instruments, Hedging Activities, and Investments in Securities
	337	Inquiry of a Client's Lawyer Concerning Litigation, Claims, and Assessments
	901	Public Warehouses—Controls and Auditing Procedures for Goods Held
Reporting on Financial Statements Prepared in Accordance With a Financial Reporting Framework Generally Accepted in Another Country	534	Reporting on Financial Statements Prepared for Use in Other Countries
Reporting on Compliance With Aspects of Contractual Agreements or Regulatory Requirements in Connection With Audited Financial Statements	623 ^d	Special Reports
Letters for Underwriters and Certain Other Requesting Parties	634	Letters for Underwriters
Filings with the U.S. Securities and Exchange Commission under the Securities Act of 1933	711	Filings under Federal Securities Statutes
Interim Financial Information	722	Interim Financial Information

Notes:

- ^a The Auditing Standards Board also has agreed to ballot on the issuance of a final Statement on Quality Control Standards (SQCS), *A Firm's System of Quality Control (Redrafted)*, that will supersede SQCS No. 7 of the same name.
- ^b This section includes both final issued standards and those voted to ballot for issuance as final standards. As of the date of this course, many of the final standards had not actually been issued.
- ^c SSAE No. 16 is effective for service auditors' reports for periods ending on or after June 15, 2011, with earlier implementation permitted.
- ^d The clarified standard supersedes certain paragraphs of the AU section.
- ^e To address practice issues, these three clarified standards have been issued and assigned a specific SAS number (SAS Nos. 118–120). They also have an earlier effective date than the remainder of the clarified SASs. The effective date is for periods beginning on or after December 15, 2010, with early implementation permitted.

* * *

When all of the standards have been clarified and converged and are in final form, they will be issued as one SAS that will be codified in AU section format. The effective date is expected to be for audits of financial statements for periods ending on or after December 15, 2012. When the new clarified SAS becomes effective, SASs issued prior to SAS No. 117 will be superseded. Early adoption of the clarified standards is not permitted unless indicated otherwise. (However, an auditor can implement aspects of the clarified standards if he or she complies with existing standards.) Auditors can monitor the status of the exposure drafts at www.aicpa.org.

Current Developments in Standard Setting for Compilation and Reviews for Nonpublic Entities

The basic task of the Accounting and Review Services Committee (ARSC) is to keep the existing SSARS up to date as changes are made in other authoritative literature and to make sure current standards coincide with recent developments in technology and regulation. From time to time, ARSC also will issue interpretations, develop technical practice aids, or issue other guidance to address recurring practice problems relating to existing SSARS. The following paragraphs provide a brief discussion on some of the recent ARSC developments.

Issuance of TIS 9150.26, *The Accountant's Responsibilities for Subsequent Events in Compilation and Review Engagements*. This Technical Practice Aid (TPA) clarifies the accountant's responsibilities for subsequent events in both compilation engagements and review engagements.

Issuance of TIS 9150.27, *The Accountant's Reporting Responsibility With Respect to Subsequent Discovery of Facts Existing at the Date of the Report*. This Technical Practice Aid clarifies the use of the term *where applicable* as it applies to the accountant's reporting responsibility with respect to subsequent discovery of facts existing at the date of the report.

Issuance of SSARS No. 19, *Compilation and Review Engagements*. In December 2009, ARSC issued Statement on Standards for Accounting and Review Services No. 19, *Compilation and Review Engagements*. SSARS No. 19 is the most significant change to the compilation and review standards since their inception in 1978. It supersedes AR 20, AR 50, and AR 100 and is generally effective for compilations and reviews of financial statements for periods ending on or after December 15, 2010. Early implementation is permitted only for the optional disclosure in the compilation report of the reasons for an independence impairment. This course has been updated throughout to incorporate the requirements of SSARS No. 19.

Recent ARSC Activities. In June 2010, the ARSC issued exposure draft SSAE, *Reporting on Compiled Prospective Financial Statements When the Accountant's Independence is Impaired*. The proposed SSAE would remove the prohibition against disclosing the reasons for an independence impairment in a compilation report on prospective

financial statements, just as SSARS No. 19 removed this prohibition in a compilation report on historical financial statements. The proposed amendment would be effective for compilations of prospective financial statements for periods ending on or after December 15, 2010, with early implementation permitted.

In July 2010, the ARSC issued an exposure draft of a SSARS that would amend SSARS No. 19 (AR 90.01) to conform the guidance regarding when SSARSs apply in reviews of interim financial statements to the guidance in SAS No. 116, as clarified. AR 90.01 currently states that SSARS are not applicable when the accountant audited the entity's latest annual financial statements and expects to be engaged to audit the current year financial statements. The proposed amendment would revise the SSARS such that the SSARS would not be applicable when the auditor audited the entity's latest annual financial statements and the appointment of an auditor to audit the current year financial statements is not effective prior to the period covered by the review. This change would allow for an appropriate transition between the predecessor auditor and the auditor of the current year financial statements. The amendment is expected to be effective for reviews of financial statements for periods beginning after December 15, 2011, and coincides with the effective date of the SAS No. 116 amendment. Early application would be permitted.

Other items on the agenda for ARSC to consider include:

- Proposed SSARS, *The Accountant's Responsibility for Unaudited Financial Statements That Have Not Been Compiled or Reviewed*.
- Proposed SSARS, *Reporting on Financial Statements Prepared in Accordance With a Financial Reporting Framework Generally Accepted in Another Country*.
- Clarify SSARS in the same format as the SASs are being clarified.
- SSARS No. 1 Interpretations.

Current Developments in Accounting Standard Setting

In June 2009, the FASB issued FASB ASC 105-10 (formerly SFAS No. 168, *The Hierarchy of Generally Accepted Accounting Principles*, which replaces SFAS No. 162 and authorizes the *FASB Accounting Standards Codification*[™] as the single source of authoritative generally accepted accounting principles to be applied by non-SEC companies. (All other accounting literature not included in the Codification is nonauthoritative.) The authoritative version of the Codification, which was officially released on July 1, 2009, is effective for annual and interim periods ending after September 15, 2009.

All new standards the FASB issues after the effective date of the codification will be issued through an accounting standards update (ASU). ASUs will be sequentially numbered by year. All authoritative GAAP issued by the FASB will apply this format, regardless of how such guidance was previously issued (for example, Statement of Financial Accounting Standard, FASB Staff Position, or EITF Consensus).

Current Developments in Professional Ethics Standards

The AICPA's Professional Ethics Executive Committee (PEEC) issued new guidance that revises Interpretation 101-1, under Rule 101, *Independence*, and is effective on June 1, 2011, with earlier application permitted:

- "Application of the Independence Rules to Covered Members Formerly Employed by a Client or Otherwise Associated With a Client" and "Application of the Independence Rules to a Covered Member's Immediate Family" (ET 101.02)

In addition, the following have also been issued and were effective May 31, 2010:

- Ethics Ruling No. 107, "Participation in Employee Benefit Plan Sponsored by Client." (ET 191.214-.215)
- "Retirement, Savings, Compensation, or Similar Plans" of Interpretation No. 101-15, "Financial Relationships," under Rule 101 (ET 101.17).

SELF-STUDY QUIZ

Determine the best answer for each question below. Then check your answers against the correct answers in the following section.

17. Sean has been engaged to perform a compliance audit on Kids Care Organization (KCO). KCO is required to obtain an audit on their internal control since they received governmental financial assistance. Which of the following authoritative literature would Sean find guidance on completing his engagement?
 - a. SAS No. 117.
 - b. SAS No. 118.
 - c. SAS No. 119.
 - d. SAS No. 120.
18. Based on the clarity project of the Auditing Standard Board (ASB), if an item is stated as a *must* statement in the current standards, it will become a(n) _____ in the redrafted standards.
 - a. Requirements.
 - b. Explanatory material.
 - c. Objective.

SELF-STUDY ANSWERS

This section provides the correct answers to the self-study quiz. If you answered a question incorrectly, reread the appropriate material. **(References are in parentheses.)**

17. Sean has been engaged to perform a compliance audit on Kids Care Organization (KCO). KCO is required to obtain an audit on their internal control since they received governmental financial assistance. Which of the following authoritative literature would Sean find guidance on completing his engagement? **(Page 36)**
 - a. **SAS No. 117.** [This answer is correct. SAS No. 117, *Compliance Audits*, was issued in December 2009 and supersedes SAS No. 74. It applies when an auditor is engaged, or required by law or regulations, to perform a compliance audit of certain governmental and other entities receiving governmental financial assistance, including engagements to report on internal control over compliance with laws, regulations, contracts and grant requirements. SAS No. 117 is effective for periods ending on or after June 15, 2010.]
 - b. SAS No. 118. [This answer is incorrect. SAS No. 118, *Other Information in Documents Containing Audited Financial Statements*, superseded SAS No. 8 and was issued in February, 2010. Auditors would use this literature for guidance on the information accompanying the basic financial statements.]
 - c. SAS No. 119. [This answer is incorrect. SAS No. 119, *Supplementary Information in Relation to the Financial Statement as a Whole*, would provide Sean great information on the auditors' related responsibilities for the information accompanying the basic financial statements, but would not help with the compliance audit that he is completing for KCO.]
 - d. SAS No. 120. [This answer is incorrect. SAS No. 120, *Required Supplementary Information*, defines the types of information accompanying the basic financial statements and would provide guidance to Sean on the auditors' related responsibilities, including reporting responsibilities. In addition. The SAS eliminates the distinction between auditor-submitted documents and client-prepared documents.]
18. Based on the clarity project of the Auditing Standard Board (ASB), if an item is stated as a *must* statement in the current standards, it will become a(n) _____ in the redrafted standards. **(Page 37)**
 - a. Requirements. [This answer is incorrect. Items that are *should* statements will become requirements in the redrafted standards, according to the ASB clarity project.]
 - b. Explanatory material. [This answer is incorrect. All of the guidance and suggested procedures from existing standards that assist in meeting the requirements will be included in the application and other explanatory material. Explanatory material will tie directly to the requirements; that is, for each requirement, there will be related explanatory material.]
 - c. **Objective.** [This answer is correct. The ASB has decided that generally, items that are *must* statements in the existing standards will be objectives in the redrafted standards based on the clarity project.]

EXAMINATION FOR CPE CREDIT**Lesson 1 (NTETG101)**

Determine the best answer for each question below. Then mark your answer choice on the Examination for CPE Credit Answer Sheet located in the back of this workbook or by logging onto the Online Grading System.

1. Generally, when should nontraditional engagements occur?
 - a. When a client has a specific goal in mind.
 - b. When a client is in need of standard audit services.
 - c. When a client is in need if a special type of service.
 - d. When a client is in need of services other than agreed-upon procedures.
2. Which of the following statements about an agreed-upon procedures engagement is **not** correct?
 - a. An agreed-upon procedures engagement generally is less expensive than standardized services.
 - b. In an agreed-upon procedures engagement, the practitioner's report provides overall assurance on the subject matter.
 - c. Agreed-upon procedures engagements often can reduce litigation risk.
 - d. The value of an agreed-upon procedures engagement is that it enhances the credibility of the information to which the procedures are applied.
3. Construction costs statements, accounts receivable schedules, and PP&E summaries are ALL examples of which of the following?
 - a. Performance measurement services.
 - b. Specific financial statement elements.
 - c. Pro forma information.
 - d. Independence considerations.
4. The application of agreed-upon procedures concerning the internal control's effectiveness is considered which of the following types of engagements?
 - a. Lease agreement.
 - b. Contract.
 - c. Attestation.
 - d. Compliance.

5. Match the following engagements with the appropriate service(s) performed.

- | | |
|----------------------------|--|
| 1. Pro forma | a. Enrollment statistics |
| 2. Internal control | b. Define strategy |
| 3. Acquisition assistance | c. Recast of historical information |
| 4. Performance measurement | d. Due diligence |
| 5. Attestation procedures | e. Communication of management letters |

- a. 1,c; 2,e,3,d; 4,b; 5,a.
- b. 2,a; 1,d; 4,c; 3,e; 5,b.
- c. 4,e; 5,d; 1,c; 2,a; 3,b.
- d. 5,a; 4,b; 3,d; 2,e; 1,d.

6. Which of the following provides the structure for the Code's specific rules?

- a. Rules of conduct.
- b. Interpretations.
- c. Principles of professional conduct.
- d. Rulings.

7. Safeguards are controls that are implemented to decrease or eliminate threats to independence. When independence threats are at an unacceptable level, which of the following should be documented when safeguards are applied?

- a. The created regulations.
- b. The safeguards not used by the client.
- c. The identified threats.
- d. Do not select this answer choice.

8. In regards to Interpretation 101-3, which of the following statements is correct?

- a. Practitioners who are initially engaged to only provide nonattest services can also perform attest services by structuring the engagement so performance of the nonattest services will not impair independence.
- b. Practitioners are required to document the understanding with the client regarding the nonattest services performance other than in the engagement letter.
- c. Generally, the documentation requirement applies to nonattest services performed prior to the client becoming an attest client.
- d. The Interpretation cautions against a practitioner's representation of a client in administrative proceeding before a taxing authority will impair independence.

9. Which of the following statements regarding Interpretation 101-3 is **not** correct?
- a. Providing expert witness testimony to a large group of plaintiffs will impair independence.
 - b. Certain actuarial services generally impair independence.
 - c. Independence is impaired when a practitioner provides litigation services where he or she is an arbitrator in a matter involving a client.
 - d. Performance of internal audit assistance does not always impair independence.
10. Which of the following types of standards apply to audits of financial statements of nonpublic companies?
- a. Statements on Standards for Accounting and Review Services.
 - b. Statements on Standards for Attestation Engagements.
 - c. Statements on Auditing Standards.
 - d. Statements on Standards for Consulting Services.
11. Which of the following statements best describes auditing interpretations?
- a. Like the statements on auditing standards, auditing interpretations also are issued by the Accounting Services Committee.
 - b. Auditing interpretations explain sections of standards that are ambiguous or the standards' application in situations not envisioned when they were originally issued.
 - c. Auditing interpretations are enforceable under the AICPA's *Code of Professional Conduct*.
 - d. Auditing interpretations are exposed prior to issuance.
12. Which of the following statements about the Statements on Standards for Attestation Engagements (SSAEs) is correct?
- a. When the practitioner is engaged to issue or does issue an examination, review, or agreed-upon procedures report on subject matter that is the responsibility of another party, SSAEs will apply.
 - b. The SSAEs provide for three levels of service: examination, review, and compilation.
 - c. Practitioners are required by Rule 101 of the *Code of Professional Conduct* to follow the procedure and reporting guidance in SSAEs when they apply.
 - d. SSAEs may be issued by any of three AICPA senior technical committees—the Auditing Standards Board, Accounting and Review Services Committee, or the Peer Review Executive Committee.
13. SSAE No. 14, *SSAE Hierarchy*, identifies the body of attest literature and clarifies the authority of attest publications issued by the AICPA and others. According to SSAE No. 14, which of the following properly describes the hierarchy of SSAE literature?
- a. Attestation interpretations, attestation standards, other attestation publications.
 - b. Other attestation publications, attestation interpretations, attestation standards.
 - c. Attestation standards, attestation interpretations, other attestation publications.
 - d. Attestation standards and other attestation publications, which include attestation interpretations.

14. What is the reason that the Accounting Standards Board (ASB) has decided to tackle the clarity project?
- a. To synchronize the U.S. auditing standards with the international auditing standards.
 - b. To issue new standards to make clear all the ethical requirements for auditors.
 - c. To explain the current standards in a more readable and understanding process.
 - d. To include all the current auditing standards in the codification process.
15. Which of the following is **not** a section to be included in the redrafted auditing standards by the ASB?
- a. Definitions.
 - b. Special Considerations.
 - c. Other explanatory materials.
 - d. Objective.
16. As part of the clarity project, which of the following existing standards will be included in the clarified standard, "Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with GAAS"?
- a. Planning and supervision.
 - b. Illegal acts by clients.
 - c. Training and proficiency of the independent auditor.
 - d. Audit risk and materiality in conducting an audit.

Lesson 2: Overview of Agreed-upon Procedures Engagements

INTRODUCTION

This lesson provides an overview of agreed-upon procedures engagements, including a discussion of which standards apply to which types of engagements. In addition, the lesson describes the attestation standards a practitioner is required to follow when performing an agreed-upon procedures engagement under the attestation standards. Further, this lesson defines all concepts relevant to an understanding of an agreed-upon procedures engagement and describes factors to consider when deciding whether to perform one. Finally, this lesson describes factors to consider when deciding whether to accept a particular agreed-upon procedures engagement.

Learning Objectives:

Completion of this lesson will enable you to:

- Identify the standards that apply to agreed-upon procedures engagements.

An agreed-upon procedures engagement is one in which a practitioner is engaged by a client to perform specific procedures and report findings. The practitioner does not perform an examination or provide an opinion. Rather, the practitioner reports only procedures and findings.

This lesson provides guidance on applying agreed-upon procedures to—

- Financial information.
- Nonfinancial information.

Agreed-upon Procedures Engagements

Definition. An agreed-upon procedures engagement is one in which a practitioner is engaged by a client to perform specific procedures and report findings. The practitioner does not perform an audit or provide an opinion relating to the subject matter or assertion about the subject matter. Rather, the practitioner performs only those procedures that have been agreed upon and reports findings.

Purpose. Agreed-upon procedures engagements generally arise when clients need the practitioner's involvement, but do not want a compilation, review, or audit. A problem often encountered in these types of engagements is that clients do not necessarily want an agreed-upon procedures engagement. Instead, their desires are less precisely defined. Clients may want the practitioner to *verify* the information or *check it out and let us know if there are any problems we should know about*. The practitioner is then faced with the challenge of crafting an engagement that both satisfies the client's desires and does not expose the practitioner to undue risk. One way of satisfying the somewhat undefined desires of clients is to perform agreed-upon procedures and report the results of those procedures as findings.

Agreed-upon procedures engagements also arise when a client provides information to a third party, and the third party requires involvement by the practitioner to enhance the credibility of the information. Examples of such third parties include banks, regulatory agencies, prospective investors, and prospective purchasers. They are referred to in this course as *specified parties* of the practitioner's report. In many cases, the client is also a specified party. The person or entity providing the information is referred to as the *responsible party*.

At the onset of an agreed-upon procedures engagement, the practitioner and the specified parties agree upon the procedures that the parties believe are appropriate to meet their needs. Because parties' needs vary significantly from one engagement to another, the specific nature of each agreed-upon procedures engagement varies as well. Consequently, the parties assume responsibility for the sufficiency of the requested procedures since they best understand their own needs.

Example. An agreed-upon procedures engagement might occur, for example, if a potential investor (the specified party) is interested in assessing the collectibility of a potential investee's (the responsible party's) accounts

receivable. In that case, the potential investor might request the practitioner to perform procedures to determine whether the investee's accounts receivable agings are accurate. Such procedures might include selecting an agreed-upon number of accounts receivable balances and testing the agings based on supporting invoices. In such an engagement, the practitioner provides no assurance about the collectibility of the investee's accounts receivable, but simply reports the results of his or her findings (that is, whether the selected accounts receivable balances are properly aged based on the supporting invoices).

AUTHORITATIVE LITERATURE

SSAE No. 10

Agreed-upon procedures engagements are governed by Statement on Standards for Attestation Engagements No. 10, *Attestation Standards: Revision and Recodification*, as amended by SSAE No. 11, *Attest Documentation*, and SSAE No. 12, *Amendment to Statement on Standards for Attestation Engagements No. 10, Attestation Standards: Revision and Recodification*. The specific guidance for agreed-upon procedures engagements is contained in the following sections of SSAE No. 10:

- AT 101, *Attestation Standards*
- AT 201, *Agreed-Upon Procedures Engagements*

Practitioners should also follow the relevant guidance in SSAE No. 13, *Defining Professional Requirements in Statements on Standards for Attestation Engagements*, and SSAE No. 14, *SSAE Hierarchy*.

AT 101, *Attestation Standards*

AT 101, *Attestation Standards*, is the umbrella standard that governs all types of attestation engagements, of which there are three: examinations, reviews, and agreed-upon procedures engagements.

AT 201, *Agreed-upon Procedures Engagements*

AT 101 states that the general, fieldwork, and reporting standards for attestation engagements apply to agreed-upon procedures engagements. However, it then directs the practitioner to the specific guidance on performing agreed-upon procedures engagements contained in AT 201, *Agreed-Upon Procedures Engagements*. Thus, the remainder of this lesson provides guidance on performing agreed-upon procedures engagements under AT 201.

What It Covers. AT 201 provides guidance on applying agreed-upon procedures in the following areas:

- The nature of an agreed-upon procedures engagement and the applicable attestation standards.
- Conditions required for performing an agreed-upon procedures engagement.
- The nature, timing, and extent of procedures performed in an agreed-upon procedures engagement.
- The involvement of internal auditors and others in an agreed-upon procedures engagement.
- The responsibilities of the practitioner and the responsible party.
- The responsibilities of the specified parties of an agreed-upon procedures report.
- Reporting in an agreed-upon procedures engagement.

Other sections of SSAE No. 10, however, discuss agreed-upon procedures in specific contexts:

- AT 301, *Financial Forecasts and Projections*, discusses applying agreed-upon procedures to prospective financial statements.

- AT 601, *Compliance Attestation*, discusses reports on agreed-upon procedures with respect to compliance with laws, regulations, or contracts.

The following AICPA statements of position (SOP) discuss applying agreed-upon procedures in specific regulatory circumstances:

- SOP 01-3, *Performing Agreed-upon Procedures Engagements That Address Internal Control Over Derivative Transactions as Required by the New York State Insurance Law*.
- SOP 02-1, *Performing Agreed-upon Procedures Engagements That Address Annual Claims Prompt Payment Reports as Required by the New Jersey Administrative Code*.
- SOP 07-2, *Attestation Engagements That Address Specified Compliance Control Objectives and Related Controls at Entities That Provide Services to Investment Companies, Investment Advisers, or Other Service Providers*.
- SOP 09-1, *Performing Agreed-Upon Procedures Engagement That Address the Completeness, Accuracy, or Consistency of XBRL-Tagged Data*.

Engagements Performed under Other Authoritative Literature

The following agreed-upon procedures engagements are subject to other literature and should not be performed under the attestation standards:

- Engagements to report in accordance with SAS No. 117 (AU 801), *Compliance Audits*. (However, a practitioner may agree to apply agreed-upon procedures to specified elements of a financial statement for the benefit of a government body. In these situations, the practitioner would follow the guidance in this lesson as well as any applicable governmental requirements.)
- Engagements in which a service auditor includes in his or her report a separate reference to substantive procedures applied to user transactions or assets at the service organization as discussed in Paragraph 62 of SAS No. 70 (AU 324), *Reports on the Processing of Transactions by Service Organizations*. (If a service auditor issues a separate report on the results of such procedures, it is subject to the requirements of AT 201 discussed in this lesson.)
- Engagements performed under SAS No. 72 (AU 634), *Letters for Underwriters and Certain Other Requesting Parties*.
- Engagements in which the practitioner reports on specified compliance requirements based solely on an audit of financial statements, as addressed in SAS No. 62 (AU 623), *Special Reports*.

Applicability of General, Fieldwork, and Reporting Standards

As previously discussed, a practitioner applying agreed-upon procedures should follow the general, fieldwork, and reporting standards for attestation engagements. Those standards are listed in the following discussion, along with references to interpretive guidance for applying them in an agreed-upon procedures engagement:

a. General Standards

- (1) The practitioner must have adequate technical training and proficiency to perform the attestation engagement.
- (2) The practitioner must have adequate knowledge of the subject matter.
- (3) The practitioner must have reason to believe that the subject matter is capable of evaluation against criteria that are suitable and available to users.

- (4) The practitioner must maintain independence in mental attitude in all matters relating to the engagement.
- (5) The practitioner must exercise due professional care in the planning and performance of the engagement and the preparation of the report.

b. Standards of Fieldwork

- (1) The practitioner must adequately plan the work and must properly supervise any assistants.
- (2) The practitioner must obtain sufficient evidence to provide a reasonable basis for the conclusion that is expressed in the report.

c. Standards of Reporting

- (1) The practitioner must identify the subject matter or the assertion being reported on and state the character of the engagement in the report.
- (2) 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.
- (3) 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.
- (4) 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:
 - (a) 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.
 - (b) When the criteria used to evaluate the subject matter are available only to specified parties.
 - (c) When reporting on subject matter and a written assertion has not been provided by the responsible party.
 - (d) When the report is on an attestation engagement to apply agreed-upon procedures of the subject matter.

Even though the practitioner is not *required* to consider the guidance in auditing standards, that guidance may sometimes be helpful.

Definitions and Terms

AT 201 provides guidance to the practitioner on applying agreed-upon procedures to any type of information. Applying agreed-upon procedures generally involves performing specific procedures on *subject matter* or on a related *assertion*. Those terms, as well as others used in SSAE No. 10, are discussed below.

What Constitutes a Written Assertion? According to AT 201, an assertion is any declaration or set of related declarations about whether the subject matter is based on or in conformity with the criteria selected.

Is a Written Assertion Required? According to AT 201, a written assertion generally is not required in an agreed-upon procedures engagement unless specifically required by another attest standard that applies to the particular type of agreed upon procedures engagement being performed. (For instance, AT 601, *Compliance Attestation*, requires practitioners to obtain a written assertion about compliance from the responsible party in an agreed-upon procedures engagement.)

What Is the Subject Matter? All engagements are made about something; that is the subject matter. The subject matter is what the practitioner applies procedures to. In an audit of financial statements, the subject matter is the financial results portrayed in the financial statements. In an examination regarding the effectiveness of a company's internal control over financial reporting, the subject matter is the internal control over financial reporting.

The subject matter may or may not be related to the financial statements, and it may or may not be numeric. Some of the forms the subject matter might take include:

- Historical or prospective performance or condition (for example, historical or prospective financial information, performance measurements, accounting records, or backlog data).
- Schedules of financial or nonfinancial information (for example, a schedule of accounts receivable, a schedule of sales in units, or a list of invoice numbers and dates).
- Physical characteristics (for example, narrative descriptions, square footage of facilities).
- Historical events (for example, price of a market basket of goods on a certain date).
- Analyses (for example, break-even analyses).
- Systems and processes (for example, internal control).
- Behavior (for example, corporate governance, compliance with laws and regulations, and human resource practices).

Practitioners might be asked to perform agreed-upon procedures on a financial statement element, an entity's compliance with certain laws, an entity's rate of return on invested assets, or the quantity of gallons of wastewater processed. The subject matter might or might not be reduced to writing and, if it is, it might or might not accompany the practitioner's report.

What Are the Criteria? The subject matter must have an objective parameter by which it is measured—this basis is called the criteria. In addition, the subject matter must be capable of reasonably consistent estimation or measurement against the criteria. For example, the financial statements represent the subject matter of financial results; GAAP are the criteria against which they are measured. In an attestation engagement, the client asserts that the subject matter is in conformity with criteria. The criteria might or might not be formally established, like GAAP. In an agreed-upon procedures engagement, the criteria against which the subject matter is measured merely have to be agreed upon between the practitioner and the specified parties. That is, practitioners can evaluate the subject matter against any criteria that the specified parties find useful for their purposes. (Of course, the report has to be restricted to the use of the specified parties.) Subject matter, criteria, and procedures are discussed further later in this course.

Who Is the Responsible Party? The responsible party is someone, other than the practitioner, who takes responsibility for the subject matter. Generally, the responsible party is the management of the entity whose subject matter is being measured. The responsible party is generally a group—akin to management—rather than an individual. The responsible party need not be the practitioner's client.

Who Are the Specified Parties? In an agreed-upon procedures engagement, the specified parties assume responsibility for the sufficiency of the procedures for their purposes. The specified parties will normally include the client, the responsible party (if the responsible party is not the client), and other specified users who assume responsibility for the sufficiency of the procedures. Responsibilities of the specified parties are discussed later in this course.

DECIDING BETWEEN AN AGREED-UPON PROCEDURES ENGAGEMENT AND A CONSULTING ENGAGEMENT

When a practitioner is requested by a client to perform procedures, the practitioner may be unsure of whether the services should be structured as agreed-upon procedures or consulting services. Since professional standards for agreed-upon procedures and consulting engagements differ significantly, it is important that the engagement be structured appropriately and performed under the applicable standards. Because most clients will not be familiar with the types of services available, or the differences between those services, the practitioner ordinarily must explain the available services and assist the client in determining the type of service that best suits the client's needs.

It is generally believed an agreed-upon procedures engagement is preferable because it offers more protection for the practitioner. As discussed throughout this course, agreed-upon procedures engagements must meet specific performance and reporting requirements, whereas consulting engagements are subject to less stringent requirements. Agreed-upon procedures reports are normally very precise in nature, reporting results in the form of procedures and findings. Because there are no specific reporting standards for consulting reports, however, those reports are often more subjective and may describe practitioners' procedures in a less precise manner. Should litigation later arise, practitioners may be in a better defensive position if they have performed an agreed-upon procedures engagement.

On the other hand, practitioners will sometimes find consulting engagements to be more flexible than agreed-upon procedures engagements. Because of this, consulting engagements may, in some cases, better fit a client's needs and represent a more practical alternative. Examples include due diligence assistance services and certain services performed in conjunction with eldercare engagements.

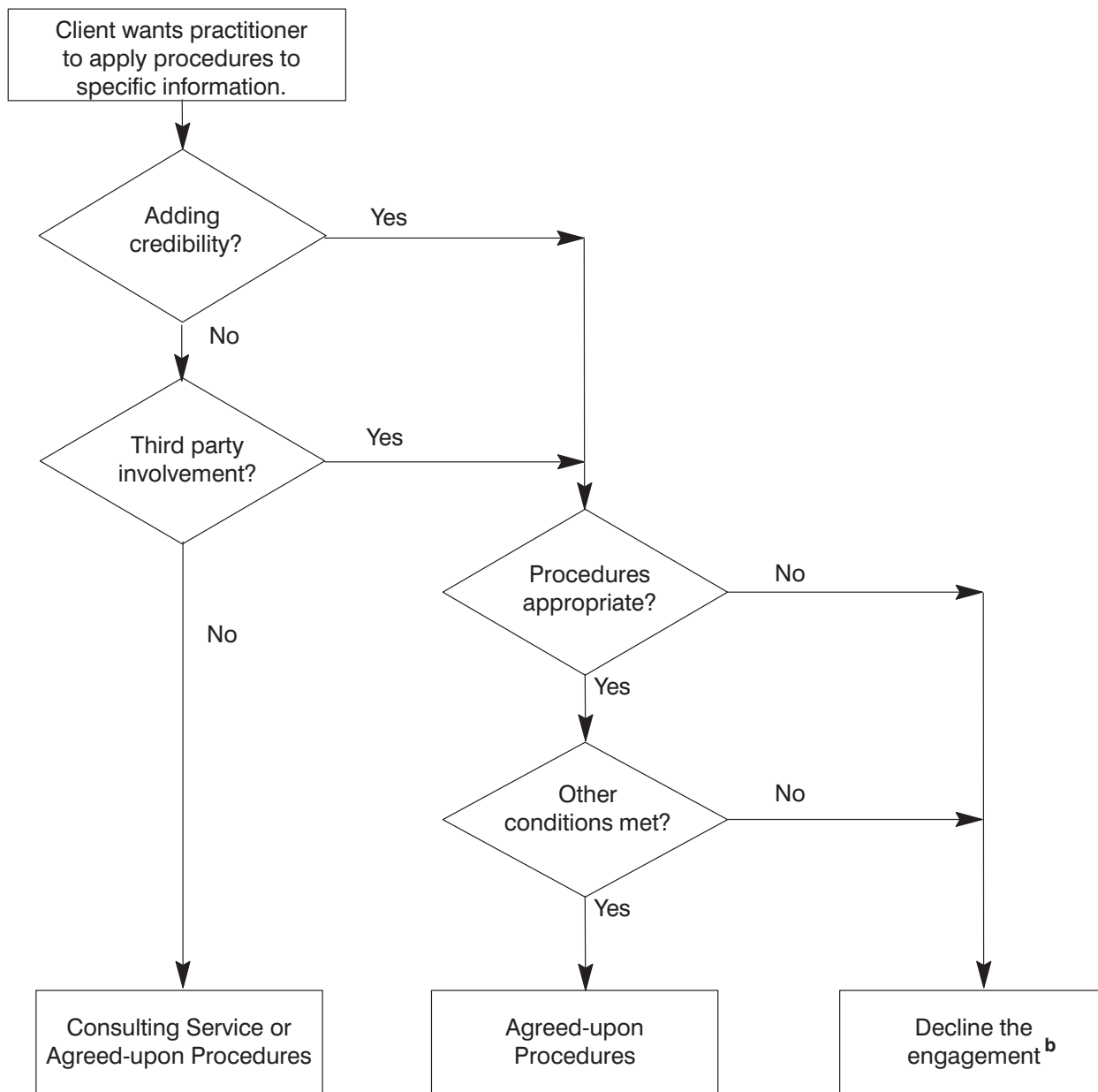
Exhibit 2-1 presents some recommendations to assist practitioners in determining whether an agreed-upon procedures engagement or a consulting engagement may be appropriate for a specific client situation. The following paragraphs discuss the considerations in greater detail.

Adding Credibility

A general rule for determining what type of engagement should be performed is to assess whether the practitioner is adding credibility to subject matter that is the responsibility of a third party. When that is the case, generally an agreed-upon procedures engagement is preferable. In an agreed-upon procedures engagement, a practitioner is normally bringing evidence to bear and adding credibility to subject matter provided by the responsible party. Generally, this is for the benefit of another third party that wishes to use the information for his or her purposes. Although the practitioner does not express an opinion, the purpose of an agreed-upon procedures engagement is usually to enhance the credibility of subject matter or an assertion related thereto for the benefit of a third party.

Third-party Involvement

A consulting engagement often involves only two parties—the practitioner and the client—whereas an agreed-upon procedures engagement often involves three parties—the practitioner, the responsible party (which might or might not be the client), and the interested parties (the specified parties of the report). In a consulting engagement, the practitioner is often engaged to generate information and to present his or her own findings, conclusions, and recommendations for the purpose of benefiting the client. However, the practitioner is not necessarily *adding credibility* to subject matter that is the responsibility of a third party. In a consulting engagement, the practitioner may evaluate subject matter as part of his or her research, but the findings and recommendations remain those of the practitioner. When a third-party user of the report is involved, it is believed an agreed-upon procedures engagement is preferable.

Exhibit 2-1**Agreed-upon Procedures or Consulting Engagement^a****Notes:**

- ^a This exhibit is intended only to assist practitioners in deciding between agreed-upon procedures and consulting engagements. It does not address engagements covered under Statements on Standards for Valuation Services.
- ^b Practitioners might be able to meet the client's needs by providing another type of service under the consulting standards.

* * *

Determining Whether the Services Can Be Performed as an Agreed-upon Procedures Engagement

Determining If the Procedures Are Appropriate. If the practitioner determines that the purpose of an engagement is to add credibility to subject matter that is the responsibility of a third party, the practitioner should then determine whether the requested procedures are appropriate for an agreed-upon procedures engagement. If the procedures are not considered appropriate, an agreed-upon procedures engagement is prohibited. In that case, the practitioner has the following choices:

- Work with the client and specified parties to refine the procedures.
- Perform the procedures as part of a consulting engagement.
- Decline the engagement.

This assumes that the client wants the engagement to consist of enumerated procedures applied to the subject matter. If that is not the case, other alternatives exist. For example, depending upon the nature of the subject matter, the practitioner might be able to audit a specified element under SAS No. 62, examine or review the subject matter under the attestation standards, or provide a financial statement service (compilation, review, or audit).

When making this decision, the practitioner must balance the desires and needs of the client against the practitioner's desire to limit risk. As noted previously, clients seldom want the practitioner to perform an agreed-upon procedures engagement. Instead, their desires are less precisely defined. The practitioner is then faced with the challenge of crafting an engagement that both satisfies the client's desires and does not expose the practitioner to undue risk.

Determining Whether Other Conditions Can Be Met. Once a practitioner determines that an agreed-upon procedures engagement is the appropriate type of engagement, a determination should then be made of whether the practitioner will be able to comply with applicable professional standards, particularly the engagement acceptance conditions. If those conditions cannot be met, the practitioner would either perform the procedures as part of a consulting engagement or decline the engagement.

Other Engagement Alternatives. As discussed in the preceding paragraph, if the practitioner cannot meet all of the performance requirements of an agreed-upon procedures engagement, he or she may be able to provide other services that will meet the client's needs under the consulting standards.

If the practitioner provides a consulting service, the practitioner's consulting report should be *clearly distinguishable* from an agreed-upon procedures report. This issue is discussed further in lesson 3.

Dual Engagements

Determining which type of service to provide may not always be an easy decision for the practitioner. Often, it will be difficult at best. In some cases, the practitioner may perform an agreed-upon procedures engagement as *part* of a larger consulting engagement. If that occurs, it is important that the practitioner communicate to the client the differences in the types of services performed. For agreed-upon procedures engagements performed under the attestation standards, AT 101 indicates the practitioner should do the following:

- *Establish and Document Client Understanding.* Discuss the differences between consulting services and attest (agreed-upon procedures) services with the client and obtain concurrence that the attest portion of the engagement is to be performed in accordance with the SSAE requirements. In addition, it is believed the practitioner should document the requirements to perform the attest service in the engagement letter or in an amendment thereto.
- *Communicate Results.* Issue separate reports on the two services. Both reports can be in the same binder as long as the reports are clearly identified and separated.

Case Study

The following case study illustrates a dual engagement that involves both consulting services and agreed-upon procedures.

Jacqueline Smith, office manager/bookkeeper for Hansen and Sons Construction Company, had been an employee of the company for two years. David Hansen, president, was not very involved in the front office, preferring to spend most of his time at individual job sites. David provided Jacqueline with a company credit card, which she used to make last minute purchases of building materials for the job sites. In March 20X9, David received an anonymous letter implying that Jacqueline was improperly using company funds. Although he believed that the implication of wrongdoing by Jacqueline was false, he contacted his CPA firm of Griffin, Smith & Co.

Colleen Price, a partner with Griffin, Smith & Co., was contacted by David Hansen and his company's attorney. During preliminary discussions, Colleen determined that David's wife was vigilant in reconciling the cash account, reviewing cash receipts, and reviewing cash disbursements each month. Because of the strong internal controls over cash, Colleen and David agreed that procedures would not be performed in that area.

Colleen also discovered that, although David and his wife tried to review documentation for credit card charges, they were not always thorough in this process. As internal controls over the company credit cards were considered to be less than adequate, David requested Colleen and her staff perform a *general investigation* to determine whether further procedures were warranted. Because David did not need or request a written report, Colleen decided it was appropriate to structure this portion of the engagement as a consulting engagement and to follow professional standards for consulting engagements.

As part of their general investigation, Colleen and her staff decided it would be beneficial to perform an analytical review of the company's financial statements for the previous five-year period. A quick analytical review revealed unusual increases in general and administrative expenses during the period that Jacqueline had been employed. David determined that if fraudulent amounts were indeed involved, he would want to submit the amounts to his bonding company. Therefore, he requested Colleen and her staff perform additional specific procedures and report their findings to him in a written report that could be submitted to his bonding company.

Because Jacqueline had authority to use the company credit card only for building materials purchased from approved vendors, David determined that any charges other than those would represent misuse of company funds. Accordingly, David requested that Colleen and her staff examine supporting documentation for all charges appearing on credit card statements for the two-year period ended March 31, 20X9. Based on the documentation, David instructed Colleen to categorize the charges into the following categories:

- Category 1—Charges for building materials purchased from a vendor appearing on the company's approved vendor list.
- Category 2—Unapproved charges.

Because the report was to be submitted to David's bonding company, Colleen determined that the purpose of the report was to add credibility to subject matter (that is, unauthorized credit card charges for the two-year period ended March 31, 20X1) for the benefit of a third party (the bonding company.) In addition, because the procedures to be performed were considered appropriate for an agreed-upon procedures engagement, and because Colleen and her staff were able to comply with applicable professional standards, Colleen determined that it was appropriate to structure this portion of the engagement as an agreed-upon procedures engagement. Colleen obtained a signed engagement letter from David and began the procedures.

After reviewing credit card charges for the two-year period ended March 31, 20X9, Colleen's staff summarized the charges as follows:

- Category 1—185 charges, totaling \$578,056.90
- Category 2—35 charges, totaling \$50,568.95

Colleen and her staff summarized their procedures and findings in an agreed-upon procedures report using the reporting guidance presented in lesson 3. Before submitting the report to the bonding company, Colleen obtained the bonding company's acknowledgment for the sufficiency of the procedures.

In this case study, Colleen may perform either an agreed-upon procedures engagement or a consulting engagement. Colleen chose to perform this part of the engagement as an agreed-upon procedures engagement under AT 201 because it was for use by a third party. Had David requested Colleen to prepare a written report summarizing

the changes in Category 1 and Category 2, but intended the report to be only for his own use, Colleen might have decided to perform the entire engagement as a consulting engagement. In that situation, Colleen would be generating information for the use of the client only.

ACCEPTING AN AGREED-UPON PROCEDURES ENGAGEMENT

Conditions for Engagement Acceptance

AT 201 includes several conditions for engagement performance. In order to ensure that a practitioner does not accept an engagement that he or she is unable to perform, it is believed that the following conditions should generally be met before *accepting* an agreed-upon procedures engagement.

- The practitioner is independent. Ethics Interpretation 101-11 (ET 101.13) establishes unique independence rules for certain engagements that fall under SSAE No. 10.
- One of the following conditions is met—
 - The client is responsible for the subject matter or has a reasonable basis for providing a written assertion about the subject matter when the nature of the subject matter is such that a responsible party does not otherwise exist.
 - The client is not responsible for the subject matter but is able to provide the practitioner, or have a third party who is responsible for the subject matter provide the practitioner, with evidence of the third party's responsibility for the subject matter.
- The practitioner and the specified parties agree to the procedures performed or to be performed by the practitioner.
- The specified parties take responsibility for the sufficiency of the agreed-upon procedures for their purposes.
- The subject matter to which the procedures are to be applied is subject to reasonably consistent measurement.
- The criteria to be used in the determination of findings are agreed upon between the practitioner and the specified parties.
- The procedures to be performed are expected to result in reasonably consistent findings.
- Evidential matter related to the subject matter to which the procedures are applied is expected to exist and to provide a reasonable basis for expressing the practitioner's findings.
- When applicable, the practitioner and specified parties agree on any materiality limits for reporting purposes.
- Use of the report is restricted to the specified parties.

The following additional conditions also should be met for certain specific engagements:

- In an agreed-upon procedures engagement relating to prospective financial statements, significant assumptions should be disclosed. (AT 301, *Financial Forecasts and Projections*).
- For engagements relating to compliance, management should evaluate the entity's compliance with requirements or the effectiveness of internal control over compliance (AT 601, *Compliance Attestation*).

The practitioner should also consider:

- Whether there are any professional reasons not to provide services to the client, and
- What services are to be provided and whether professional standards or other relevant requirements can be met in providing those services.

As discussed above, the specified parties assume responsibility for the sufficiency of the procedures for their purposes in an agreed-upon procedures engagement. Thus, in most cases, practitioners may perform any procedures requested by the specified parties. However, when the requested procedures appear obviously insufficient to meet the needs of the specified parties, some practitioners believe those concerns should be communicated to the client. Depending on the client's reaction, those practitioners may wish to reconsider whether to accept the agreed-upon procedures engagement.

Finally, the conditions for engagement performance include no requirement that the practitioner be the client's ongoing auditor or accountant. Consequently, practitioners can provide agreed-upon procedures for any existing or potential client, as long as all requirements for engagement performance (including independence) are met.

Prospective Client's Reputation

Before accepting a new client, a practitioner should consider the reputation of the prospective client and its management. Statement on Quality Control Standards No. 7 (QC 10.27), *A Firm's System of Quality Control for a CPA Firm's Accounting and Auditing Practice*, requires CPA firms to establish policies and procedures to provide the firm with reasonable assurance that it will undertake or continue relationships and engagements only where the firm has considered the integrity of the client. In many small businesses, ownership and operational control are concentrated in one or a few individuals. This means that, for many engagements, a primary consideration in client acceptance is the general honesty and good faith of the owner/manager.

Factors to Consider When Evaluating Integrity. When evaluating the integrity of the client, paragraph 30 of SQCS No. 7 (QC 10.30) offers the following factors to consider:

- Nature of operations and specific business practices.
- Attitude of the client's principal owners, key management, and those charged with its governance towards aggressive accounting and internal control matters.
- Length of the relationship with the client.

Gathering Evidence of Integrity. It is recommended that the firm consider conducting a thorough and complete screening of any current and prospective clients. For small firms and acceptance of relatively small clients, cost-benefit considerations are involved in determining the extent to which the firm would ordinarily perform client screening. However, SQCS No. 7 requires firms to consider current and prospective client integrity, and it is believed that firms should consider performing thorough client screening procedures whenever feasible. Practitioners may also want to consider the guidance in the AICPA's Professional Issues Task Force Practice Alert 2003-03, *Acceptance and Continuance of Clients and Engagements*. The practice alert is nonauthoritative, but may help practitioners further understand what they should consider when establishing policies and procedures for accepting or continuing a client relationship. The practice alert is available at www.aicpa.org.

Communication with a Predecessor or Primary Accountant. It is suggested that the practitioner who is considering accepting a new agreed-upon procedures engagement consider applying procedures similar to those in SAS No. 84 (AU 315), *Communications Between Predecessor and Successor Auditors*. Although such communication is not required by professional standards, such communication may be useful in providing valuable information to the practitioner.

The precise form of communication with a predecessor is not specified by SQCS No. 7. For example, written communication is not required—simply talking with the predecessor is enough. If the client is currently served by

another practitioner for recurring accounting or auditing services, it is suggested making inquiries of that practitioner regarding:

- Facts that may bear on the integrity of management.
- Significant disagreements with management.
- Whether the current practitioner refused to provide this service and, if so, why.
- Communication to those charged with governance regarding fraud or other illegal acts performed by the client or its employees, and internal control related matters.

If the client has until now used another practitioner for recurring accounting and auditing services, but the firm is now picking up all of the client's work, the practitioner should also inquire regarding the items discussed above. In addition, the practitioner should also ask about matters that may affect the conduct of the engagement, such as areas that required inordinate amounts of time or unusual items, and the predecessor's understanding of the reasons for the change in practitioners.

The practitioner should obtain the prospective client's permission for communicating with the predecessor or primary accountant. (This is necessary because of the ethical requirement for confidentiality.) The practitioner should also request that the client authorize the predecessor or primary accountant to respond fully. If the prospective client refuses to provide this permission, the practitioner should find out why. Such a refusal is considered by many practitioners to be sufficient reason to turn down an engagement. Generally, the practitioner does not need to review the workpapers of the predecessor or primary accountant unless it is necessary for performing one of the agreed-upon procedures.

Meeting Professional Standards and Other Requirements

Assessment of Required Services. A preliminary discussion with the prospective client is usually necessary to become familiar with the services that will be required. This allows the practitioner to consider whether the firm's resources are adequate to provide those services.

The preliminary discussion should include consideration of the following:

- *The Nature of the Procedures.* Are the procedures appropriate for an agreed-upon procedures engagement, and will outside resources be necessary to complete the engagement?
- *Expected Use of the Report.* Is the report needed to meet contractual requirements, to meet the requirements of a government agency, for the information of absentee owners, or for use in negotiating a sale of the business? Are all specified parties of the report identified?
- *Need for Agreed-upon Procedures.* Does the prospective client understand the differing scopes, levels of assurance, and costs associated with examinations, reviews, agreed-upon procedures, and consulting engagements?
- *Need for Other Services.* Are other services, such as consulting services or other assistance, needed?
- *Reporting Deadlines.* Is the report needed by a particular date to meet the client's needs? Does the date allow sufficient time to perform the necessary testwork?

Adequate Training and Knowledge. Before accepting a new engagement, the practitioner is required to consider whether he or she has adequate knowledge and training to complete the engagement. The practitioner must have adequate knowledge of the subject matter. That knowledge may be obtained through formal or continuing education, through consultation with others, or through practical experience. As part of planning any agreed-upon procedures engagement, the practitioner should obtain an adequate understanding of the requested procedures to determine whether outside resources will be necessary to complete the engagement. This understanding can normally be obtained through discussions with the client.

While practitioners are not required to possess all of the necessary knowledge *before* accepting an engagement, it is a good idea to consider resources that will be needed for successful completion before acceptance. In some cases, a practitioner might want to seek the assistance of other practitioners or specialists. Participation of others may range from availability to provide advice to active participation in parts of the engagement.

Although AT 201 does not address the active involvement of other practitioners in an engagement, the guidance regarding the use of internal auditors would generally apply to other practitioners. While a practitioner may consult with other practitioners on certain issues, procedures enumerated in the agreed-upon procedures report should be performed by the practitioner who was engaged to perform the engagement.

Independence. As noted previously, one of the conditions for engagement performance is that the practitioner be independent. For agreed-upon procedures engagements performed under the attestation standards, practitioners must be independent pursuant to Rule 101 of the AICPA *Code of Professional Conduct*. It is recommended that practitioners read Rule 101 of the *Code*, the interpretations of Rule 101, and the independence rulings for thorough guidance concerning independence.

Just as in traditional accounting and auditing services, the practitioner may assist the client in developing the subject matter and still remain independent. However, SSAE No. 10 requires management to accept responsibility for the subject matter or provide evidence of a third party's responsibility for the subject matter. If the practitioner is providing nonattest services for an attest client, he or she should follow Ethics Interpretation 101-3, "Performance of Nonattest Services," (ET 101.05) from the AICPA *Code of Professional Conduct*.

In some agreed-upon procedures engagements (for example, procedures related to a proposed acquisition), the client may not be the responsible party. (As noted previously, the person or entity providing the information is referred to as the responsible party.) When the client is not the responsible party, the question may arise as to whether the practitioner must be independent of both the client and the responsible party. It is believed that the practitioner should be independent of both. Otherwise, the practitioner may be seen as being biased in the performance of his or her procedures. Also, professional standards seem to require independence of both the client and the responsible party. ET 92.03 states that the term *client* includes both the entity that engages the CPA and the entity with respect to which professional services are performed. In an agreed-upon procedures engagement, it is the subject matter provided by the responsible party to which practitioners perform professional services.

Interpretation 101-11 (ET 101.13) provides unique guidance on the application of Rule 101 to attest engagements when the report is restricted to specified parties (that is, agreed-upon procedures reports and reports that are restricted because the criteria are appropriate only for specified parties). Interpretation 101-11 specifically addresses independence with respect to the responsible party in such engagements. The Interpretation does not require that *all* members of the firm be independent of the responsible party. Instead, it requires that the members of the engagement team, individuals who directly supervise or manage the attest engagement partner, and individuals who consult with the attest engagement team regarding issues specific to the related engagement be independent. Independence is not required of other individuals in the firm. Independence would also be considered impaired if the firm has a financial relationship with the responsible party that is covered by Interpretation 101-1A (ET 101.02) and material to the firm.

Subject Matter, Criteria, and Procedures

AT 201 allows the practitioner to perform an agreed-upon procedures attestation engagement only if he or she believes that the subject matter is capable of reasonably consistent evaluation against criteria that are suitable and available to users.

Thus, it is believed that an agreed-upon procedures engagement can be performed as long as—

- The procedures agreed to are expected to result in findings that are capable of reasonably consistent evaluation (that is, the procedures are not overly subjective, described in an unclear manner, or open to varying interpretation, and
- The procedures relate to the subject matter.

Engagement Acceptance Form

Before accepting an engagement, some firms find it useful to complete checklists that summarize relevant considerations.

Existing Client

Practitioners are often requested to perform agreed-upon procedures for existing clients. SQCS No. 7 (QC 10.27) requires policies and procedures for assessing a continuing association with a client. Thus, the practitioner should consider the topics discussed in this lesson and reassess the desire and ability to retain an existing client. This reassessment is especially important if there has been a high degree of turnover in key management positions.

CONSIDERING THE USE OF A SPECIALIST

While practitioners should be knowledgeable about general business matters, they are not required to have the experience or qualifications of persons trained for another profession. When an agreed-upon procedures engagement requires expertise beyond that of the practitioner, the practitioner may agree to be assisted by a specialist in performing certain procedures. According to AU 336, a specialist is a person or firm that possesses special skill or knowledge in a field other than the attest function. A specialist does not include an individual employed by the practitioner's firm.

Situations in which the practitioner might need to use the work of a specialist include the following:

- Valuations of unusual assets.
- Determination of physical characteristics. (For instance, a medical specialist might assist the practitioner in understanding the characteristics of diagnosis codes involved in applying procedures to specified medical records.)
- Determination of amounts through use of statistical or actuarial techniques.
- Interpretations of technical or legal requirements. (For example, an attorney might provide assistance in interpreting legal terminology that involves certain regulatory or contractual requirements.)

When a specialist is used in an attestation engagement, the attestation standards require that the practitioner have sufficient knowledge of the subject matter to:

- Communicate to the specialist the objectives of the work and
- Evaluate the specialist's work to determine if the objectives were achieved.

In addition, any time a specialist is used in an agreed-upon procedures engagement, the specified parties should explicitly agree to such involvement. It is recommended that the agreement be documented in the engagement letter. Also, when a practitioner uses a specialist that is not employed by the practitioner's firm, the practitioner should consider the requirements of Ethics Ruling No. 112 (ET 191.224–.225) related to the use of third-party service providers. Finally, the nature of the assistance provided by the specialist should be described in the practitioner's report.

Appropriate and Inappropriate Uses of a Specialist's Work

When using the work of a specialist, the practitioner may agree to apply certain agreed-upon procedures to the work or report of the specialist and may also agree to refer to the work or report of the specialist in the agreed-upon procedures report. However, the practitioner should not agree to merely read the report of a specialist solely for the purpose of describing or repeating the specialist's findings. In addition, the practitioner should not take responsibility for any of the specialist's work.

Responsibility for Deciding Whether a Specialist Is Needed

Because the specified parties of an agreed-upon procedures report are responsible for the sufficiency of procedures to be performed, those parties should ultimately be responsible for deciding when to use a specialist.

However, because the specified parties may not know whether a practitioner has adequate knowledge and training to perform an engagement, the practitioner may need to be involved in that decision. To ensure that the specified parties ultimately take responsibility for determining when a specialist is used, it is recommended to address this matter in the engagement letter.

Responsibility for Evaluating the Competency of a Specialist

When performing an agreed-upon procedures engagement, the practitioner is not required to evaluate the competency of a specialist as required for audits under SAS No. 73 (AU 336), *Using the Work of a Specialist*. However, when matters come to the practitioner's attention by other means that contradict the subject matter, the practitioner should ordinarily include such matters in the report. It is believed that if matters come to the practitioner's attention concerning the competency of a specialist, the practitioner might consider communicating those matters to the specified parties. Although practitioners would not be required to follow the guidance in SAS No. 73 when evaluating matters that come to their attention, practitioners might find that guidance to be useful. In addition, specified parties might find the guidance in SAS No. 73 to be useful in performing their own evaluation of a specialist's competency.

Because clients often erroneously assume that a practitioner will automatically evaluate the competency of a specialist, this responsibility should be addressed in the engagement letter. In order to avoid any misunderstandings in this area, adding a sentence such as the following to the engagement letter is recommended:

We assume no responsibility for assessing the competency of specialists to be used in this engagement.

SELF-STUDY QUIZ

Determine the best answer for each question below. Then check your answers against the correct answers in the following section.

19. AT 201, *Agreed-Upon Procedures Engagements*, provides guidance to the practitioner on applying agreed-upon procedures to any type of information. According to AT 201, which one of the following terms used in that standard is defined correctly?
 - a. An assertion is any declaration or set of related declarations about whether the subject matter is based on or in conformity with GAAP.
 - b. The subject matter is what the practitioner applies procedures to.
 - c. The selective parameter about which the subject matter is measured is called the criteria.
 - d. The responsible party is the practitioner's client.
20. AT 201 requires that certain conditions exist whenever a practitioner performs an agreed-upon procedures engagement. Which of the following conditions are **not** required to exist?
 - a. The practitioner and the specified parties agree to the procedures to be performed by the practitioner.
 - b. The specified parties take responsibility for the sufficiency of the agreed-upon procedures for their purposes.
 - c. The subject matter to which the procedures are to be applied is the responsibility of a third party.
 - d. The procedures to be performed are expected to result in reasonably consistent findings.
21. AT 201 includes several conditions that must exist whenever a practitioner performs an engagement. **All but which** of the following conditions should generally be met before accepting an agreed-upon procedures engagement?
 - a. The criteria to be used in the determination of findings are agreed upon between the practitioner and the specified parties.
 - b. The practitioner is independent.
 - c. When the nature of the subject matter is such that a responsible party does not otherwise exist, the client is responsible for the subject matter or has a reasonable basis for providing a written assertion about the subject matter.
 - d. The subject matter to which the procedures are to be applied is material to the annual financial statements.
22. SAS No. 84, *Communications Between Predecessor and Successor Auditors*, provides guidance for successor auditors who wish to communicate with predecessor auditors. Although not required by professional standards, it is suggested that a practitioner who is considering accepting a new agreed-upon procedures engagement consider applying procedures similar to those in SAS No. 84. Which of the following best describes some of those procedures described in SAS No. 84?
 - a. SAS No. 84 requires the auditor to communicate with the predecessor auditors in writing.
 - b. SAS No. 84 requires the practitioner to obtain the prospective client's permission for communicating with the predecessor or primary accountant.
 - c. SAS No. 84 requires the practitioner to instruct the predecessor or primary accountant to respond fully.
 - d. SAS No. 84 requires the practitioner to review the workpapers of the predecessor or primary accountant.

23. One of the conditions for performance of an agreed-upon procedures engagement under the attestation standards is that the practitioner be independent pursuant to Rule 101 of the AICPA *Code of Professional Conduct*. Which of the following best describes the practitioner's responsibilities under Rule 101 in an agreed-upon procedures engagement?
- a. Unlike in traditional accounting and auditing services, the practitioner may not assist the client in developing the subject matter and still remain independent.
 - b. If the practitioner assists the client in developing the subject matter of the engagement, management must accept responsibility for the subject matter in order for the practitioner to maintain his or her independence.
 - c. When the client is not the responsible party, it is believed that the practitioner should be independent of the client but not necessarily of the responsible party.
 - d. All members of the practitioner's firm must be independent of the responsible party.
24. Ross Martin, CPA, was hired by Bendrick Watches to perform certain agreed-upon procedures on its raw materials inventory. Since part of the inventory included diamonds, Ross decided to hire a specialist to assist with the determination of certain physical characteristics attributable to diamonds. Which of the following best describes Ross' responsibilities for the procedures performed by the specialist?
- a. Ross is required to have sufficient knowledge about diamonds to communicate to the specialist the objectives of the work and evaluate the specialist's work to determine if the objectives were achieved.
 - b. When using the work of a specialist, Ross may agree to read the report of a specialist solely for the purpose of describing or repeating the specialist's findings in his report.
 - c. As long as the specified users agree with the use of a specialist, Ross may take responsibility for the specialist's work in his report.
 - d. When performing an agreed-upon procedures engagement, Ross' responsibility to evaluate the competency of a specialist is the same as required for audits under SAS No. 73, *Using the Work of a Specialist*.

SELF-STUDY ANSWERS

This section provides the correct answers to the self-study quiz. If you answered a question incorrectly, reread the appropriate material. **(References are in parentheses.)**

19. AT 201, *Agreed-Upon Procedures Engagements*, provides guidance to the practitioner on applying agreed-upon procedures to any type of information. According to AT 201, which one of the following terms used in that standard is defined correctly? **(Page 52)**
- a. An assertion is any declaration or set of related declarations about whether the subject matter is based on or in conformity with GAAP. [This answer is incorrect. While financial statements represent the subject matter of financial results and GAAP are the criteria against which they are measured, that is not true in other types of agreed-upon procedures engagements. In such engagements, the client can assert that the subject matter is in conformity with any criteria, and that criteria might or might not be formally established, like GAAP. In an agreed-upon procedures engagement, the criteria against which the subject matter is measured merely has to be agreed upon between the practitioner and the specified parties. That is, practitioners can evaluate the subject matter against any criteria that the specified parties find useful for their purposes per AT 201.]
 - b. **The subject matter is what the practitioner applies procedures to. [This answer is correct. The subject matter is what the engagement is about. For example, in an audit of financial statements, the subject matter is the financial results portrayed in the financial statements. In an examination regarding the effectiveness of a company's internal control over financial reporting, the subject matter is the internal control over financial reporting.]**
 - c. The selective parameter about which the subject matter is measured is called the criteria. [This answer is incorrect. The subject matter must have an *objective* parameter by which it is measured. Furthermore, the subject matter must be capable of reasonably consistent estimation or measurement against the criteria per AT 201.]
 - d. The responsible party is the practitioner's client. [This answer is incorrect. While the responsible party might be the practitioner's client, it does not have to be. The responsible party is someone, other than the practitioner, who takes responsibility for the subject matter per AT 201.]
20. AT 201 requires that certain conditions exist whenever a practitioner performs an agreed-upon procedures engagement. Which of the following conditions are **not** required to exist? **(Page 53)**
- a. The practitioner and the specified parties agree to the procedures to be performed by the practitioner. [This answer is incorrect. In all agreed-upon procedures engagements, the practitioner and specified parties must agree to the procedures to be performed per AT 201.]
 - b. The specified parties take responsibility for the sufficiency of the agreed-upon procedures for their purposes. [This answer is incorrect. The responsible party must take responsibility for the sufficiency of the procedures.]
 - c. **The subject matter to which the procedures are to be applied is the responsibility of a third party. [This answer is correct. If the client is the responsible party, the subject matter is the client's responsibility. If the responsible party is not the client, the practitioner can still perform an agreed-upon procedures engagement as long as the responsible party provides the practitioner with evidence of the third party's responsibility for the subject matter.]**
 - d. The procedures to be performed are expected to result in reasonably consistent findings. [This answer is incorrect. It is believed that, to be appropriate, procedures should generally meet the following two tests: (a) they should address nature, timing, and extent and (b) they should result in findings that are capable of reasonably consistent estimation or measurement. In other words, for a procedure to be appropriate, the practitioner should be able to demonstrate that he or she accomplished it (i.e., sufficient evidence.)]

21. AT 201 includes several conditions that must exist whenever a practitioner performs an engagement. **All but which** of the following conditions should generally be met before accepting an agreed-upon procedures engagement? **(Page 58)**
- a. The criteria to be used in the determination of findings are agreed upon between the practitioner and the specified parties. [This answer is incorrect. AT 201 does require the practitioner and the specified parties to agree on the criteria to be used in the engagement.]
 - b. The practitioner is independent. [This answer is incorrect. The practitioner must be independent in order to perform an agreed-upon procedures engagement. Ethics Interpretation 101-11 establishes unique independence rules for certain engagements that fall under SSAE No. 10.]
 - c. When the nature of the subject matter is such that a responsible party does not otherwise exist, the client is responsible for the subject matter or has a reasonable basis for providing a written assertion about the subject matter. [This answer is incorrect. AT 201 requires the client to be responsible for the subject matter or to have a reasonable basis for providing a written assertion about the subject matter when the nature of the subject matter is such that a responsible party does not otherwise exist.]
 - d. **The subject matter to which the procedures are to be applied is material to the annual financial statements. [This answer is correct. According to AT 201, the condition that must exist before performing the engagement is that the subject matter is subject to reasonably consistent measurement.]**
22. SAS No. 84 (AU 315), *Communications Between Predecessor and Successor Auditors*, provides guidance for successor auditors who wish to communicate with predecessor auditors. Although not required by professional standards, it is suggested that a practitioner who is considering accepting a new agreed-upon procedures engagement consider applying procedures similar to those in SAS No. 84. Which of the following best describes some of those procedures described in SAS No. 84? **(Page 60)**
- a. SAS No. 84 requires the auditor to communicate with the predecessor auditors in writing. [This answer is incorrect. Written communication is not required—simply talking with the predecessor is enough per SAS No. 84.]
 - b. **SAS No. 84 requires the practitioner to obtain the prospective client's permission for communicating with the predecessor or primary accountant. [This answer is correct. Obtaining such permission is necessary because of the ethical requirement for confidentiality per SAS No. 84.]**
 - c. SAS No. 84 requires the practitioner to instruct the predecessor or primary accountant to respond fully. [This answer is incorrect. The practitioner should not make this request to the predecessor accountant but to the client. It is the client who should authorize the predecessor or primary accountant to respond fully. If the prospective client refuses to provide this permission, the practitioner should find out why. Such a refusal is considered by many practitioners to be sufficient reason to turn down an engagement per SAS No. 84.]
 - d. SAS No. 84 requires the practitioner to review the workpapers of the predecessor or primary accountant. [This answer is incorrect. The practitioner is generally not required to review the workpapers unless it is necessary for performing one of the agreed-upon procedures per SAS No. 84.]

23. One of the conditions for performance of an agreed-upon procedures engagement under the attestation standards is that the practitioner be independent pursuant to Rule 101 of the AICPA *Code of Professional Conduct*. Which of the following best describes the practitioner's responsibilities under Rule 101 in an agreed-upon procedures engagement? **(Page 61)**
- a. Unlike in traditional accounting and auditing services, the practitioner may not assist the client in developing the subject matter and still remain independent. [This answer is incorrect. According to Rule 101 of the Code, the practitioner can assist the client in developing the subject matter and still retain his or her independence just as in more traditional types of engagements.]
 - b. If the practitioner assists the client in developing the subject matter of the engagement, management must accept responsibility for the subject matter in order for the practitioner to maintain his or her independence. [This answer is correct. As long as management accepts responsibility for the subject matter, the practitioner would remain independent.]**
 - c. When the client is not the responsible party, it is believed that the practitioner should be independent of the client but not necessarily of the responsible party. [This answer is incorrect. The belief is that the practitioner should be independent of both. Otherwise, the practitioner may be seen as being biased in the performance of his or her procedures. Professional standards seem to require independence of both the client and the responsible party. ET 92.03 states that the term *client* includes both the entity that engages the CPA and the entity with respect to which professional services are performed. In an agreed-upon procedures engagement, it is the subject matter provided by the responsible party to which practitioners perform professional services.]
 - d. All members of the practitioner's firm must be independent of the responsible party. [This answer is incorrect. Interpretation 101-11 specifically addresses independence with respect to the responsible party in agreed-upon procedures engagements. It requires that members of the engagement team, individuals who directly supervise or manage the attest engagement partner, and individuals who consult with the attest engagement team regarding issues specific to the related engagement be independent. Independence is not required of other individuals in the firm.]
24. Ross Martin, CPA, was hired by Bendrick Watches to perform certain agreed-upon procedures on its raw materials inventory. Since part of the inventory included diamonds, Ross decided to hire a specialist to assist with the determination of certain physical characteristics attributable to diamonds. Which of the following best describes Ross' responsibilities for the procedures performed by the specialist? **(Page 62)**
- a. Ross is required to have sufficient knowledge about diamonds to communicate to the specialist the objectives of the work and evaluate the specialist's work to determine if the objectives were achieved. [This answer is correct. This is a requirement of the attestation standards. In addition, any time a specialist is used in an agreed-upon procedures engagement, the specified parties should explicitly agree to such involvement. The agreement should be documented in the engagement letter.]**
 - b. When using the work of a specialist, Ross may agree to read the report of a specialist solely for the purpose of describing or repeating the specialist's findings in his report. [This answer is incorrect. Per the attestation standards, when using the work of a specialist, the practitioner may agree to apply certain agreed-upon procedures to the work or report of the specialist and may also agree to refer to the work or report of the specialist in the agreed-upon procedures report. However, the practitioner should not agree to merely read the report of a specialist solely for the purpose of describing or repeating the specialist's findings.]
 - c. As long as the specified users agree with the use of a specialist, Ross may take responsibility for the specialist's work in his report. [This answer is incorrect. Per the attestation standards, the practitioner should not take responsibility for any of the specialist's work.]
 - d. When performing an agreed-upon procedures engagement, Ross' responsibility to evaluate the competency of a specialist is the same as required for audits under SAS No. 73, *Using the Work of a Specialist*. [This answer is incorrect. When performing an agreed-upon procedures engagement, the

practitioner is not required to evaluate the competency of a specialist as required for audits under SAS No. 73. However, when matters come to the practitioner's attention by other means that contradict the subject matter, the practitioner should ordinarily include such matters in the report. Best practices indicate that if matters come to the practitioner's attention concerning the competency of a specialist, the practitioner might consider communicating those matters to the specified parties. Although practitioners would not be required to follow the guidance in SAS No. 73 when evaluating matters that come to their attention, practitioners might find that guidance to be useful. In addition, specified parties might find the guidance in SAS No. 73 to be useful in performing their own evaluation of a specialist's competency.]

EXAMINATION FOR CPE CREDIT**Lesson 2 (NTETG101)**

Determine the best answer for each question below. Then mark your answer choice on the Examination for CPE Credit Answer Sheet located in the back of this workbook or by logging onto the Online Grading System.

17. AT 101, *Attestation Standards*, is the umbrella standard that governs all types of attestation engagements, including many agreed-upon procedures engagements. Which of the following engagements is governed by AT 101?
- a. Engagements in which the practitioner is engaged to apply agreed-upon procedures to prospective financial statements.
 - b. Engagements in which a service auditor includes in his or her report a separate reference to substantive procedures applied to user transactions or assets at the service organization.
 - c. Engagements in which the practitioner reports on specified compliance requirements based solely on an audit of financial statements.
 - d. Engagements in which an accountant is engaged to issue letters for underwriters and certain other requesting parties in connection with financial statements and financial statement schedules contained in registration statements filed with the Securities and Exchange Commission (SEC) under the Securities Act of 1933 (the Act) and other securities offerings.
18. AT 201, *Agreed-Upon Procedures Engagements*, provides guidance to the practitioner on applying agreed-upon procedures to any type of information. Which of the following best describes a requirement of AT 201?
- a. According to AT 201, a written assertion is required in an agreed-upon procedures engagement.
 - b. In an agreed-upon procedures engagement, the subject matter may or may not be related to the financial statements, and it may or may not be numeric.
 - c. In an agreed-upon procedures engagement, the practitioner assumes responsibility for the sufficiency of the procedures.
 - d. The responsible party in an agreed-upon procedures engagement is always the practitioner's client.
19. A practitioner requested by a client to perform procedures may be unsure of whether the services should be structured as agreed-upon procedures or consulting services. Since professional standards for agreed-upon procedures and consulting engagements differ significantly, it is important that the engagement be structured appropriately and performed under the applicable standards. Which of the following statements best describes the differences between these engagements?
- a. Consulting engagements often are more flexible than agreed-upon procedures engagements; therefore, consulting engagements may, in some cases, better fit a client's needs and represent a more practical alternative.
 - b. Because there are specific reporting requirements for consulting reports, such reports are normally very precise in nature. Because there are no specific reporting standards for agreed-upon procedures reports, however, those reports are often more subjective and may describe practitioners' procedures in a less precise manner.
 - c. Consulting engagements must meet specific performance and reporting requirements, whereas agreed-upon procedures engagements are subject to less stringent requirements.

- d. A consulting engagement is often preferable because it offers more protection for the practitioner. Should litigation later arise, practitioners may be in a better defensive position if they have performed a consulting engagement.
20. The type of entity and business practice, aggressive accounting practices, and the length of the relationship with the client are all examples of which of the following?
- a. Factors to consider when evaluating integrity.
 - b. Factors to consider when choosing a specialist.
 - c. Factors to consider when choosing a specified party.
 - d. Do not select this answer choice.
21. When an agreed-upon procedures engagement requires expertise beyond that of the practitioner, the practitioner may agree to be assisted by a specialist in performing certain procedures. Which of the following statements about the practitioner's responsibilities when using a specialist in an agreed-upon procedures engagement is **not** correct?
- a. The practitioner must have sufficient knowledge of the subject matter to communicate to the specialist the objectives of the work and evaluate the specialist's work to determine if the objectives were achieved.
 - b. Ultimately, the specified parties are responsible for deciding whether to use a specialist.
 - c. The practitioner must read the report of a specialist in order to take responsibility for any of the specialist's work.
 - d. Do not select this answer choice.

Lesson 3: Performing an Agreed-upon Procedures Engagement

INTRODUCTION

This lesson describes how to perform an agreed-upon procedures engagement, from establishing an understanding with the client to issuing the agreed-upon procedures report. Specifically, it addresses how to plan the agreed-upon procedures engagement and design the agreed-upon procedures to be performed, as well as the basic requirements of workpapers in such an engagement. Furthermore, this lesson describes how to summarize findings in an agreed-upon procedures engagement. It also discusses reviewing workpapers and performing other administrative functions at the end of the engagement. Finally, this lesson describes the elements of a representation letter obtained from the responsible party as well as each element of the practitioner's agreed-upon procedures report.

Occasionally, during the course of an engagement, the client might request the practitioner to change the nature of the engagement. The request may be either to an agreed-upon procedures engagement (for example, from an audit to an agreed-upon procedures engagement) or from an agreed-upon procedures engagement (for example, from an agreed-upon procedures engagement to a consulting engagement). This lesson discusses the practitioner's considerations when this occurs. It also discusses the quality control and peer review standards that apply to agreed-upon procedures engagements.

Learning Objectives:

Completion of this lesson will enable you to:

- Identify how to establish the terms of the engagement, as well as each element of the understanding with the client required by the attestation standards.
- Determine factors affecting engagement planning, including the responsibilities of the practitioner.
- Determine the purpose and basic requirements of workpapers and the representation letter in an agreed-upon procedures engagement.
- Recognize the elements of the practitioner's agreed-upon procedures report.
- Assess factors to consider when determining how to handle a change in the nature of the engagement and identify the quality control and peer review standards applying to agreed-upon procedures engagements.

ESTABLISHING THE TERMS OF THE ENGAGEMENT

Responsibilities of the Specified Parties and the Practitioner

As previously noted, specified parties must agree upon the procedures performed or to be performed and must take responsibility for the sufficiency of the procedures for their purposes. In some cases, the practitioner may have already performed the procedures as part of a consulting engagement. Even so, the specified parties must still agree to the procedures and take responsibility for their sufficiency.

In determining the specific procedures to be performed, the specified parties assume the risk that the procedures might be insufficient for their purposes. They also assume the risk that they might misunderstand or misapply the practitioner's reported findings. In performing an agreed-upon procedures engagement, the practitioner's responsibility is to carry out the procedures requested by the specified parties. In doing so, the practitioner bears the risk that procedures may be misapplied and that inappropriate findings may be reported. In addition, the practitioner bears the risk that appropriate findings may not be reported or may be reported incorrectly. The practitioner, however, assumes no responsibility for determining the sufficiency of the procedures. Some practitioners believe that, when requested procedures appear obviously inadequate to meet the needs of the specified parties, those concerns should be communicated to the client.

Obtaining Agreement on Procedures

To ensure that the specified parties agree upon the procedures performed or to be performed, the practitioner should ordinarily communicate directly with each of the specified parties and obtain affirmative acknowledgment

for the sufficiency of procedures. This may be accomplished either by meeting with the specified parties or by distributing a draft of the anticipated report or a copy of an engagement letter to the specified parties and obtaining their agreement. When possible, meeting with the specified parties and discussing the proposed procedures is recommended. In that way, practitioners can ask questions to clear up any ambiguities and suggest alternatives when more efficient or less costly procedures can be substituted. When the specified parties are unsure of the procedures that might be applied to accomplish their objectives, practitioners can provide suggestions. Ultimately, however, the specified parties must decide what procedures will be performed and take responsibility for their sufficiency.

When practitioners are unable to communicate directly with all of the specified parties, they should apply one or more of the following alternative procedures:

- Compare the procedures to be applied to written requirements of the specified parties.
- Discuss the procedures to be applied with appropriate representatives (such as legal counsel) of the specified parties involved.
- Review relevant contracts with or correspondence from the specified parties.

If practitioners use a draft of the report to establish the procedures to be applied, clearly state that it is a draft. The following is an example of a paragraph that can be added to the draft report to make this clear:

This draft is furnished solely for the purpose of indicating the form of report that we would expect to issue, the matters expected to be covered in the report, and the nature of the procedures we would expect to perform. Based on our discussions with [Client], it is our understanding that the procedures listed in this draft report are those that [Specified Party] expects us to perform. Unless [Specified Party] informs us otherwise, we shall assume that there are no additional procedures it wishes us to perform. The text of the report itself will depend, of course, on the results of the procedures, which we would not expect to complete until shortly before our report is issued.

It is important that the draft (and final) report clearly describe the procedures to be applied so that there is no misunderstanding about the basis of the practitioner's findings, and so that the specified parties can decide whether the procedures are sufficient for their purposes.

Obtaining Written Acknowledgment. While AT 201 does not require practitioners to obtain *written* acknowledgment from the specified parties for the sufficiency of procedures, it is generally good practice to do so. Written acknowledgment is obtained if all specified parties sign the engagement letter. However, if all specified parties do not sign the engagement letter, a "Request for Specified Party's Comments on Procedures" can be sent along with a copy of the report or engagement letter. In some situations (for example, if procedures are part of a law or regulation), it may not be practical to obtain written acknowledgment.

Engagement Letters

AT 201 requires that practitioners establish and document a clear understanding regarding the terms of the engagement, preferably in an engagement letter. Although an engagement letter is not *required*, it is believed that one should be obtained on every attestation engagement. Doing so is one of the best ways to ensure that the client, the practitioner, and any other specified parties have a clear understanding of the terms of the engagement.

When a practitioner agrees to provide services to a client for a fee, a contract is created. It is good business practice in any engagement to reduce that contract to writing by using an engagement letter. In an agreed-upon procedures engagement, however, the need for an engagement letter can be even greater. By their nature, agreed-upon procedures engagements are susceptible to misunderstandings about what procedures were performed and who was responsible for determining the procedures. Engagement letters are excellent tools for educating clients about their own responsibilities and those of the practitioner. If an engagement letter is properly written and explained to the parties involved, it can eliminate many misconceptions that clients and specified parties frequently have. Obtaining an engagement letter signed by all specified parties is one of the practitioner's most important tools for limiting the business risk involved in performing an agreed-upon procedures engagement.

Required Elements. SSAE No. 10 requires the practitioner to obtain an understanding with the client about each of the following matters:

- *The Objectives of the Engagement.* The practitioner should address the objectives of the engagement and any limitations thereof primarily through discussions with the client about the level of services the practitioner will provide. In an agreed-upon procedures engagement, the practitioner should ensure that the client understands that the engagement will not result in an opinion about whether the subject matter conforms to the agreed-upon criteria. Rather, the practitioner will merely list the procedures performed and resulting findings. The practitioner should also consider whether a consulting engagement, while not resulting in an agreed-upon procedures report, might meet the client's needs at a lower cost. The practitioner should discuss the various alternatives with the client to determine the client's needs and preferences.
- *Client's Responsibilities.* In an agreed-upon procedures engagement, it is the client's responsibility to select the criteria and determine that it is appropriate for its purposes. Furthermore, it is the client's responsibility to select the procedures and determine whether they are sufficient for its purposes. If the client is the responsible party, the client is also responsible for the subject matter (or related assertion) to which the practitioners will perform their procedures.
- *Practitioner's Responsibilities.* In an agreed-upon procedures engagement, the practitioner is responsible for carrying out the procedures specified, but not for determining the sufficiency of those procedures. Nor is the practitioner responsible for applying other procedures that might be applied in other types of professional engagements, such as audits. Practitioners are encouraged to describe their services as precisely as possible to avoid misunderstandings that might arise.
- *Limitations of the Engagement.* The limitations that practitioners should address relate to at least two aspects of each engagement: (a) limitations of the types of services to be performed and (b) use limitations based on the type of service. For example, in an agreed-upon procedures engagement, the practitioner provides no assurance on whether the subject matter is in conformity with the agreed-upon criteria. Furthermore, the report is restricted to use by the specified parties only. If a restricted-use report is not acceptable to the client, the practitioner should discuss engagement alternatives that would provide a practitioner's report appropriate for general use.

Other Matters. Other matters practitioners should consider discussing with the client and including in the engagement letter include—

- *Subject Matter to Which Procedures Are to Be Applied.* The practitioner should determine specifically the subject matter to be reported on. This understanding should be used to determine that the practitioner has, or can acquire, sufficient expertise to perform the engagement.
- *Identification of Specified Parties.* In an agreed-upon procedures engagement, the practitioner may report using criteria that, although not otherwise suitable, have been agreed to by the specified parties and the client. But such a report should be restricted to the specified parties who agreed on the criteria or who can be presumed to understand it, and, like all agreed-upon procedures reports, is not appropriate for general use. Knowing who the specified parties are helps the practitioner assess the risks in the engagement and also provides information regarding the appropriateness of the service to be provided.
- *Identification of the Responsible Party.* The client might not always be the responsible party.
- *Specified Parties' Acknowledgment of Their Responsibility for the Sufficiency of the Procedures.* This is part of the client's responsibilities as discussed in the preceding paragraph. In certain situations, additional users might be added before the agreed-upon procedures engagement is complete. To cover those situations, the engagement letter also should include a statement that additional users will provide an acknowledgment of their agreement to the procedures and a statement that such procedures are sufficient for their purposes. One of the ways that other specified parties can document their responsibilities is by signing the engagement letter.

- *Agreement on Procedures to Be Applied by Listing (or Referring to a Separate Listing of) the Procedures.* As previously discussed, the specified parties agree upon the procedures to be performed in an agreed-upon procedures engagement. The procedures should either be listed in the engagement letter or the engagement letter should refer to the document where such procedures are listed.
- *Identification of Criteria.* The criteria to be used must be agreed-upon by specified parties. Generally, it can be anything those parties agree to as long as it meets their needs. The engagement letter should identify the criteria to be used when applying the agreed-upon procedures.
- *Reference to Attestation Standards Established by the AICPA.* The engagement letter should contain a statement that the agreed-upon procedures engagement will be performed in accordance with attestation standards established by the AICPA.
- *Disclaimers Expected to Be Included in the Report.* The engagement letter should clarify that the practitioner's agreed-upon procedures report will disclaim an opinion or any form of assurance on whether the subject matter is presented in conformity with the criteria.
- *Restrictions on the Use of the Report.* As previously discussed, an agreed-upon procedures report is restricted to specified parties who have agreed to the procedures and criteria.
- *Involvement of a Specialist, If Any.*
- *Agreed-upon Materiality Limits and Sample Sizes.*
- *Subsequent Events.*
- *Logistics.* The practitioner should ascertain whether the client has the necessary personnel and expertise to develop the subject matter. The practitioner may assist the client in developing the subject matter, including the related disclosures or underlying data. However, the level of practitioner involvement in this exercise may affect the timing of the engagement and the nature and extent of the attestation procedures applied.
- *Fees.* The practitioner should determine that the fee arrangements are appropriate. Considerations include the following:
 - The size of the fee relative to the amount of effort required and risk assumed.
 - The form of the fee (for example, fees should not be contingent).
 - The timing of the payment (for example, whether retainers or progress payments are required).
- *Third-party Outsourcing Arrangements.*

When the Client Is Not the Responsible Party. A practitioner can perform an agreed-upon procedures engagement when the engaging entity is not the party responsible for the subject matter. This might occur, for example, when a potential buyer of a business wants agreed-upon procedures applied to the seller's information (such as in a due diligence engagement). Applying procedures, making inquiries, and obtaining representations from the responsible party might be more difficult when the responsible party is not the client.

When the client is not the responsible party, the practitioner is required to obtain evidence of the responsible party's responsibility for the subject matter or assertion. This evidence might be, for example, in an engagement letter or representation letter, within the presentation of the subject matter (including notes), in a written assertion, or stated in legislation, regulation, or contracts.

The respective responsibilities and expectations should ideally be made clear in the engagement letter. Also, it is believed the practitioner should be independent of both the client and the responsible party.

Who Should Sign the Letter? The engagement letter should be signed by those to whom it is addressed. It is believed that it is preferable for the letter to be addressed to and signed by the client and all other specified parties. In some cases, however, that may not be practical (for example, if the letter contains fee information and the client prefers to keep fee information confidential). If the engagement letter is not signed by all specified parties, other methods must be used to obtain their agreement on the procedures.

When Should the Letter Be Obtained? The engagement letter should generally be obtained prior to beginning the procedures. However, it is not uncommon for the final engagement letter to be obtained just prior to the issuance of the report. That generally occurs because of the evolving nature of many agreed-upon procedures engagements. When that is the case, it is recommended that practitioners consider obtaining an engagement letter early on and then modifying it.

Modifying Terms after the Engagement Has Begun

Because of the evolving nature of an agreed-upon procedures engagement, it is not uncommon for the terms to be revised before the engagement is completed. Often, additional procedures are requested as a result of the practitioner's findings. If circumstances arise that cause the practitioner to believe additional procedures are advisable or that the terms of the engagement should be modified, the practitioner should obtain agreement from the specified parties for the modification. Normally, such an agreement should be documented in writing. That can be done by obtaining a new engagement letter.

When circumstances arise that restrict the performance of the agreed-upon procedures, and the specified parties do not agree to the restriction, the practitioner should describe the restrictions in his or her report or withdraw from the engagement.

Adding Users after the Engagement Has Begun

The practitioner's agreed-upon procedures report should be restricted to the specified parties. As a result, the practitioner may be requested to add users who did not agree upon the terms of the engagement (nonparticipant parties). When this occurs, the practitioner should consider the identity of the nonparticipant parties and the intended use of the report. If the request is made before the procedures are completed and the practitioner consents, it is recommended that the engagement letter be amended as necessary and a "Request for Specified Party's Comments on Procedures" be obtained from the nonparticipant party(ies).

If the request is made after the procedures are completed (either before or after the report is issued), AT 201 requires that the practitioner obtain affirmative acknowledgment from the nonparticipant parties agreeing to the procedures performed and taking responsibility for their sufficiency. Normally, the required acknowledgment should be in writing and should include other matters pertinent to the engagement, such as acknowledgment of the fact that the practitioner has performed no additional procedures since the date of the report.

If the nonparticipant parties acknowledge their responsibility for the sufficiency of the procedures, the practitioner may add those parties as specified parties. If the report has already been issued, the practitioner may do one of the following:

- Provide a copy of the report to the added user with a cover letter acknowledging that the party has been added as a specified party and stating that no procedures have been performed since the date of the report.
- Reissue the report with the new user included in the list of specified parties. If the report is reissued, it should be dated as of the date of the original report (that is, the date that the agreed-upon procedures were completed). AT 201 indicates that AU 530.06–.07 may be helpful in this situation.

When adding users, the practitioner is not required to notify or obtain the permission of the original users. However, there may be circumstances in which the practitioner should consider doing so (for example, if the parties are specified by contract). It is believed that it is generally better to obtain permission of the original specified parties, preferably in writing. That can usually be done by amending the engagement letter and having all parties sign the amendment.

When additional users request to be added, the practitioner can always approach the situation as a new agreed-upon procedures engagement. This might be an effective solution if, for example, the added user requests the practitioner to perform additional procedures that were not part of the original engagement.

SELF-STUDY QUIZ

Determine the best answer for each question below. Then check your answers against the correct answers in the following section.

25. XYZ Corporation engages Blake Smith, CPA, to perform an agreed-upon procedures engagement. As one of the specified parties, which of the following statements best describes the responsibilities of XYZ Corp. in the engagement?
- a. XYZ Corporation assumes the risk that the agreed-upon procedures might be insufficient for the purpose of the engagement.
 - b. XYZ Corporation assumes the risk that appropriate findings may not be reported or may be reported incorrectly.
 - c. XYZ Corporation bears the risk that agreed-upon procedures may be misapplied and that inappropriate findings may be reported.
 - d. XYZ Corporation does not necessarily have to agree with the practitioner about the procedures to be performed.
26. In an agreed-upon procedures engagement, the specified parties must agree with the practitioner about the procedures to be performed. Which of the following statements about obtaining their approval is **incorrect**?
- a. To ensure that the specified parties agree upon the procedures performed or to be performed, the practitioner should ordinarily communicate directly with each of the specified parties and obtain affirmative acknowledgment for the sufficiency of procedures.
 - b. The practitioner can communicate with the specified parties by distributing a draft of the anticipated report or a copy of an engagement letter to the specified parties and obtaining their agreement.
 - c. When the specified parties are unsure of the procedures that might be applied to accomplish their objectives, the practitioner cannot perform the engagement.
 - d. While AT 201 does not require practitioners to obtain written acknowledgment from the specified parties for the sufficiency of procedures, generally, it is good practice to do so.
27. SSAE No. 10 requires practitioners to establish an understanding with the client before performing an engagement. In an agreed-upon procedures engagement, the practitioner is required to obtain an understanding with the client about **all but which** of the following matters?
- a. The fees for the engagement.
 - b. The client's responsibilities in the agreed-upon procedures engagement.
 - c. The objectives of the engagement.
 - d. The limitations of the engagement.

SELF-STUDY ANSWERS

This section provides the correct answers to the self-study quiz. If you answered a question incorrectly, reread the appropriate material. **(References are in parentheses.)**

25. XYZ Corporation engages Blake Smith, CPA, to perform an agreed-upon procedures engagement. As one of the specified parties, which of the following statements best describes the responsibilities of XYZ Corp. in the engagement? **(Page 73)**
- a. **XYZ Corporation assumes the risk that the agreed-upon procedures might be insufficient for the purpose of the engagement. [This answer is correct. In an agreed-upon procedures engagement, the specified parties—of which the responsible party is one—must assume the risk that the procedures might be insufficient for their purposes.]**
 - b. XYZ Corporation assumes the risk that appropriate findings may not be reported or may be reported incorrectly. [This answer is incorrect. This is the responsibility of the practitioner, not the specified party per AT 201.]
 - c. XYZ Corporation bears the risk that agreed-upon procedures may be misapplied and that inappropriate findings may be reported. [This answer is incorrect. This is the responsibility of the practitioner, not the specified party per AT 201.]
 - d. XYZ Corporation does not necessarily have to agree with the practitioner about the procedures to be performed. [This answer is incorrect. According to AT 201 in an agreed-upon procedures engagement, the specified parties must agree with the practitioner about the procedures to be performed.]
26. In an agreed-upon procedures engagement, the specified parties must agree with the practitioner about the procedures to be performed. Which of the following statements about obtaining their approval is **incorrect**? **(Page 74)**
- a. To ensure that the specified parties agree upon the procedures performed or to be performed, the practitioner should ordinarily communicate directly with each of the specified parties and obtain affirmative acknowledgment for the sufficiency of procedures. [This answer is incorrect. Under AT 201, the practitioner should communicate directly with the specified parties and obtain their approval.]
 - b. The practitioner can communicate with the specified parties by distributing a draft of the anticipated report or a copy of an engagement letter to the specified parties and obtaining their agreement. [This answer is incorrect. Under AT 201 distributing a draft of the anticipated report or an engagement letter is one way to obtain the specified parties' agreement.]
 - c. **When the specified parties are unsure of the procedures that might be applied to accomplish their objectives, the practitioner cannot perform the engagement. [This answer is correct. In this case, the practitioner can provide suggestions. Ultimately, however, the specified parties must decide what procedures will be performed and take responsibility for their sufficiency. Assuming the specified parties and the practitioner are able to agree to the procedures, there is no problem with the practitioner performing the engagement.]**
 - d. While AT 201 does not require practitioners to obtain written acknowledgment from the specified parties for the sufficiency of procedures, generally, it is good practice to do so. [This answer is incorrect. Obtaining a written acknowledgement from the specified parties is the best way to ensure there is agreement about the procedures to be performed per AT 201.]

27. SSAE No. 10 requires practitioners to establish an understanding with the client before performing an engagement. In an agreed-upon procedures engagement, the practitioner is required to obtain an understanding with the client about **all but which** of the following matters? **(Page 75)**
- a. **The fees for the engagement.** [This answer is correct. Although it is good practice to establish an understanding with the client about the fees to be incurred, SSAE No. 10 does not mandate that the practitioner obtain an understanding with the client about fees. Ordinarily, however, the practitioner should determine that the fee arrangements are appropriate considering the size of the fee relative to the amount of effort required and risk assumed; the form of the fee (for example, fees should not be contingent); and the timing of the payment (for example, whether retainers or progress payments are required).]
 - b. The client's responsibilities in the agreed-upon procedures engagement. [This answer is incorrect. In an agreed-upon procedures engagement, it is the client's responsibility to select the criteria and determine that it is appropriate for its purposes. Furthermore, it is the client's responsibility to select the procedures and determine whether they are sufficient for its purposes. SSAE No. 10 requires the practitioner to establish an understanding with the client about its responsibilities.]
 - c. The objectives of the engagement. [This answer is incorrect. SSAE No. 10 requires the practitioner to address the objectives of the engagement and any limitations thereof primarily through discussions with the client about the level of services the practitioner will provide. In an agreed-upon procedures engagement, the practitioner should ensure that the client understands that the engagement will not result in an opinion about whether the subject matter conforms to the agreed-upon criteria.]
 - d. The limitations of the engagement. [This answer is incorrect. In an agreed-upon procedures engagement, the practitioner is required to obtain an understanding with the client about the limitations of the engagement: (a) limitations of the types of services to be performed and (b) use limitations based on the type of service. In an agreed-upon procedures engagement, the practitioner provides no assurance on whether the subject matter is in conformity with the agreed-upon criteria. Furthermore, the report is restricted to use by the specified parties only. If a restricted-use report is not acceptable to the client, the practitioner should discuss engagement alternatives that would provide a practitioner's report appropriate for general use.]

PLANNING AN AGREED-UPON PROCEDURES ENGAGEMENT

After establishing the terms of the engagement, the practitioner should then plan the engagement. In an audit (or examination), planning includes deciding on an overall strategy for the audit, making an initial assessment of audit risk and materiality, and deciding on the overall timing of the engagement. One of the primary purposes of planning is to allow the auditor to develop an effective audit program. In an agreed-upon procedures engagement, the specified parties determine the procedures. The practitioner may assist the specified parties in designing the procedures, but the practitioner is not responsible for the sufficiency of the procedures. Consequently, many of the planning issues for audits or examinations are not relevant in agreed-upon procedures engagements. Planning issues relevant to agreed-upon procedures engagements is discussed below.

Responsibilities of the Practitioner

Engagement Risk. In an audit of financial statements, audit risk is the risk that the auditor may unknowingly fail to appropriately modify his or her opinion on financial statements that are materially misstated. In an examination, attestation risk is the risk that the practitioner may unknowingly fail to appropriately modify his or her attest report on subject matter that is materially misstated. Audit risk in a financial statement audit, as well as attestation risk in an examination engagement, consists of the following:

- Inherent risk.
- Control risk.
- Detection risk.

In an agreed-upon procedures engagement, the specified parties assume complete responsibility for inherent risk and control risk by incorporating their own assessments of those risks into their determination of the desired procedures. In addition, the specified parties assume partial responsibility for detection risk by determining the appropriateness and effectiveness of the procedures selected. The only risk assumed by the practitioner in an agreed-upon procedures engagement is a portion of detection risk. The practitioner assumes responsibility for the portion of detection risk associated with misapplying the agreed-upon procedures, misinterpreting their results, or communicating the findings incorrectly or ambiguously. The practitioner controls this risk by adequately planning and supervising the engagement and by exercising due professional care in performing the engagement.

Knowledge of the Subject Matter. The practitioner should have adequate knowledge of the subject matter. This includes understanding both the nature of the subject matter as well as the transactions or events that give rise to its measurement. It may also involve understanding the client's industry and how its business operates. As previously discussed, that knowledge may be obtained through formal or continuing education, through consultation with others, or through practical experience.

Understanding of the Procedures. The practitioner should also obtain an adequate understanding of the requested procedures to determine whether outside resources will be necessary to complete the engagement. As noted previously, this understanding can normally be obtained through discussions with the client. In some cases, a practitioner might want to seek the assistance of other practitioners or specialists. Participation of others may range from availability to provide advice, all the way to active participation in parts of the engagement.

Assignment of Personnel

The staffing of an agreed-upon procedures engagement will depend on the specific nature of each engagement and on each firm's own quality control policies. Although staff members can often be used to perform many of the agreed-upon procedures, it is believed heavy manager and partner involvement is usually necessary, particularly in the planning and reporting stages of the engagement. This is because agreed-upon procedures engagements, especially those involving nonfinancial information, are generally non-recurring and unique in nature.

DESIGNING PROCEDURES

Users' Responsibilities

In an agreed-upon procedures engagement, responsibility for the nature, timing, and extent of procedures lies with the specified parties of the report. In determining the procedures to be performed, the specified parties assume the risk that the procedures might be insufficient for their purposes. In addition, they assume the risk that they might misunderstand or inappropriately use findings that are properly reported by the practitioner.

Practitioner's Responsibilities

The practitioner's responsibility in an agreed-upon procedures engagement is to carry out the procedures and report the findings agreed to by the client and the specified parties in accordance with applicable professional standards. The practitioner does not assume risk for the sufficiency of the procedures, as that risk lies with the specified parties. In an agreed-upon procedures engagement, the procedures to be performed may be more or less extensive than those that would be necessary in another type of engagement (for example, an examination or review). The practitioner has no responsibility to determine the differences in the procedures agreed to and those that would be necessary for another type of engagement. In addition, the practitioner should perform only the procedures that he or she is *engaged* to perform. Any modification or extension of the procedures should be discussed with and approved by the specified parties.

Performing Procedures That Are Also Performed in an Examination or Review. If the procedures agreed to are equivalent to those that would be performed in another type of engagement, the practitioner would still issue an agreed-upon procedures report. For example, if the procedures were equivalent to those that would be performed in a review, the practitioner would *not* issue a review report but instead would issue an agreed-upon procedures report.

Applying Agreed-upon Procedures to All, or Substantially All, of the Elements, Accounts, or Items in a Financial Statement. Sometimes, practitioners might be requested to perform agreed-upon procedures on all, or substantially all, of the elements, accounts, or items of a financial statement. The authors believe that is appropriate as long as the procedures relate to individual financial statement elements and not to the financial statements as a whole.

Evidential Matter. One of the conditions for performing an agreed-upon procedures engagement is that the practitioner must expect that evidential matter exists to provide a reasonable basis for expressing his or her findings in the report. That means that the practitioner should be able to demonstrate that he or she performed the requested procedures. Thus, if the practitioner believes that evidential matter is not expected to exist, he or she should inform the client. It is suggested that this communication be made in writing. If done orally, it should be documented in the engagement workpapers.

Appropriate Procedures

Except for the types of procedures described under Inappropriate Procedures below, the practitioner may generally perform and report on any procedures that are requested by the specified parties. The procedures may be as limited or extensive as those parties desire, and the practitioner has no responsibility for making this determination. (However, mere reading of the subject matter does not constitute a sufficient procedure.) Examples of procedures that would generally be considered appropriate for an agreed-upon procedures engagement include the following:

- Inspecting specified documents for evidence of certain types of transactions or characteristics.
- Comparing certain documents, schedules, or analyses with specified attributes.
- Performing agreed-upon mathematical computations.
- Performing specific procedures to work that has been performed by others, including internal auditors. (However, it is inappropriate to merely read work performed by others solely to describe their findings.)

- Executing a sampling application after agreeing on relevant parameters.
- Confirming specified information with third parties.

To be appropriate, procedures should generally meet the following two tests:

- They should address nature, timing, and extent.
- They should result in findings that are capable of reasonably consistent estimation or measurement. In other words, for a procedure to be appropriate, you should be able to demonstrate that you accomplished it.

Inappropriate Procedures

In an agreed-upon procedures engagement, the practitioner may generally perform any procedures requested by the specified parties provided the procedures are not overly subjective, described in an unclear manner, or open to varying interpretation. This is because the practitioner's report should *clearly* list and describe the procedures performed. Examples of procedures that are not sufficiently clear include:

- Performing a *general review* of the company's accounts receivable.
- *Checking* the company's inventory balances.
- *Reconciling* the company's cash accounts.
- *Testing* the company's accounts payable balances.
- Performing a *limited review* of the company's cash accounts.

Use of vague terms such as these should generally be avoided. If they must be used, they should be accompanied by an explanation of what procedures are meant by the terms.

In addition to procedures that are described in a vague or unclear manner, the following procedures would normally also be considered inappropriate because they do not result in findings that are meaningful:

- Mere reading of the subject matter. (However, reading the subject matter is appropriate if it is performed in addition to other 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.

Materiality and Sampling

Applicability to an Agreed-upon Procedures Engagement. While the concept of materiality is essential in a financial statement audit, it is normally not relevant in an agreed-upon procedures engagement. In an agreed-upon procedures engagement, the practitioner is engaged to perform specific procedures that are requested by the specified parties. Any scopes or materiality levels used in performing the procedures should be determined by those users, stated in the engagement letter, and described in the practitioner's report.

Responsibility for Determining Materiality. While making a materiality judgment is not a required step in an agreed-upon procedures engagement, there may be engagements in which the client or specified parties request the practitioner to assist in determining a materiality limit (for example, by performing calculations for purposes of

determining scopes and/or sample sizes). When a client makes such a request, the practitioner may assist the client provided there is a clear understanding between the practitioner and the client that any resulting scopes or sample sizes are the responsibility of the specified parties. In addition, any materiality limits should be described in the agreed-upon procedures report. Note, however, that the materiality limit can be any amount the specified parties believe meets their needs. It may or may not be the same materiality amount that an auditor would use.

Responsibility for Adequacy of Sample Sizes. The responsibility for determining sample sizes in an agreed-upon procedures engagement lies with the specified parties of the report. The practitioner has no responsibility to calculate sample sizes. However, the specified parties may request the practitioner's assistance in determining sample sizes. Whenever a practitioner assists in making such a calculation, there should be a clear understanding that the responsibility for deciding on a specific sample size lies with the specified parties.

Execution of a sampling plan is an appropriate procedure if relevant sampling parameters have been agreed upon. This means that sampling parameters such as confidence levels and acceptable rates of misstatement must be discussed with and agreed to by specified parties. It is believed this is appropriate only in the rare circumstance in which statistical sampling is used (since sampling risk cannot be measured when nonstatistical sampling is used). This does not, however, preclude the use of nonstatistical sampling to assist the specified parties in determining the scope of procedures. It means only that the procedures should not refer to a sample. Instead, the procedure should refer to the number of items to be selected (which may or may not be based on a sample size calculation). Again, the sufficiency of the procedures is the responsibility of the specified parties, not the practitioner.

Planning the Extent of Procedures. When engaging a practitioner to apply agreed-upon procedures to specified financial statement elements, the client and users will need to decide the following:

- What subject matter the procedures should be applied to.
- What types of procedures should be applied (nature).
- How many items the procedure should be applied to (extent).
- As of what date or period the procedures should be applied (timing).

Because clients are often inexperienced in making those types of decisions, it is common in an agreed-upon procedures engagement for the client to request assistance from the practitioner in determining the nature, timing, and extent of procedures.

The number of items selected for a procedure can be any amount the specified parties believe meets their needs. It may or may not be the same scope that an auditor would use.

Documenting Materiality Levels and Sample Sizes in the Engagement Letter. Whenever a practitioner assists a client in determining materiality levels or sample sizes, the engagement letter should state specifically what procedures will be performed and what scopes or sample sizes will be used in performing the procedures. The engagement letter should *not*, in any way, state or infer that the practitioner will calculate materiality levels, scopes, or sample sizes. For example, it is believed that the procedures agreed to in the engagement letter should not include procedures such as the following:

- We will confirm all material accounts receivable balances as of December 31, 20X3.
- We will select and confirm a representative sample of accounts receivable balances as of December 31, 20X3.

However, those same procedures would be appropriate if they were revised as follows:

- We will confirm all accounts receivable balances exceeding \$25,000 as of December 31, 20X3.
- We will randomly select and confirm 25 accounts receivable balances as of December 31, 20X3.

Information Obtained through Other Means

The practitioner has no obligation to determine the sufficiency of procedures or to perform procedures beyond those requested by the specified parties. If, in connection with the performance of the agreed-upon procedures, information comes to the practitioner's attention by other means that significantly contradicts the subject matter, AT 201 indicates that the practitioner should include such information in his or her report. The practitioner, however, has no obligation to perform additional procedures as a result of the contradictory information. The practitioner is required only to include the information in his or her report.

Subsequent Events

AT 101 states that the practitioner has no responsibility to detect events occurring after the date of the subject matter (or assertion) that might affect it. However, it requires that he or she ask the responsible party (and the client, if it is not the responsible party) about whether it is aware of any events that occurred between the date of the subject matter or assertion and the date of the practitioner's report that contradict the subject matter or assertion. If the practitioner obtains a representation letter, this representation would ordinarily be included in it.

It is unclear how the requirement in AT 101 applies in agreed-upon procedures engagements. It is believed that, if the practitioners obtain a representation letter, it is good practice to include a representation from management about whether it is aware of subsequent events. If there are any such events, practitioners should consider the need to disclose such information. If the subsequent event is a loss caused by a fire, flood, or natural disaster, practitioners may wish to consider the guidance in the AICPA's Technical Practice Aid (TIS) 9070.05, *Consideration of Impact of Losses From Natural Disasters Occurring After Completion of Audit Field Work and Signing of the Auditor's Report But Before Issuance of the Auditor's Report and Related Financial Statements*. Although the guidance relates to audits, practitioners performing agreed-upon procedures may find this guidance helpful. Communicating other matters that come to their attention is discussed later in this lesson.

Other Information in a Document Containing the Practitioner's Report

If a client includes the practitioner's report (a) in an annual report to holders of securities or beneficial interests, annual reports of organizations for charitable or philanthropic purposes distributed to the public, and annual reports filed with regulatory authorities under the Securities Exchange Act of 1934 or (b) in other documents to which the practitioner, at the client's request, devotes attention, AT 101 requires the practitioner to read the other information not covered by the practitioner's report or covered by the report of another practitioner and consider whether it, or the manner of its presentation, is materially inconsistent with the information appearing in the practitioner's report.

From a practical standpoint, it may be difficult to determine how other information contained in such a document might be inconsistent with an agreed-upon procedures report, particularly since the practitioner expresses no conclusion in such report. In any event, the authors recommend that practitioners read the other information to ensure that there are no inconsistencies with their report.

Use of Client Personnel and Internal Auditors

In performing an agreed-upon procedures engagement, the practitioner may be requested to work with internal auditors or other client personnel. Depending on the nature of the subject matter to which procedures are to be applied, it might be appropriate for client personnel to assist the practitioner in preparing schedules, accumulating information, or performing other clerical tasks. However, the procedures enumerated in the practitioner's report should be performed solely and entirely by the practitioner.

In some cases, the specified parties may wish to have internal auditors perform and report on procedures deemed appropriate to meet their needs. Those procedures may or may not be similar to procedures being performed by the practitioner. As part of the agreed-upon procedures engagement, the specified parties may then request the practitioner to perform procedures on information documented in the workpapers of internal auditors. For example, the client may request the practitioner to reperform all or some of the internal auditors' procedures. Or, the practitioner may be requested to review the workpapers of the internal auditors (for example, to determine whether the internal auditors' workpapers contain documentation of procedures and findings and whether findings are

presented in the internal auditors' report). It is generally appropriate for a practitioner to perform this type of service as long as *only* the procedures performed by the practitioner are enumerated in his or her report. AT 201 states that it is not appropriate for the practitioner to perform the following procedures:

- Read the internal auditors' report for the sole purpose of describing or repeating the internal auditors' findings.
- Take responsibility for any portion of the internal auditors' procedures by reporting on those procedures as if they were performed by the practitioner.
- Report in any manner that implies joint responsibility for the procedures performed by internal auditors.

Use of Procedures Checklists

It is believed the approach that tends to be most effective and efficient for the typical agreed-upon procedures engagement is to use a standardized procedures checklist that is tailored, where necessary, to the particular engagement. Even though the specific agreed-upon procedures will vary from engagement to engagement, many of the standard procedures are the same in all engagements.

SELF-STUDY QUIZ

Determine the best answer for each question below. Then check your answers against the correct answers in the following section.

28. In an audit of financial statements, *audit risk* is the risk that the auditor may unknowingly fail to appropriately modify his or her opinion on financial statements that are materially misstated. Audit risk in a financial statement audit consists of inherent risk, control risk, and detection risk. Which of the following best describes the risks in an agreed-upon procedures engagement?
- a. The practitioner assumes responsibility for the portion of detection risk associated with misapplying the agreed-upon procedures, misinterpreting their results, or communicating the findings incorrectly or ambiguously.
 - b. The practitioner assumes complete responsibility for inherent risk and control risk when he determines which procedures to perform.
29. Meow Cat Food engaged its accountants to perform an agreed-upon procedures engagement. In establishing the terms of the engagement, it asked the accountants to perform the following procedures. Which of these procedures would be **inappropriate** in the agreed-upon procedures engagement?
- a. We confirmed the cash on deposit as of December 31, 20XX from the banks listed in Schedule A.
 - b. We tested the company's accounts payable balances as of December 31, 20XX.
 - c. We compared details of daily deposit slips for 5 days with the postings to the related individual receivable accounts.
 - d. We inspected the securities on hand at the company as of December 31, 20XX, which are shown in Schedule A, and examined each to determine if they were registered in the company's name.
30. In an agreed-upon procedures engagement, a practitioner may generally perform and report on any procedures that are requested by the specified parties. The procedures may be as limited or extensive as those parties desire, and the practitioner has no responsibility for making this determination. However, there are certain procedures that are considered inappropriate. Which of the following procedures would generally be **inappropriate** for the practitioner to perform?
- a. Performing specific procedures to work that has been performed by others, including internal auditors.
 - b. Evaluating the competency or objectivity of another party.
 - c. Executing a sampling application after agreeing on relevant parameters.
 - d. Confirming specified information with third parties.

31. Which of the following workpapers is generally **not** required in an agreed-upon procedures engagement?
- a. Documentation of engagement acceptance.
 - b. Documentation of how the users specified the procedures.
 - c. Procedures checklist.
 - d. Judgments about materiality.
32. Which of the following statements best describes the concepts of materiality in an agreed-upon procedures engagement?
- a. Like in a financial statement audit, the concept of materiality is essential in an agreed-upon procedures engagement.
 - b. In an agreed-upon procedures engagement, any scopes or materiality levels used in performing the procedures is determined by the practitioner.
 - c. Making a materiality judgment is a required step in every agreed-upon procedures engagement.
 - d. Execution of a sampling plan is an appropriate procedure if relevant sampling parameters have been agreed upon between the specified parties and the practitioner.

SELF-STUDY ANSWERS

This section provides the correct answers to the self-study quiz. If you answered a question incorrectly, reread the appropriate material. **(References are in parentheses.)**

28. In an audit of financial statements, *audit risk* is the risk that the auditor may unknowingly fail to appropriately modify his or her opinion on financial statements that are materially misstated. Audit risk in a financial statement audit consists of inherent risk, control risk, and detection risk. Which of the following best describes the risks in an agreed-upon procedures engagement? **(Page 82)**
- a. **The practitioner assumes responsibility for the portion of detection risk associated with misapplying the agreed-upon procedures, misinterpreting their results, or communicating the findings incorrectly or ambiguously. [This answer is correct. The practitioner controls this risk by adequately planning and supervising the engagement and by exercising due professional care in performing the engagement.]**
 - b. The practitioner assumes complete responsibility for inherent risk and control risk when he or she determines which procedures to perform. [This answer is incorrect. The specified parties assume responsibility for inherent and control risk by incorporating their own assessments of those risks into their determination of the desired procedures.]
29. Meow Cat Food engaged its accountants to perform an agreed-upon procedures engagement. In establishing the terms of the engagement, it asked the accountants to perform the following procedures. Which of these procedures would be **inappropriate** in the agreed-upon procedures engagement? **(Page 84)**
- a. We confirmed the cash on deposit as of December 31, 20XX from the banks listed in Schedule A. [This answer is incorrect. It is believed that, to be appropriate, procedures generally should (a) address nature, timing, and extent and (b) result in findings that are capable of reasonably consistent estimation or measurement. This procedure meets those criteria.]
 - b. **We tested the company's accounts payable balances as of December 31, 20XX. [This answer is correct. This procedure uses a term that is ambiguous and vague—tested. Many report users will be unclear about what this means; therefore, the accountant should not agree to perform this procedure. Instead, the accountant should work with the client to arrive at an appropriate procedure that can be performed to address the client's objectives.]**
 - c. We compared details of daily deposit slips for 5 days with the postings to the related individual receivable accounts. [This answer is incorrect. It is believed that, to be appropriate, procedures generally should (a) address nature, timing, and extent and (b) result in findings that are capable of reasonably consistent estimation or measurement. This procedure meets those criteria.]
 - d. We inspected the securities on hand at the company as of December 31, 20XX, which are shown in Schedule A, and examined each to determine if they were registered in the company's name. [This answer is incorrect. Best practices indicate that, to be appropriate, procedures generally should (a) address nature, timing, and extent and (b) result in findings that are capable of reasonably consistent estimation or measurement. This procedure meets those criteria.]

30. In an agreed-upon procedures engagement, a practitioner may generally perform and report on any procedures that are requested by the specified parties. The procedures may be as limited or extensive as those parties desire, and the practitioner has no responsibility for making this determination. However, there are certain procedures that are considered inappropriate. Which of the following procedures would generally be **inappropriate** for the practitioner to perform? **(Page 84)**
- a. Performing specific procedures to work that has been performed by others, including internal auditors. [This answer is incorrect. According to AT 201 performing specific procedures to work performed by others is an acceptable procedure since it should result in findings that are capable of reasonably consistent estimation or measurement and the practitioner should be able to demonstrate that he or she accomplished it.]
 - b. **Evaluating the competency or objectivity of another party. [This answer is correct. According to AT 201, evaluating the competency of another party generally would not result in meaningful findings; therefore, the practitioner should not do it.]**
 - c. Executing a sampling application after agreeing on relevant parameters. [This answer is incorrect. Executing a sampling application is an acceptable procedure since it would result in findings that are capable of reasonably consistent estimation and the practitioner would be able to demonstrate that he or she accomplished it.]
 - d. Confirming specified information with third parties. [This answer is incorrect. According to AT 201 confirming specified information with third parties is an acceptable procedure since it would result in findings that are capable of reasonably consistent estimation and the practitioner would be able to demonstrate that he or she accomplished it.]
31. Which of the following workpapers is generally **not** required in an agreed-upon procedures engagement? **(Page 84)**
- a. Documentation of engagement acceptance. [This answer is incorrect. Practitioners generally would have this workpaper in their agreed-upon procedures engagement.]
 - b. Documentation of how the users specified the procedures. [This answer is incorrect. Practitioners generally would have this workpaper in their agreed-upon procedures engagement.]
 - c. Procedures checklist. [This answer is incorrect. Practitioners generally would have this workpaper in their agreed-upon procedures engagement.]
 - d. **Judgments about materiality. [This answer is correct. Making a materiality judgment is not a required step in an agreed-upon procedures engagement. Nevertheless, there may be engagements in which the client or specified parties request the practitioner to assist in determining a materiality limit (for example, by performing calculations for purposes of determining scopes and/or sample sizes). When a client makes such a request, the practitioner may assist the client provided there is a clear understanding between the practitioner and the client that any resulting scopes or sample sizes are the responsibility of the specified parties.]**

32. Which of the following statements best describes the concepts of materiality in an agreed-upon procedures engagement? **(Page 85)**
- a. Like in a financial statement audit, the concept of materiality is essential in an agreed-upon procedures engagement. [This answer is incorrect. While the concept of materiality is essential in a financial statement audit, it is normally not relevant in an agreed-upon procedures engagement. In an agreed-upon procedures engagement, the practitioner is engaged to perform specific procedures that are requested by the specified parties. Any scopes or materiality levels used in performing the procedures should be determined by those users, stated in the engagement letter, and described in the practitioner's report.]
 - b. In an agreed-upon procedures engagement, any scopes or materiality levels used in performing the procedures is determined by the practitioner. [This answer is incorrect. In an agreed-upon procedures engagement, any scopes or materiality levels used in performing the procedures should be determined by the specified parties, stated in the engagement letter, and described in the practitioner's report.]
 - c. Making a materiality judgment is a required step in every agreed-upon procedures engagement. [This answer is incorrect. While making a materiality judgment is not a required step in an agreed-upon procedures engagement, there may be engagements in which the client or specified parties request the practitioner to assist in determining a materiality limit as discussed in d.]
 - d. **Execution of a sampling plan is an appropriate procedure if relevant sampling parameters have been agreed upon between the specified parties and the practitioner. [This answer is correct. This means that sampling parameters such as confidence levels and acceptable rates of misstatement must be discussed with and agreed to by specified parties. The authors believe this is appropriate only in the rare circumstance in which statistical sampling is used (since sampling risk cannot be measured when nonstatistical sampling is used). This does not, however, preclude the use of nonstatistical sampling to assist the specified parties in determining the scope of procedures. It means only that the procedures should not refer to a sample. Instead, the procedure should refer to the number of items to be selected (which may or may not be based on a sample size calculation). Again, the sufficiency of the procedures is the responsibility of the specified parties, not the practitioner.]**

WORKPAPERS

Basic Requirements

Workpapers are a practitioner's written record of the procedures applied and findings detected in an agreed-upon procedures engagement. SSAE No. 10 (AT 101), as amended by SSAE No. 11, *Attest Documentation*, establishes the documentation requirements for all engagements performed under the Statement on Standards for Attestation Engagements (SSAEs), including agreed-upon procedures engagements. SSAE No. 10, as amended, states that *attest documentation* is commonly referred to as *workpapers*.

According to SSAE No. 10, as amended, the form, quantity, and content of workpapers should be designed to meet the circumstances of the particular engagement and are matters of the practitioner's professional judgment. Workpapers record the procedures applied by the practitioner and the related findings. Workpapers might include work programs, analyses, memoranda, letters of confirmation and representation, and schedules or commentaries prepared or obtained by the practitioner. In deciding on the quantity, type, and content of the workpapers for a particular engagement, the practitioner might consider the following factors:

- Nature of the engagement (for example, type of entity, period to be covered, types of procedures to be applied).
- Manner in which the users specify the procedures (for example, through direct contact, through representatives, by reference to regulatory requirements).
- Nature of the subject matter to which the practitioner is applying procedures.
- The level of supervision and review needed in the particular circumstances (for example, the size and experience of the staff assigned to the engagement).

Recommended Content

It is recommended that the practitioner's workpapers include at least the following:

- Documentation of engagement acceptance.
- Engagement letter.
- Documentation of how the users specified the procedures.
- Documentation of planning considerations.
- Procedures checklist.
- A list of the procedures agreed to with a cross-reference to documentation of performance.
- Summary of findings.
- Attestation reporting checklist for agreed-upon procedures engagements.
- Agreed-upon procedures report.
- Representation letter.
- Documentation that the workpapers were reviewed.
- Documentation of unusual matters encountered and their resolution. (This should include documentation of the justification for any departure from a presumptively mandatory requirement and a description of how the practitioner achieved its objectives.)

Many practitioners will find that standard checklists and forms, are useful in meeting documentation requirements for an agreed-upon procedures engagement. When those practice aids are used, most other documentation decisions will relate to the format and extent of detail for documenting the specific procedures and findings.

REVIEW AND EVALUATION

Summarization of Findings

Throughout the engagement, the practitioner will accumulate findings detected while performing the agreed-upon procedures. One of the final stages of the engagement is summarizing the findings for preparation of the report. Practitioners can develop their own. A variety of workshop formats can be used for this purpose.

As noted previously, unless the specified parties indicate that only findings exceeding a specified amount should be reported, the concept of materiality does not apply. Absent any materiality limitations, all findings should be accumulated and reported.

Review of Workpapers

The review of workpapers near the conclusion of the engagement has two stages: (a) detailed review of the work of assistants and (b) a higher-level supervisory review. Although a senior accountant usually reviews the work of staff assistants and a manager or partner usually makes a supervisory review, there is considerable variation in practice. For example, in some agreed-upon procedures engagements, the senior accountant may be the only staff on the engagement. Specific practice may vary with the size and nature of the engagement, the size of the engagement team, and firm policies and practices on engagement administration.

Detailed Review. The idea of a detailed review is basically the same for an agreed-upon procedures engagement as for an audit. The objectives are to ensure that there is (a) adherence to professional standards and firm policies and procedures and (b) proper summarization of the results of procedures for the attention of the supervisory reviewer and for reporting to the specified parties.

The detailed review usually observes the following steps:

- a. For the subject matter to which procedures were applied, reviewing the supporting workpapers to assure that:
 - (1) The presentation of the subject matter is complete and properly headed, dated, initialed, and indexed.
 - (2) The procedures checklist has been indexed and completed, as indicated by initials, and the workpaper schedules indicate that the procedures have been performed.
 - (3) Findings have been properly identified and summarized.
 - (4) Any unusual matters have been included in the representation letter (usually in draft stage at this point), if one is to be obtained.
- b. Reviewing summary schedules and drafting the agreed-upon procedures report.

According to SSAE No. 10, as amended, the workpapers should indicate which engagement team members performed and reviewed the work. Some firms require the person performing the detailed review to initial each workpaper and schedule that is reviewed.

Supervisory Review. In practice, the greatest variations in review of workpapers occur in the extent and levels of supervisory review. Those variations are usually a result of differences in engagement size and complexity, engagement team size and qualifications, and individual firm policies and preferences for engagement administration. Generally, the supervisory review focuses more on the summary schedules, and less time and attention is given to supporting workpaper schedules. It is usually conducted after the agreed-upon procedures report has been drafted, and it is the final check on whether the procedures performed support the findings presented in the report.

Engagement Quality Control and Technical Review. SQCS No. 7 includes a requirement for the firm to establish criteria against which all engagements are to be evaluated to determine whether an engagement quality control review should be performed. An *engagement quality control review* (EQCR) is defined as “a process designed to provide an objective evaluation, by an individual or individuals who are not members of the engagement team, of the significant judgments the engagement team made and the conclusions reached in formulating the report.”

SQCS No. 7 (QC 10.81–.82) states that if an engagement meets specified criteria established by the firm, an EQCR should be performed for that engagement and completed before the report is released. Additionally, firm policies and procedures should indicate that the engagement partner is still responsible for the engagement and its performance, notwithstanding involvement of the engagement quality control reviewer. The engagement quality control reviewer may be a firm partner, an other person in the firm, a qualified external person, or a team comprised of such individuals, none of whom are part of the engagement team. The reviewer(s) should possess sufficient and appropriate experience and authority to perform the EQCR.

It is recommended that an engagement quality control and technical review be performed for each agreed-upon procedures engagement. In addition to meeting the requirements of SQCS No. 7, the review should be directed toward compliance with AICPA presentation and reporting guidelines and should focus on considering whether there are obvious errors.

SQCS No. 7 (QC 10.99) indicates that firms should establish policies and procedures for preparing appropriate documentation of the engagement quality control review, including documentation that reflects that—

- The engagement quality control review procedures required by firm policies have been performed.
- The engagement quality control review has been completed before the report is released.
- The reviewer is not aware of any unresolved matters that would cause him or her to believe that significant judgments made and conclusions reached were not appropriate.

Documentation supporting performance of the EQCR should indicate that the review was completed prior to the issuance of the engagement report.

Supervision, Review, and Approval Form

Most firms use some form of checklist to serve as a reminder of important engagement completion matters and to document completion of the review of the workpapers.

REPRESENTATION LETTER

Reasons for Obtaining a Letter

While it is recommended obtaining a representation letter in an agreed-upon procedures engagement, AT 201 does not require it. It requires only that a practitioner consider obtaining a representation letter from the responsible party.

Matters to Be Included. Examples of matters that might appear in such a representation letter include the following:

- a. A statement acknowledging the responsible party's responsibility for the subject matter and, when applicable, the assertion.
- b. The responsible party's assertion about the subject matter based on the criteria selected.
- c. A statement acknowledging responsibility for selecting the criteria and for determining that such criteria are appropriate for their purposes.
- d. A statement that the responsible party has disclosed to the practitioner all known matters contradicting the subject matter.

- e. A statement that any communication from regulatory agencies affecting the subject matter or the assertion has been disclosed to the practitioner.
- f. A statement that all records relevant to the subject matter and the agreed-upon procedures have been made available to the practitioner.
- g. A statement that the responsible party has disclosed any known events subsequent to the period (or point in time) of the subject matter being reported on, that would contradict the subject matter (or, if applicable, the assertion).
- h. Other matters as the practitioner deems appropriate.

Matters to Be Included When Client Is Not the Responsible Party. When the client is not the responsible party, the practitioner should also consider obtaining a representation letter from the client. Examples of matters that might appear in such a letter include the following:

- a. A statement that the client has disclosed any known events subsequent to the period (or point in time) of the subject matter being reported on, that would contradict the subject matter (or, if applicable, the assertion).
- b. A statement acknowledging the client's responsibility for selecting the criteria and for determining that such criteria are appropriate for their purposes.
- c. Other matters as the practitioner deems appropriate.

Refusal to Furnish a Representation Letter

If the responsible party or the client refuses to furnish all written representations that the practitioner deems necessary, the responsible party's or the client's refusal to furnish the written representations constitutes a limitation on the performance of the engagement. In such circumstances, practitioners should take one of the following actions:

- Disclose in the agreed-upon procedures report the inability to obtain written representations.
- Withdraw from the engagement. According to AT 201, the client's refusal to furnish all required representations in an agreed-upon procedures engagement performed under AT 601, *Compliance Attestation*, also constitutes a limitation on the scope of the engagement that would require the practitioner to withdraw from the engagement.
- Change the engagement to another type of engagement (for example, a consulting engagement).

The first option, disclosing in the report the inability to obtain a representation letter, might be used when, for example, the client has hired the practitioner to perform procedures on subject matter that is the responsibility of another party (that is, the client is not the responsible party). By including such a statement in the report, the client will be put on notice that the other party did not provide a representation letter. It is recommended that such a statement be included.

On the other hand, when a practitioner has determined that a representation letter is necessary and the client, who is also the responsible party, refuses to provide one, the practitioner should consider the potential risks of being associated with the engagement. It is believed that a refusal to provide a representation letter calls into question the practitioner's ability to rely on any representations made by the responsible party. Consequently, in most cases, the practitioner should obtain the representation letter or withdraw from the engagement.

Signing and Dating the Representation Letter

The representation letter should be obtained from the responsible party. Generally, the letter will be signed by the owner/manager and the highest-ranking officer under whose responsibility the subject matter falls. If the client is

not the party responsible for the subject matter, it is recommended that a separate representation letter be obtained from the client.

Neither AT 101 nor AT 201 indicate when the representation letter should be dated. (AT 101 does not require representation letters, but states that the practitioner *should* consider obtaining one. AT 201 also makes obtaining a representation letter optional, but notes that such letters are required for agreed-upon procedures engagement related to compliance with specified requirements under AT 601.)

However, certain other attestation standards (specifically, AT 501, 601, and 701) all specifically refer to the guidance on dating representation letters in SAS No. 85 (AU 333.09). AU 333.09, as amended by SAS No. 13, states that the representations should be made as of the date of the auditor's report. Therefore, it is recommended that representation letters for engagements under SSAEs that are silent on dating the representation letter follow the guidance in the auditing literature and make the date of the representation letter as of the date of the practitioner's report.

SELF-STUDY QUIZ

Determine the best answer for each question below. Then check your answers against the correct answers in the following section.

33. SSAE No. 10 (AT 101), as amended by SSAE No. 11, *Attest Documentation*, establishes the documentation requirements for all engagements performed under the SSAEs, including agreed-upon procedures engagements. **All but which** of the following statements describe the purpose and basic requirements of workpapers in an agreed-upon procedures engagement?
- a. Workpapers are a practitioner's written record of the procedures applied and findings detected in an agreed-upon procedures engagement.
 - b. The form, quantity, and content of workpapers should be designed to meet the circumstances of the particular engagement and are matters of the practitioner's professional judgment.
 - c. The basic purpose of the workpapers is to record the practitioner's understanding with the client and to document the client's agreement with the procedures to be performed.
 - d. Workpapers might include work programs, analyses, memoranda, letters of confirmation and representation, and schedules or commentaries prepared or obtained by the practitioner.
34. The responsible party's or the client's refusal to furnish all written representations that the practitioner deems necessary constitutes a limitation on the performance of the engagement. In such circumstances, **all but which** option is available to the practitioners?
- a. Describe the responsible party's oral representations in a memo in the workpapers.
 - b. Disclose in the agreed-upon procedures report the inability to obtain written representations.
 - c. Withdraw from the engagement.
 - d. Change the engagement to another type of engagement (for example, a consulting engagement).

SELF-STUDY ANSWERS

This section provides the correct answers to the self-study quiz. If you answered a question incorrectly, reread the appropriate material. **(References are in parentheses.)**

33. SSAE No. 10 (AT 101), as amended by SSAE No. 11, *Attest Documentation*, establishes the documentation requirements for all engagements performed under the SSAEs, including agreed-upon procedures engagements. **All but which** of the following statements describe the purpose and basic requirements of workpapers in an agreed-upon procedures engagement? **(Page 94)**
- a. Workpapers are a practitioner's written record of the procedures applied and findings detected in an agreed-upon procedures engagement. [This answer is incorrect. This is the basic purpose of workpapers in an agreed-upon procedures engagement per SSAE No. 10.]
 - b. The form, quantity, and content of workpapers should be designed to meet the circumstances of the particular engagement and are matters of the practitioner's professional judgment. [This answer is incorrect. According to SSAE No. 10, the particular circumstances of the engagement, along with the practitioner's judgment, affect the form, quantity, and content of workpapers in an agreed-upon procedures engagement.]
 - c. **The basic purpose of the workpapers is to record the practitioner's understanding with the client and to document the client's agreement with the procedures to be performed. [This answer is correct. Although these items should be documented in the workpapers, the basic purpose is broader than this: it is to record all procedures applied by the practitioner and the related findings.]**
 - d. Workpapers might include work programs, analyses, memoranda, letters of confirmation and representation, and schedules or commentaries prepared or obtained by the practitioner. [This answer is incorrect. All of these items might be included in the workpapers of an agreed-upon procedures engagement per SSAE No. 10.]
34. The responsible party's or the client's refusal to furnish all written representations that the practitioner deems necessary constitutes a limitation on the performance of the engagement. In such circumstances, **all but which** option is available to the practitioners? **(Page 97)**
- a. **Describe the responsible party's oral representations in a memo in the workpapers. [This answer is correct. This is not an option. When the responsible party/client will not furnish a representation letter, the practitioner generally should withdraw from the engagement as discussed in c. below. In certain situations, the practitioner might agree to change the engagement to a consulting engagement as discussed in item d. If the client is not the responsible party, the practitioner might consider disclosing the inability to obtain a representation letter in the report as discussed in item b.]**
 - b. Disclose in the agreed-upon procedures report the inability to obtain written representations. [This answer is incorrect. Disclosing in the report the inability to obtain a representation letter might be used when, for example, the client has hired the practitioner to perform procedures on subject matter that is the responsibility of another party (that is, the client is not the responsible party). By including such a statement in the report, the client will be put on notice that the other party did not provide a representation letter. It is recommended that such a statement be included.]
 - c. Withdraw from the engagement. [This answer is incorrect. When a practitioner has determined that a representation letter is necessary and the client, who is also the responsible party, refuses to provide one, the practitioner should consider the potential risks of being associated with the engagement. Best practices indicate that a refusal to provide a representation letter calls into question the practitioner's ability

to rely on any representations made by the responsible party. Consequently, in most cases, the practitioner should obtain the representation letter or withdraw from the engagement.]

- d. Change the engagement to another type of engagement (for example, a consulting engagement). [This answer is incorrect. If the responsible party's refusal to furnish written representations, the practitioner should consider the effects of that restriction on his or her decision to change the nature of the engagement. If the client, who is also the responsible party, refuses to provide a representation letter, it is recommended that the practitioner withdraw from the engagement.]

REPORTING

Content of the Report

According to AT 201.31, the practitioner's report on an agreed-upon procedures engagement should be in the form of procedures and findings and should include the following elements:

- A title that includes the word "independent."
- An identification of the specified parties.
- Identification of the subject matter (or the assertion related thereto) and the character of the engagement. (The reference to the character of the engagement would be to clarify the purpose of the procedures.)
- Identification of the responsible party.
- A statement that the subject matter is the responsibility of the responsible party.
- A statement that the procedures performed were those agreed to by the specified parties identified in the report.
- A statement that the agreed-upon procedures engagement was conducted in accordance with attestation standards established by the American Institute of Certified Public Accountants.
- 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 the procedures.
- A list of the procedures performed (or a reference to such a listing) and related findings.
- When applicable, a description of any materiality limits agreed to by the specified parties.
- A statement that the practitioner was not engaged to, and did not, conduct an examination of the subject matter. If the practitioner wishes, he or she can also state that a review was not performed. Furthermore, if the subject matter consists of elements, accounts, or items of a financial statement, alternative wording, such as the following, may be used: "We were not engaged to, and did not, perform an audit or a review, the objectives of which would be the expression of an opinion or limited assurance on the [Describe subject matter.]. Accordingly, we do not express such an opinion or limited assurance."
- A disclaimer of opinion on the subject matter.
- 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. The practitioner should refer to the guidance in either AU 504, *Association with Financial Statements*, or SSARS No. 19 for guidance on the practitioner's responsibility for financial statements when he or she consents to the inclusion of the agreed-upon procedures in a document or written communication containing the entity's financial statements.
- A statement restricting the use of the report to the specified parties.
- Where applicable, any reservations or restrictions concerning procedures or findings.
- For agreed-upon procedures engagements related to prospective financial statements, the elements required by AT 301.55. (*PPC's Guide to Forecasts and Projections* discusses engagements related to prospective financial statements.)
- Where applicable, a description of the nature of the assistance provided by a specialist.
- The manual or printed signature of the practitioner's firm.

- The date of the report.

Exhibit 3-1 shows an example report based on the requirements of AT 201.

Exhibit 3-1

Report on Applying Agreed-upon Procedures

INDEPENDENT ACCOUNTANT'S REPORT ON APPLYING AGREED-UPON PROCEDURES

We have performed the procedures enumerated below, which were agreed to by [List specified parties.], solely to assist you in evaluating [Identify the subject matter—for example, the accompanying schedule of investment returns of XYZ Company (prepared in accordance with the criteria specified therein).] for the year ended December 31, 20X1. [Identify responsible party.]'s management is responsible for the [Identify the subject matter.]. This agreed-upon procedures engagement was conducted in accordance with attestation standards established by the American Institute of Certified Public Accountants. The sufficiency of these procedures is solely the responsibility of those parties specified in this report. Consequently, we make no representation regarding the sufficiency of the procedures described below either for the purpose for which this report has been requested or for any other purpose.

[Include paragraphs to enumerate the procedures and findings.]

We were not engaged to, and did not, conduct an examination, the objective of which would be the expression of an opinion on [Identify the subject matter—for example, XYZ Company's schedule of investment returns.]. Accordingly, we do not express such an opinion. Had we performed additional procedures, other matters might have come to our attention that would have been reported to you.

This report is intended solely for the information and use of [List specified parties.] and is not intended to be and should not be used by anyone other than those specified parties.

[Firm Signature]

[Report Date]

* * *

Clearly Distinguishable Reports

AT 201 states that a practitioner who issues the form of report described in the standard is subject to those standards, even if not specifically engaged to perform an attest engagement. The standard warns that a report that looks like an attestation report might be reasonably inferred to be one, causing users to reasonably believe the standards were followed. Therefore, a report not intended to be an attestation report should be *clearly distinguishable* from the standard form of report.

The only guidance provided by the standard on how different the nonattest report (generally, this would mean a consulting report) needs to be is that a report that only excludes the words, “. . . was conducted in accordance with attestation standards established by the American Institute of Certified Public Accountants . . .” may still be inferred to be an attest report. It is believed that, at a minimum, a report that is not intended to be an attestation report (that is, a consulting report) should not:

- Call the service provided an agreed-upon procedures engagement.
- Claim to comply with AICPA standards (unless other standards are clearly identified).

Identifying the Subject Matter

In an agreed-upon procedures engagement, the subject matter may accompany the practitioner's report or it may be presented only in the representation letter. Regardless of how the subject matter is presented, the practitioner's report should both describe the subject matter and clearly indicate that it is the responsibility of the responsible party. Otherwise, the report might imply that the practitioner takes responsibility for it.

Heading the Report

According to AT 201, the title to the practitioner's report should include the word "independent." This is to distinguish the report from representations of the client or the responsible party. Also, the word "independent" in the title emphasizes a characteristic of the practitioner's work that might not otherwise be apparent. Although the example report in AT 201 is titled "Independent Accountant's Report on Applying Agreed-Upon Procedures," it is believed that a title such as "Independent Accountant's Report" would also be appropriate. The term *accountant* is recommended rather than the term *auditor* because it more clearly indicates that the practitioner is not performing an *audit* of the specified elements.

Addressing the Report

Addressing the report is a matter of professional judgment as well as, in certain states, a matter of legal judgment. It is suggested that, as a matter of policy, the report be addressed to the practitioner's client and to the specified parties. If the specified parties are a group of separate entities with common representation for the purpose of determining the practitioner's procedures, such as a creditors' committee, the authors believe that the report may be addressed to a representative of the group that the practitioner dealt with regarding the scope of the engagement (for example, "DDS Corp. as Representative of the Creditors' Committee").

If the client is not the responsible party, the practitioner may, but is not required to, include the responsible party as a specified party. (Note that all specified parties must agree to the procedures.) In most cases, the responsible party will have been provided a draft of the report for its approval of the findings and so will be familiar with the report's content.

Dating the Report

The practitioner's report should be dated as of the date that the agreed-upon procedures are completed.

Nature of the Practitioner's Conclusions

Procedures and Findings. Practitioners should present their conclusions on the results of the agreed-upon procedures in the form of procedures and findings. In describing the procedures performed, practitioners should generally avoid using terms of uncertain meaning such as general review, limited review, check, or test. If such terms must be used, they should be accompanied by an explanation of what procedures are meant by the terms.

In reporting findings, practitioners should exercise care to avoid representations not supported by their work. A statement such as "We have ascertained (found or determined) that the net sales of ABC Company for the year 20X1 were \$XX,XXX," could be considered such a representation. Practitioners are rarely in a position to use terms such as *correct*, *accurate*, and *verify* in a report because that language implies a level of precision that is inconsistent with the level of procedures applied. In addition, the practitioner should be clear and precise and should avoid vague or ambiguous language (for example, the total of the accounts receivable trial balance *approximated* the accounts receivable balance recorded in the company's general ledger). Example findings resulting from the application of specific agreed-upon procedures are presented in Exhibit 3-2.

Exhibit 3-2**Example Findings Resulting from Specific Agreed-upon Procedures**Agreed-upon Procedure

Trace all outstanding checks appearing on the December 31, 20X1 bank reconciliation to checks clearing in the January 20X2 bank statement.

Confirm all accounts receivable balances recorded in the June 30, 20X2 general ledger.

Example Finding

Except for the following, all outstanding checks appearing on the December 31, 20X1 bank reconciliation were cleared in the January 20X2 bank statement:

(List exceptions)

Except for the following, all accounts receivable balances recorded in the June 30, 20X2 general ledger were confirmed with the respective customers without exception:

(List exceptions)

* * *

Reporting All Findings. In reporting findings, the practitioner should report *all* findings detected as a result of the procedures. It is also recommended that a specific finding be provided for *each* procedure. The concept of materiality does not apply unless the specified parties have specifically agreed that the practitioner should report only those amounts exceeding an agreed-upon materiality threshold. In those situations, the report should include a description of any agreed-upon materiality limits.

Providing Negative Assurance

Under AT 201, practitioners are prohibited from providing negative assurance. Instead, the practitioner would express a positive finding for each procedure or include a statement such as “No exceptions were found as a result of applying the procedure.” When possible, it is recommended expressing a positive finding.

One problem with not providing negative assurance is that clients will often ask questions like “Did you find anything else I should know about?” or “Did anything else come to your attention?” To resolve the client’s concern, the practitioner can make it clear, possibly through the engagement letter, that the practitioner’s report will include:

- *All* findings. (See above.)
- Any other matters that come to the practitioner’s attention while performing the procedures. (See guidance below.)

Restricting Use of the Report

AT 101 requires that an agreed-upon procedures report always be restricted. The reason for that restriction is to limit the use of the report to only those parties who agreed to the procedures and took responsibility for the sufficiency of the procedures for their purposes.

Communicating Other Matters

The practitioner need not perform procedures beyond those agreed to by the parties involved (for example, the client and specified parties). If, in connection with the application of the agreed-upon procedures, matters come to the practitioner’s attention by other means that significantly contradict the subject matter, the practitioner should include such matters in his or her report.

For instance, a footnote to AT 201 states that, if the practitioner has audited the financial statements to which the subject matter relates and the auditor's report contains a departure from the standard report, the practitioner should consider including a reference to the report and departure in the agreed-upon procedures report. (Although not discussed, the authors believe that the same considerations would apply had the financial statements to which the subject matter related been audited by another practitioner.)

Deciding whether such matters are important enough to communicate is a matter of professional judgment. It is believed it is generally better to err on the side of conservatism and report any matters that are relevant to the subject matter and might be considered significant to the client or specified parties.

Deciding Whether to Report Such Matters. When considering whether to report matters that come to the practitioner's attention by other means that significantly contradict the subject matter, the authors believe the practitioner may need to consider the source of the information. For example, if other matters come to the practitioner's attention, but the practitioner does not consider the source of the information to be reliable, the practitioner may decide not to follow up on those matters in order to determine whether they should be included in the report. As noted previously, deciding whether such matters are significant enough to communicate is a matter of professional judgment. It is believed it is generally better to err on the side of conservatism and report any matters that are relevant to the subject matter and might be considered significant to the client or specified parties.

Acknowledging Responsibility in the Engagement Letter. Practitioners may wish to state in the engagement letter that they will include in the report other matters that come to their attention. The engagement letter should also state, however, that such disclosures, if any, may not necessarily include all matters which might have come to the practitioners' attention had they performed additional procedures or an examination.

Considering Subsequent Events

The practitioner has no responsibility to perform procedures to detect events occurring subsequent to the date or period covered by the subject matter (unless this is one of the procedures agreed to). However, if the practitioner becomes aware of subsequent events that contradict the subject matter, it is believed this would be considered an other matter (as discussed in the preceding paragraphs), and the practitioner should consider including such information in the report.

Scope Restrictions

Since the specified parties determine the scope of the practitioner's procedures, scope restrictions do not often occur in agreed-upon procedures engagements. However, AT 201 addresses reporting when circumstances impose restrictions on the performance of the agreed-upon procedures.

When the practitioner is unable to perform the procedures agreed to, AT 201 states that the practitioner should attempt to obtain agreement from the specified parties for modification of the procedures. If the practitioner is unable to obtain agreement from the specified parties (for example, when agreed-upon procedures are published by a regulatory agency that will not modify the procedures), the practitioner should describe any restrictions in his or her report or withdraw from the engagement. Modification of the procedures can be accomplished by preparing an addendum to the engagement letter.

It is believed that, in some cases, the restriction on procedures may not be significant enough for the practitioner to pursue modification of the procedures. In those cases, it is believed it would be appropriate to simply describe the restriction(s) in the report.

If the practitioner requests a representation letter, and the responsible party refuses to provide one, the practitioner should consider the refusal to be a limitation on the performance of the engagement. When that occurs, the practitioner should take one of the following actions:

- Disclose in the agreed-upon procedures report the inability to obtain written representations.
- Withdraw from the engagement.
- Change the engagement to another type of engagement (for example, a consulting engagement).

If the client, who is also the responsible party, refuses to provide a representation letter, it is recommended that the practitioner withdraw from the engagement.

Other Explanatory Language

In addition to the matters discussed in the preceding paragraphs, AT 201 lists the following matters for which the practitioner might consider including explanatory language:

- Disclosure of stipulated facts, assumptions, or interpretations (including the source thereof) used in the application of the procedures.
- Description of the condition of records, controls, or data to which the procedures were applied.
- Explanation that the practitioner has no responsibility to update his or her report.
- Explanation of sampling risk. (It is believed that procedures should not refer to a sample. Instead, the specific number of items to be selected should be stated.)

Combined or Included Reports

In some engagements, the practitioner may be requested to apply agreed-upon procedures as part of, or in addition to, another type of service (such as an audit, review, or compilation of financial statements, another attest service, or a consulting engagement). AT 201 states that reports on applying agreed-upon procedures may be combined with reports on other service, as long as the types of services can be clearly distinguishable and the standards for each type of service are followed. AT 101 notes, however, that if practitioners issue a single combined report covering both the agreed-upon procedures and the other service, the use of the single combined report also should be restricted to the use of the specified parties.

Practitioners may also include an agreed-upon procedures report, which is restricted to the use of the specified parties, in a document that contains a general use report (such as an audit report). In that case, the intended use of either report remains unaffected. That is, the restriction in the agreed-upon procedures report would seem to adequately inform intended users of the limitations of the agreed-upon procedures report, and the audit report would be appropriate for general use.

Complete Financial Statements Presented with the Practitioner's Agreed-upon Procedures Report

If the complete financial statements of a public entity are presented in connection with an agreed-upon procedures engagement, the auditor should refer to SAS No. 26, *Association with Financial Statements*, (AU 504) to determine any other reporting responsibilities. SAS No. 26 requires that a disclaimer of opinion (a standard component of an agreed-upon procedures report) be issued when the statements are not audited. Furthermore, it is believed to be appropriate for practitioners to describe the procedures performed, even though SAS No. 26 states that, except in situations involving comfort letters, the report should not describe such procedures applied. However the logic permitting the exception for comfort letters (which is that the underwriters specifically requested the procedures and are, thus, unlikely to misunderstand the auditor's report) applies equally to other agreed-upon procedures engagements.

If the complete financial statements of a nonpublic entity are presented in connection with an agreed-upon procedures engagement, SSARS No. 19 requires the practitioner to compile the financial statements or, if the practitioner has not submitted the financial statements, to ensure that the financial statements are accompanied by an indication that the accountant has not compiled or reviewed them and assumes no responsibility for them.

SELF-STUDY QUIZ

Determine the best answer for each question below. Then check your answers against the correct answers in the following section.

35. Which of the following best describes the practitioner's reporting responsibilities in an agreed-upon procedures report?
- a. In an agreed-upon procedures engagement, the subject matter must accompany the practitioner's report.
 - b. According to AT 201, the title to the practitioner's report may, but is not required to, include the word "independent."
 - c. The practitioner should always address the agreed-upon procedures report only to his or her client, since the client is the one who engaged the practitioner.
 - d. The practitioner's report should be dated as of the date that the agreed-upon procedures are completed.
36. Which of the following findings would a user generally **not** expect to see in a report on agreed-upon procedures performed in accordance with the attestation standards?
- a. All accounts receivable balances recorded in the June 30, 20X2 general ledger were confirmed with the respective customers without exception.
 - b. Except for the following, all inventory quantities were agreed to physical counts as of December 31, 20X2.
 - c. Total per the accounts receivable trial balance approximated the accounts receivable balance recorded in the company's general ledger as of December 31, 20X2.
 - d. Except for the following, all outstanding checks appearing on the December 31, 20X1 bank reconciliation were cleared in the January 20X2 bank statement.
37. Ted Beaman, CPA, intends to present the complete financial statements of ABC Plumbing, Inc. in connection with the agreed-upon procedures report on the privately-held company. Which of the following best describes Beaman's responsibility for those financial statements?
- a. Beaman should refer to SAS No. 26, *Association with Financial Statements*, to determine his reporting responsibilities.
 - b. If Beaman has submitted complete financial statements, he should ensure that the financial statements are accompanied by an indication that the accountant has not compiled or reviewed them and assumes no responsibility for them.
 - c. Beaman should compile the statements in accordance with SSARS No. 19 if he has submitted them in connection with the agreed-upon procedures report.

SELF-STUDY ANSWERS

This section provides the correct answers to the self-study quiz. If you answered a question incorrectly, reread the appropriate material. **(References are in parentheses.)**

35. Which of the following best describes the practitioner's reporting responsibilities in an agreed-upon procedures report? **(Page 104)**
- a. In an agreed-upon procedures engagement, the subject matter must accompany the practitioner's report. [This answer is incorrect. The subject matter may accompany the report or it may be presented in the representation letter. Regardless of how the subject matter is presented, the practitioner's report should both describe the subject matter and clearly indicate that it is the responsibility of the responsible party. Otherwise, the report might imply that the practitioner takes responsibility for it.]
 - b. According to AT 201, the title to the practitioner's report may, but is not required to, include the word "independent." [This answer is incorrect. AT 201 requires use of the word "independent" in the report to distinguish it from representations of the client or the responsible party. Also, the word "independent" in the title emphasizes a characteristic of the practitioner's work that might not otherwise be apparent. Although the example report in AT 201 is titled "Independent Accountant's Report on Applying Agreed-Upon Procedures," it is believed that a title such as "Independent Accountant's Report" would also be appropriate.]
 - c. The practitioner should always address the agreed-upon procedures report only to his or her client, since the client is the one who engaged the practitioner. [This answer is incorrect. Addressing the report is a matter of professional judgment as well as, in certain states, a matter of legal judgment. It is suggested that, as a matter of policy, the report be addressed to the practitioner's client and to the specified parties. If the specified parties are a group of separate entities with common representation for the purpose of determining the practitioner's procedures, such as a creditors' committee, it is believed that the report may be addressed to a representative of the group that the practitioner dealt with regarding the scope of the engagement (for example, "DDS Corp. as Representative of the Creditors' Committee").]
 - d. **The practitioner's report should be dated as of the date that the agreed-upon procedures are completed. [This answer is correct. The practitioner's report should be dated as of the date that the agreed-upon procedures are completed, as required by AT 201.]**
36. Which of the following findings would a user generally **not** expect to see in a report on agreed-upon procedures performed in accordance with the attestation standards? **(Page 104)**
- a. All accounts receivable balances recorded in the June 30, 20X2 general ledger were confirmed with the respective customers without exception. [This answer is incorrect. The practitioner may use language such as this to describe his or her findings in an agreed-upon procedures engagement since such language is clear and unambiguous.]
 - b. Except for the following, all inventory quantities were agreed to physical counts as of December 31, 20X2. [This answer is incorrect. The practitioner may use language such as this to describe his or her findings in an agreed-upon procedures engagement since such language is clear and unambiguous.]
 - c. **Total per the accounts receivable trial balance approximated the accounts receivable balance recorded in the company's general ledger as of December 31, 20X2. [This answer is correct. Use of the word *approximated* in this description is both vague and ambiguous; therefore, it should not be used to describe a practitioner's findings in an agreed-upon procedures report.]**
 - d. Except for the following, all outstanding checks appearing on the December 31, 20X1 bank reconciliation were cleared in the January 20X2 bank statement. [This is the incorrect answer. The practitioner may use language such as this to describe his or her findings in an agreed-upon procedures engagement since such language is clear and unambiguous.]

37. Ted Beaman, CPA, intends to present the complete financial statements of ABC Plumbing, Inc. in connection with the agreed-upon procedures report on the privately-held company. Which of the following best describes Beaman's responsibility for those financial statements? **(Page 107)**
- a. Beaman should refer to SAS No. 26, *Association with Financial Statements*, to determine his reporting responsibilities. [This answer is incorrect. SAS No. 26 applies only if the financial statements are those of a public company. Since the client is a privately-held company, the practitioner's services are governed by SSARS No. 19.]
 - b. If Beaman has submitted complete financial statements, he should ensure that the financial statements are accompanied by an indication that the accountant has not compiled or reviewed them and assumes no responsibility for them. [This answer is incorrect. SSARS No. 19 requires the practitioner to at a minimum compile statements that he has submitted to the client.]
 - c. **Beaman should compile the statements in accordance with SSARS No. 19 if he has submitted them in connection with the agreed-upon procedures report. [This answer is correct. In accordance with SSARS No.19, Beaman should compile the statements if he submitted them in connection with the agreed-upon procedures report.]**

CHANGES IN TYPE OF ENGAGEMENT AFTER COMMENCEMENT

Occasionally, during the course of an engagement, the practitioner may be requested by the client to change the nature of the engagement. The request may be either *to* an agreed-upon procedures engagement (for example, from an audit to an agreed-upon procedures engagement) or *from* an agreed-upon procedures engagement (for example, from an agreed-upon procedures engagement to a consulting engagement). The following paragraphs discuss the practitioner's considerations when this occurs.

Change to an Agreed-upon Procedures Engagement

Occasionally, the practitioner may be requested to change the level of service to an agreed-upon procedures engagement. If the change is from a consulting engagement to an agreed-upon procedures engagement, it is believed the practitioner ordinarily may accommodate the client's request to change the nature of the engagement. Changing from a consulting engagement to an agreed-upon procedures engagement will usually harbor no danger for the practitioner as long as the new engagement is completed according to the standards for agreed-upon procedure engagements (including the requirement that the procedures be appropriate). If, however, the original engagement was to provide some level of assurance (for example, an audit or review), the practitioner should consider the reasons for the change.

A request to change the engagement from an audit or review to an agreed-upon procedures engagement might result from the following:

- A change in circumstances that affects the client's requirements.
- A misunderstanding as to the nature of the original or alternative services that were originally available.
- A restriction on the performance of the original engagement, whether it is imposed by the client or caused by circumstances.

Regardless of the client's reasons for requesting a change in the engagement, if the original engagement procedures are substantially complete or the effort to complete the procedures is relatively insignificant, the practitioner should consider the propriety of the change.

A change in circumstances is ordinarily an acceptable reason for changing to an agreed-upon procedures engagement as long as the users of the report acknowledge agreement to the procedures and accept responsibility for the sufficiency of the procedures.

A misunderstanding of the nature of the various services available is also normally an acceptable reason for a change to an agreed-upon procedures engagement. However, misunderstandings can cause other problems (particularly fee problems), and can often be avoided by making sure the client is aware of the types of services available before the engagement begins.

The implications of a restriction on the performance of the engagement should be considered carefully, including the possibility that the information presented is affected by the restriction and may be incorrect, incomplete, or otherwise unsatisfactory. This evaluation is a matter of professional judgment. If the practitioner has significant concerns after considering the circumstances of the restriction, he or she should not agree to change to an agreed-upon procedures engagement.

Whenever a request is made to change to an agreed-upon procedures engagement, the practitioner should be certain that the specified parties acknowledge agreement to the procedures and assume responsibility for the sufficiency of the procedures. In summary, before agreeing to change the engagement, the practitioner should consider the following:

- Whether procedures performed as part of another type of engagement are appropriate for an agreed-upon procedures engagement.
- The reason for the change in engagement, particularly any restrictions placed on the scope of the original engagement or matters to be reported.

- The additional effort that would be required to complete the original engagement.
- When applicable, any reasons for changing from a general distribution report to a restricted use report.

If, after considering the circumstances, the practitioner agrees to change the engagement to an agreed-upon procedures engagement, the agreed-upon procedures report should *not* make reference to the original engagement or any performance limitations that resulted in the change.

Change to a Consulting Engagement

Occasionally, a practitioner who has been engaged to perform an agreed-upon procedures engagement will, before the completion of the engagement, be requested to change the engagement to a consulting engagement. When this occurs, the practitioner should obtain a clear understanding of the reasons for the request.

If the reason for the request is a restriction placed on the performance of the original engagement (such as the responsible party's refusal to furnish written representations), the practitioner should consider the effects of that restriction on his or her decision to change the nature of the engagement. As noted earlier, if the client, who is also the responsible party, refuses to provide a representation letter, it is recommended that the practitioner withdraw from the engagement.

QUALITY CONTROL AND PEER REVIEWS

Statement on Quality Control Standard No. 7

In October 2007, the ASB issued Statement on Quality Control Standard No. 7, *A Firm's System of Quality Control*, which supersedes and replaces all previously existing SQCSs. SQCS No. 7 establishes standards and provides guidance for a CPA firm's responsibilities, for its system of quality control, and for its accounting and auditing practice.

Paragraph 3 of SQCS No. 7 (QC 10.08) states that the firm "must establish a system of quality control designed to provide the firm with reasonable assurance that the firm and its personnel comply with professional standards and applicable regulatory and legal requirements," and that the firm or engagement partners issue reports that are appropriate in the circumstances. The firm's quality control system consists of policies and procedures.

The purpose of a quality control system is to promote quality in performing accounting and auditing engagements. As the QC standards indicate, a firm's system of quality control is a system designed to provide the firm with reasonable assurance that the firm is (a) complying with professional standards and legal and regulatory requirements, and (b) issuing reports that are appropriate in the circumstances. In developing and maintaining its quality control system, a firm establishes policies designed to achieve the objectives associated with obtaining reasonable assurance and procedures required to implement and monitor compliance with the policies. *Reasonable assurance* is defined as a "high, but not absolute, level of assurance" (SQCS No. 7, paragraph 5).

The nature of the policies and procedures the firm develops to obtain reasonable assurance and comply with the requirements of SQCS No. 7 will depend on various factors, such as the following:

- The size of the firm.
- The operating characteristics of the firm, for example:
 - Types of services provided.
 - Types of industries served.
 - Number of partners.
 - Number of professional personnel.

Major Provisions of SQCS No. 7. SQCS No. 7 was issued to improve the quality of engagement performance. Some of the most important changes to quality control requirements as a result of SQCS No. 7 are as follows:

- The firm must establish a system of quality control designed to provide reasonable assurance that the firm complies with professional standards and issues reports appropriate in the circumstances.
- The firm should document and communicate its quality control policies and procedures.
- The firm's system of quality control encompasses six QC elements, rather than the previous five.
- The firm should promote a quality-oriented internal culture, and firm leadership should assume ultimate responsibility for the firm's system of quality control, including assigning responsibilities so that commercial considerations do not override the objective of the system of quality control.
- The firm is required to establish criteria to determine which engagements (if any) are subject to an engagement quality control review.
- The firm should follow specific requirements relating to dealing with and resolving differences of opinion.
- The firm should establish policies and procedures for dealing with complaints and allegations of noncompliance with professional standards or with the firm's system of quality control.

Professional Requirements. SQCS No. 7 establishes requirements regarding the firm's degree of responsibility it has in complying with the requirements of the standard. The firm's professional requirements, as defined in the standard, are designated into two categories—

- *Unconditional Requirements.* Unconditional requirements are those the firm must follow in all cases if the circumstances apply to the requirement. These requirements use the words *must* or *is required*.
- *Presumptively Mandatory Requirements.* Firms are also expected to comply with presumptively mandatory requirements if the circumstances apply to the requirement; however, in rare situations, a departure from the requirement is allowed if the firm documents the justification and how alternative procedures that were performed were sufficient to achieve the objectives of the requirement. Presumptively mandatory requirements are identified by the word *should*. If the SQCS uses the words *should consider* for a procedure, the consideration of the procedure is presumptively required.

Elements of a Quality Control System. SQCS No. 7 (QC 10.14) states that the firm's system of quality control should incorporate policies and procedures that address each of the following QC elements:

- *Leadership Responsibilities for Quality within the Firm (tone at the top).* The firm has policies and procedures to promote an internal culture, which is based on the recognition that quality is essential in performing engagements.
- *Relevant Ethical Requirements.* The firm and its personnel comply with relevant ethical requirements.
- *Acceptance and Continuance of Client Relationships and Specific Engagements.* The firm undertakes or continues only client relationships and engagements in which the firm (a) considers the client's integrity and the risks associated with performing the client engagement; (b) determines the firm has the competence, capabilities, and resources to perform the engagement; and (c) determines the firm can comply with legal and ethical requirements.
- *Human Resources.* The firm has sufficient personnel with the capabilities, competence, and commitment to ethical principles to (a) perform engagements in accordance with professional standards and legal and regulatory requirements, and (b) enable the firm to issue reports that are appropriate in the circumstances.
- *Engagement Performance.* Work performed by engagement personnel consistently complies with applicable professional standards and regulatory requirements, and that the firm issues reports that are appropriate in the circumstances.
- *Monitoring.* The policies and procedures established by the firm for the other elements of quality control are (a) relevant and adequate, (b) operating effectively, and (c) consistently in compliance.

Documentation and Communication of the Firm's QC Policies and Procedures. One of the most significant changes to the QC standards relates to documentation. QC 10.12 states that the firm should document its QC policies and procedures. However, matters such as the nature of the firm's practice, its size, and its structure may be considered in determining the *extent* of documentation of the firm's QC policies and procedures. Documentation of the policies and procedures of a single-office firm with a small number of partners and staff might not be expected to be as extensive as those of a large, multi-office firm.

SQCS No. 7 does not require the firm to have a formal quality control policies and procedures *document*; instead, the standard indicates only that the firm's QC policies and procedures be *documented*. SQCS No. 7 allows the firm to have flexibility and latitude in determining the documentation method that best suits their individual practice and circumstances.

In addition to documenting its QC policies and procedures, QC 10.13 states that the firm should communicate its QC policies and procedures to firm personnel. That communication is not required to be in writing, although written communication is preferable. An effective firm communication of its QC policies and procedures, as described in paragraph 13 of SQCS No. 7, incorporates the following:

- A description of the policies and procedures and the objectives they achieve.
- A message that each person is responsible for maintaining quality, as well as being familiar with the policies and procedures and complying with them.
- Comments stressing the importance of receiving feedback on how the QC system is operating and encouraging staff to communicate their concerns on quality control issues.

This practice monitoring requirement is applicable to firms that have a compilation and review practice, as well as firms that have an accounting and auditing practice, and requires those firms to undergo a peer review at least once every three years. As a result, such firms must have in place a quality control system that will withstand such a review or risk termination of firm membership in the program, individual memberships in the AICPA, and, in some states, loss of their licenses to practice.

Quality control materials consist of programs, checklists, sample confirmation letters, and other practice aids. When designing the firm's quality control policies and procedures, the firm should indicate the QCM that are being used, or make reference to the firm's accounting manuals that contain the firm's QCM.

In 2007, the AICPA issued guidance for developing QC policies and procedures in its Practice Aid, *Establishing and Maintaining a System of Quality Control for a CPA Firm's Accounting and Auditing Practice* (the AICPA Practice Aid). The AICPA Practice Aid, revised for the issuance of SQCS No. 7, provides illustrative examples of various types of policies and procedures a firm should consider when developing its system of quality control under the guidelines of SQCS No. 7. Illustrative examples of quality control documents are provided for four hypothetical firms varying in size, as follows:

- Firm with multiple offices.
- Single office firm.
- Sole practitioner.
- An alternative practice structure.

The AICPA Practice Aid is not authoritative and only presents the recommendations of the AICPA Quality Control Standards Task Force on the applicability of the new standard. Even so, the AICPA Practice Aid may be a good resource for use by the firm when drafting its QC policies and procedures. The AICPA Practice Aid can be downloaded, free of charge, at www.aicpa.org/InterestAreas/PeerReview/Resources/practiceaids/downloadabledocuments/QCPractAid.pdf.

SQCS No. 7 Redrafted for Clarity and Convergence. In June 2009, the Auditing Standards Board (ASB) issued a proposed SQCS, *A Firm's System of Quality Control (Redrafted)*. The exposure draft revised SQCS No. 7 to apply

the ASB's clarity drafting conventions (discussed in more detail beginning at paragraph 102.73) and to converge with International Standards on Quality Control No. 1, *Quality Control For Firms That Perform Audits and Reviews Of Financial Statements, And Other Assurance And Related Services Engagements* (ISQC).

At its July 2010 meeting, the ASB agreed to ballot on the issuance of a final SQCS No. 7, *A Firm's System of Quality Control (Redrafted)*, that, when effective, would supersede SCQS No. 7 of the same name. The new Statement is applicable to a firm's system of quality control for its accounting and auditing practice as of January 1, 2012.

The provisions of the redrafted quality standard do not significantly change or expand current guidance. For example, various presumptively mandatory requirements have been moved to the application and other explanatory material section of the revised standard. In addition, considerations specific to governmental entities have been added to the application and other explanatory material section for several quality control elements. However, some of the more-than-minor provisions of the new standard would require—

- The firm to consider whether other matters or circumstances exist within the firm that require it to establish additional policies and procedures to satisfy the objective of the quality control standard—even when a firm has complied with the stated requirements of the revised QC standard.
- Adding network firm personnel as others who may be subject to independence requirements.
- Additional information regarding assembly, retention, and ownership of final engagement documentation.
- That conclusions relating to consultation should be understood by the individuals seeking and providing the consultation.
- The firm to establish policies and procedures setting out the nature, timing, and extent of an engagement quality control review.
- Replacement of the engagement quality control reviewer when the reviewer's ability to perform an objective review is likely to have been impaired.
- The firm to establish quality control policies and procedures to appropriately address during monitoring the identification of an inappropriate report or the omission of engagement performance procedures.
- Firms with network affiliations that use common monitoring procedures to have additional policy and procedure requirements.
- Supervision of the investigation of complaints and allegations be performed by a partner with sufficient and appropriate experience and authority within the firm.

Future editions of this course will update for the final revisions to the quality control guidance.

Redrafted Quality Control Audit Guidance. In June 2009, the ASB also issued an exposure draft, *Quality Control for an Audit of Financial Statements*, which would supersede SAS No. 25, *The Relationship of Generally Accepted Auditing Standards to Quality Control Standards*, when final. As with SQCS No. 7, SAS No. 25 is being redrafted to apply the ASB's clarity drafting conventions and to converge with the ISQC. At its August, 2010 meeting, the ASB agreed to ballot on the issuance of a final SAS retitled *Quality Control for an Engagement Conducted in Accordance with Generally Accepted Auditing Standards*. The new standard is effective for audits of financial statements for periods beginning on or after December 15, 2012. Selected provisions of the revised SAS would provide that—

- Audit engagement teams have a responsibility, as it relates to the firm's system of quality control, to implement quality control procedures that apply to the audit engagement and provide the firm with relevant information that enables the functioning of the firm's quality control system relating to independence.
- The audit engagement partner should assume the responsibility to ensure the overall quality of each audit engagement to which he or she is assigned.

- The audit engagement partner has additional responsibilities regarding independence, including forming a conclusion about compliance with independence requirements that apply to the engagement.
- The audit engagement partner should be satisfied that appropriate procedures regarding acceptance and continuance of client relationships and specific engagements have been followed and appropriate conclusions have been reached and documented.
- The audit engagement partner should be satisfied that the entire engagement team has appropriate competence and capabilities to perform the audit engagement as required by professional standards and applicable legal and regulatory requirements.
- Responsibility be placed on the audit engagement partner to (a) ensure that appropriate consultation is undertaken and (b) be satisfied that the conclusions resulting from consultation are understood by the party consulted and that the conclusions are implemented.
- The audit engagement partner has responsibility related to assuring the proper performance of an EQCR when EQCR is required for an audit engagement.
- The audit engagement partner should consider whether any deficiencies noted in communications regarding the results of the firm's monitoring process may affect the audit engagement.

AICPA Peer Review Standards

Applicability of Peer Review Requirements. AICPA Bylaw 2.2, *Requirements for Admission to Membership*, defines the criteria that persons must possess to qualify for membership in the AICPA. Bylaw 2.2.3 states:

With respect to those persons who are engaged in the practice of public accounting as an owner or as an employee who has been licensed as a CPA for more than two years, either they are practicing in a firm that is enrolled in an Institute-approved practice-monitoring program if the services performed by such a firm are within the scope of the AICPA's practice-monitoring standards and the firm issues reports purporting to be in accordance with AICPA professional standards, or if authorized by council, are themselves enrolled in such a program.

Basically, that bylaw requires accountants who are AICPA members to enroll in a practice monitoring program when they (a) perform services covered by peer review and (b) issue reports in accordance with professional standards.

Revisions to the Peer Review Standards. In May 2008, the AICPA Peer Review Board issued revised *Standards for Performing and Reporting on Peer Reviews* (Peer Review Standards) and Interpretations. The revised Peer Review Standards supersede all existing Peer Review Standards and Interpretations and are effective for peer reviews commencing on or after January 1, 2009. The new Peer Review Standards are more principles-based, with detailed guidance provided in the Interpretations. All peer review guidance has been reevaluated, reengineered, updated, and clarified. Some of the more significant changes include:

- Revamping the language of system and engagement review reports to make them shorter and more concise. The *standard*, *modified*, and *adverse* reports have been replaced with pass, pass with deficiencies, and fail reports.
- Incorporating SQCS No. 7 throughout the new Peer Review Standards and Interpretations.
- Folding report reviews into engagement reviews while maintaining several attributes of the report review process, and making other revisions to engagement reviews.
- Eliminating the letter of comments as a means to communicate matters not deemed to be significant.
- Making various changes to the engagement review process and documentation.

- Allowing, under specified circumstances, the new Peer Review Standards to be used by certain approved administering entities to administer peer review of non-AICPA firms.
- Making changes to reviewer training and resume requirements.
- Adding the concept of a review team assessing its “capability” to perform a peer review.
- Clarifying the information to be included in the reviewed firm’s representation letter.
- Incorporating guidance for performing and reporting on peer reviews of QCM and CPE programs.

The Peer Review Standards and Interpretations are located in the AICPA Peer Review Program Manual at Sections 1000 and 2000, respectively. The guidance is also currently available on the AICPA website at www.aicpa.org/download/practmon/2009_std.pdf.

Types of Reviews. The revised Peer Review Standards provide for two types of reviews: a system review and an engagement review. Firms that perform audit engagements under the SASs or Government Auditing Standards, examinations of prospective financial statements under the SSAEs, or audits of non-SEC issuers performed under the standards of the PCAOB are required to have a system review every three years. Firms that have an accounting and auditing practice, as defined by the Peer Review Standards, but do not perform the types of engagements that require a system review and instead perform only services under the SSARS or the SSAEs (excluding examinations of prospective financial statements), are required to have an engagement review every three years, but may elect to have a system review. Firms that do not perform any of these services are not required to undergo peer review. The following paragraphs provide a brief summary of the objectives of system reviews and engagement reviews. Practitioners should refer to PPC’s Guide to Quality Control for detailed guidance on the peer review standards.

System Reviews. The Peer Review Standards, Paragraph 37, state that “a system review is designed to test a reasonable cross-section of the firm’s engagements with a focus on high-risk engagements, in addition to significant risk areas where the possibility exists of engagements not being performed and/or reported on in conformity with applicable professional standards in all material respects.” A system review does not test every engagement or compliance with every professional standard.

The objectives of system reviews are as follows:

- The reviewed firm’s system of quality control for its accounting and auditing practice has been designed in accordance with quality control standards established by the AICPA.
- The reviewed firm’s quality control policies and procedures were being complied with in order to provide the firm with reasonable assurance of performing and reporting in conformity with applicable professional standards in all material respects.

Engagement Reviews. The Peer Review Standards state, “The objective of an engagement review is to evaluate whether engagements submitted for review are performed and reported on in conformity with applicable professional standards in all material respects. An engagement review consists of reading the financial statements or information submitted by the reviewed firm and the accountant’s report thereon, together with certain background information and representations and, except for compilation engagements performed under SSARS, the applicable documentation required by professional standards.”

The peer reviewer does not attempt to evaluate the adequacy of the firm’s quality control system. Consequently, engagement reviews do not involve a test of administrative or personnel files, personnel interviews, or other non-engagement procedures performed in system reviews. Since an engagement review does not evaluate the firm’s system of quality control, an engagement review report is very different from a system review report, which expresses an opinion on the firm’s QC system. The engagement review report provides assurance only on the firm’s engagements.

Applicability of Peer Review and Quality Control Standards to AUP Engagements. Under the peer review standards, firms that perform agreed-upon procedures engagements are subject to an engagement review unless

they also have performed any of the engagements that would require them to have a system review, as previously discussed. Such firms also are subject to the requirements of the Statement on Quality Control Standard No. 7, which requires firms to establish quality control systems. It is recommended that a firm's quality control system cover all types of accounting, auditing, and attestation services, including agreed-upon procedures engagements.

Common Deficiencies Noted in Peer Reviews

The AICPA's Peer Review Board in its "Annual Report on Oversight," lists examples of noncompliance with applicable AICPA Professional Standards that have been noted on peer reviews. The report lists two significant engagement deficiencies related to attestation procedures and documentation:

- Failing to clearly identify the responsible party and/or failure to have the responsible party accept responsibility for its assertions or subject matter.
- Failing to appropriately label pro forma financial information to distinguish it from historical financial information.

The Board's report lists many other deficiencies, including those found on audit, review, or compilation engagements and those applicable to specific industries. The report can be found at www.aicpa.org/InterestAreas/Peer-Review/Resources/Transparency/Oversight/DownloadableDocuments/AICPA%202009%20Annual%20Report%20on%20Oversight.pdf.

SELF-STUDY QUIZ

Determine the best answer for each question below. Then check your answers against the correct answers in the following section.

38. Occasionally, during the course of an engagement, the practitioner may be requested by the client to change the nature of the engagement. If the change is to an agreed-upon procedures engagement, which of the following statements is correct?
- a. Changing from a consulting engagement to an agreed-upon procedures engagement will usually harbor no danger for the practitioner as long as the new engagement is completed according to the standards for agreed-upon procedure engagements (including the requirement that the procedures be appropriate).
 - b. If the original engagement involved providing some level of assurance (for example, an audit or review), there is no problem with the change to an agreed-upon procedures engagement, regardless of the reason for the change.
 - c. A change in circumstances is ordinarily not an acceptable reason for changing to an agreed-upon procedures engagement, even when the users of the report acknowledge agreement to the procedures and accept responsibility for the sufficiency of the procedures.
39. Which of the following statements regarding the revisions to the Peer Review Standards is correct?
- a. About 50% of the existing Peer Review Standards and Interpretations will be superseded by the AICPA Peer Review Board's revised *Standards for Performing and Reporting on Peer Reviews*.
 - b. One significant change to the Standards is eliminating SQCS No. 7 throughout the new Peer Review Standards and Interpretations.
 - c. The new Peer Review Standards and Interpretations removed the letter of comments as a means to communicate matters not deemed to be significant.
 - d. One significant change to the Standards is removing all reviewer training and resume requirements.
40. One of the types of reviews described in the *Standards for Performing and Reporting on Peer Reviews* is a system review. Which of the following statements about a system review is **not** correct?
- a. The objective of a system review is to provide the reviewer with a reasonable basis for expressing limited assurance that the financial statements or information and the related accountant's reports submitted for review conform in all material respects with the requirements of the applicable professional standards.
 - b. The system review is required for firms that perform engagements under SASs, Government Auditing Standards, and/or examinations of prospective financial statements under the SSAEs.
 - c. Firms that are not required to have a system review may still elect to have one.
 - d. The objective of a system review is to provide the reviewer with a reasonable basis for expressing an opinion on the design and compliance of the firm's system of quality control for its accounting and auditing practice.

SELF-STUDY ANSWERS

This section provides the correct answers to the self-study quiz. If you answered a question incorrectly, reread the appropriate material. **(References are in parentheses.)**

38. Occasionally, during the course of an engagement, the practitioner may be requested by the client to change the nature of the engagement. If the change is to an agreed-upon procedures engagement, which of the following statements is correct? **(Page 112)**
- a. **Changing from a consulting engagement to an agreed-upon procedures engagement will usually harbor no danger for the practitioner as long as the new engagement is completed according to the standards for agreed-upon procedure engagements (including the requirement that the procedures be appropriate). [This answer is correct. If the change is from a consulting engagement to an agreed-upon procedures engagement, it is believed the practitioner ordinarily may accommodate the client's request to change the nature of the engagement. The practitioner must make sure that the new engagement is completed according to the standards.]**
 - b. If the original engagement involved providing some level of assurance (for example, an audit or review), there is no problem with the change to an agreed-upon procedures engagement, regardless of the reason for the change. [This answer is incorrect. If the original engagement was to provide some level of assurance (for example, an audit or review), the practitioner should consider the reasons for the change. Reasons for the change might include (a) a change in circumstances that affects the client's requirements; (b) a misunderstanding as to the nature of the original or alternative services that were originally available; or (c) a restriction on the performance of the original engagement, whether it is imposed by the client or caused by circumstances. Regardless of the client's reasons for requesting a change in the engagement, if the original engagement procedures are substantially complete or the effort to complete the procedures is relatively insignificant, the practitioner should consider the propriety of the change.]
 - c. A change in circumstances is ordinarily not an acceptable reason for changing to an agreed-upon procedures engagement, even when the users of the report acknowledge agreement to the procedures and accept responsibility for the sufficiency of the procedures. [This answer is incorrect. A change in circumstances is ordinarily an acceptable reason for changing to an agreed-upon procedures engagement as long as the users of the report acknowledge agreement to the procedures and accept responsibility for the sufficiency of the procedures.]
39. Which of the following statements regarding the revisions to the Peer Review Standards is correct? **(Page 117)**
- a. About 50% of the existing Peer Review Standards and Interpretations will be superseded by the AICPA Peer Review Board's revised Standards for Performing and Reporting on Peer Reviews. [This answer is incorrect. In May, 2008, the AICPA Peer Review Board issued revised Standards for Performing and Reporting on Peer Reviews (Peer Review Standards) and Interpretations which supersedes all existing Peer Review Standards and Interpretations effective for peer reviews commencing on or after January 1, 2009.]
 - b. One significant change to the Standards is eliminating SQCS No. 7 throughout the new Peer Review Standards and Interpretations. [This answer is incorrect. The revisions incorporate SQCS No. 7 throughout the new Peer Review Standards and Interpretation, not eliminate it.]
 - c. **The new Peer Review Standards and Interpretations removed the letter of comments as a means to communicate matters not deemed to be significant. [This answer is correct. All peer review guidance has been reevaluated, reengineered, updated, and clarified. One of the changes includes eliminating the letter of comments as a means to communicate matters not deemed to be significant.]**
 - d. One significant change to the Standards is removing all reviewer training and resume requirements. [This answer is incorrect. One revision to the Peer Review Standards is changing the reviewer training and resume requirements; not eliminating them.]

40. One of the types of reviews described in the *Standards for Performing and Reporting on Peer Reviews* is a system review. Which of the following statements about a system review is **not** correct? **(Page 118)**
- a. **The objective of a system review is to provide the reviewer with a reasonable basis for expressing limited assurance that the financial statements or information and the related accountant's reports submitted for review conform in all material respects with the requirements of the applicable professional standards. [This answer is correct. This is one objective of an engagement review. Another is to provide the reviewer with a reasonable basis for expressing limited assurance that the reviewed firm's documentation conforms in all material respects with professional standards.]**
 - b. The system review is required for firms that perform engagements under SASs, Government Auditing Standards, and/or examinations of prospective financial statements under the SSAEs. [This answer is incorrect. Firms that perform these types of engagements are subject to a system review.]
 - c. Firms that are not required to have a system review may still elect to have one. [This answer is incorrect. A firm may elect to have a system review even if it is not required to do so.]
 - d. The objective of a system review is to provide the reviewer with a reasonable basis for expressing an opinion on the design and compliance of the firm's system of quality control for its accounting and auditing practice. [This answer is incorrect. These are the objectives of a system review per the Peer Review Standards.]

EXAMINATION FOR CPE CREDIT**Lesson 3 (NTETG101)**

Determine the best answer for each question below. Then mark your answer choice on the Examination for CPE Credit Answer Sheet located in the back of this workbook or by logging onto the Online Grading System.

22. Bob Jones, CPA, has been engaged by Boston Pizza Corp. to perform an agreed-upon procedures engagement. In addition to Boston Pizza Corp, ABC Bank is another specified party of the engagement. Since both specified parties must agree with Bob Jones about the procedures to be performed, Bob Jones attempts to communicate directly with both of them. Although he is able to obtain an engagement letter from his client, Boston Pizza, he is unable to communicate directly with ABC Bank. In this case, Bob Jones decides to apply certain alternative procedures. Which of the following is **not** an appropriate alternative procedure Bob Jones could apply?
- a. Compare the procedures to be applied to written requirements of ABC Bank.
 - b. Compare the procedures to be applied to those applied in similar agreed-upon procedures engagements.
 - c. Discuss the procedures to be applied with appropriate representatives (such as legal counsel) of ABC Bank.
 - d. Review relevant contracts with or correspondence from ABC Bank.
23. In an agreed-upon procedures engagement, SSAE No. 10 *requires* the practitioner to obtain an understanding with the client about which of the following matters?
- a. Subject matter to which procedures are to be applied.
 - b. Identification of criteria.
 - c. Practitioner's responsibilities in the engagement.
 - d. Disclaimers expected to be included in report.
24. Which of the following statements regarding matters that a practitioner should consider when discussing with the client and including in the engagement letter is most accurate?
- a. The practitioner should only consider the engagement when the client is the responsible party.
 - b. The agree-upon procedures report should be reviewed by any specified parties who have agreed to the criteria.
 - c. Understanding which subject matter should be reported on can be used to determine if the practitioner has enough experience to perform the engagement.
 - d. The practitioner is not allowed to assist the client in developing the subject matter.

25. Because of the evolving nature of an agreed-upon procedures engagement, it is not uncommon for the terms to be revised before the engagement is completed. Which of the following is recommended when the terms of an agreed-upon procedures engagement are modified while the engagement is in process?
- a. The practitioner should obtain oral agreement from the specified parties for the modification.
 - b. Unless the practitioner obtains written agreement for the modifications from the specified parties, the practitioner cannot agree to the changes.
 - c. One way to document the specified parties' agreement to the modifications is to obtain a new engagement letter.
 - d. When circumstances arise that restrict the performance of the agreed-upon procedures, the practitioner must withdraw from the engagement.
26. Rockfish Restaurant engages the services of John Able, CPA, to provide agreed-upon procedures on certain balance sheet items for purposes of ensuring compliance with specific loan covenants for ABC Bank. After the engagement begins, Rockfish management requests the CPA to add City Bank as a specified user of the engagement. In that case, which of the following best describes what the practitioner can do in this situation?
- a. The practitioner may add City Bank as a specified party as long as Rockfish Restaurant makes the request in writing.
 - b. Although the practitioner is unable to add City Bank as a specified party after the engagement has begun, he can provide them with a copy of his report.
 - c. The practitioner may add City Bank as a specified party as long as he receives affirmative acknowledgment from them agreeing to the procedures performed and taking responsibility for their sufficiency.
 - d. The practitioner cannot add City Bank as a specified party unless he obtains written agreement from ABC Bank.
27. Which of the following best describes what a practitioner should do when planning an agreed-upon procedures engagement?
- a. The practitioner should determine whether he or she has adequate knowledge of the subject matter. If the practitioner does not have adequate knowledge, he or she cannot begin the engagement.
 - b. The practitioner should obtain an adequate understanding of the requested procedures to ensure that no outside personnel will be necessary to complete the engagement.
 - c. Generally, the practitioner can assign staff members to perform most, if not all, of the engagement since the firm is not providing assurance on the subject matter.
 - d. The staffing of an agreed-upon procedures engagement will depend on the specific nature of each engagement and on each firm's own quality control policies.
28. Frank Best, CPA, was engaged by Coal Vines Creamery to perform an agreed-upon procedures engagement. As part of obtaining the understanding with the client, Frank sat down to discuss the objectives of the engagement and the types of procedures that would be performed to best achieve them. Frank and Coal Vines management agreed to all of the procedures except one. Which of the following would be **inappropriate** for Frank to perform?
- a. Confirming accounts receivable balances with customers.
 - b. Inspecting sales journals for evidence of transactions with certain customers.
 - c. Reconciling the company's cash accounts.
 - d. Performing mathematical computations on the sales journal.

29. Which of the following best describes the practitioner's responsibility for sampling in an agreed-upon procedures engagement?
- a. The responsibility for determining sample sizes in an agreed-upon procedures engagement lies with the specified parties of the report.
 - b. The practitioner is responsible for calculating sample sizes.
 - c. It is common to use statistical sampling methods in an agreed-upon procedures engagement.
 - d. The engagement letter should clarify that the practitioner will calculate scopes and sample sizes.
30. Which of the following best describes the practitioner's responsibility for subsequent events in an agreed-upon procedures engagement?
- a. AT 101 states that the practitioner has the responsibility to detect events occurring after the date of the subject matter (or assertion) that might affect it.
 - b. The practitioner is required to ask the responsible party (and the client, if it is not the responsible party) about whether it is aware of any events that occurred between the date of the subject matter or assertion and the date of the practitioner's report that contradict the subject matter or assertion.
 - c. It is not necessary for the practitioner to include a representation about subsequent events in the representation letter, if the practitioner decides to obtain one.
 - d. If the practitioner becomes aware of subsequent events, he or she should communicate them to the client and, between them, agree whether to include them in the practitioner's report.
31. Sara Smith, CPA, has been engaged by Sofine Carpets to perform an agreed-upon procedures engagement. In performing that engagement, internal auditors and other client personnel will assist Sara by preparing schedules, accumulating information, or performing other clerical tasks. What is Sara's responsibility for working with client personnel?
- a. The practitioner may take responsibility for any portion of the internal auditors' procedures by reporting on those procedures as if they were performed by the practitioner.
 - b. The practitioner's may use work performed by client personnel as long as the practitioner takes joint responsibility for the procedures performed by internal auditors in his or her report.
 - c. The practitioner should read the internal auditor's report for the sole purpose of describing or repeating the internal auditor's procedures in the practitioner's report.
 - d. The procedures enumerated in the practitioner's report should be performed solely and entirely by the practitioner.
32. When reviewing workpapers, who is generally responsible for performing the supervisory review?
- a. Practitioner.
 - b. Senior accountant.
 - c. Assistant.
 - d. Partner.

33. The process designed to provide an objective evaluation by individuals who are not members of the engagement team, of the significant judgments the engagement team made and the conclusions reached in formulating the report is considered which of the following?
- a. Compilation review.
 - b. Analytical review.
 - c. Engagement quality control review.
 - d. Peer review.
34. Which of the following statements best describes the practitioner's responsibility to obtain a representation letter in an agreed-upon procedures engagement?
- a. AT 201 requires the practitioner to obtain a representation letter from the responsible party.
 - b. While AT 201 does not require the practitioner to obtain a representation letter in an agreed-upon procedures engagement, obtaining one is recommended.
 - c. When the client is not the responsible party, it is not necessary for the practitioner to consider obtaining a representation letter from the client.
 - d. AT 201 indicates the representation letter should be dated as of the date of the practitioner's report.
35. The partner in charge of Brennan CPAs has asked Nick Jones, senior accountant, to prepare a first draft of the agreed-upon procedures report on Moo Ice Cream, Inc. Which of the following statements would Nick **not** include in the draft of that report?
- a. A title that includes the word "independent."
 - b. An identification of the responsible party.
 - c. A statement that the practitioner's responsibility is to express an opinion on the subject matter.
 - d. A statement that the subject matter is the responsibility of the responsible party.
36. AT 201 states that a practitioner who issues the form of report described in the standard is subject to those standards, even if not specifically engaged to perform an attest engagement. Therefore, a report not intended to be an attestation report should be clearly distinguishable from the standard form of report. Which of the following statements is correct about a nonattest report?
- a. A nonattest report should not include a paragraph listing the specified parties.
 - b. A consulting report should include a reference to the practitioner's compliance with Statements on Standards for Consulting Services.
 - c. A consulting report may call the service provided an agreed-upon procedures engagement as long as it does not also include a reference to the attestation standards.
 - d. A report that is not intended to be an attestation report should not claim to comply with AICPA standards (unless other standards are clearly identified).

37. AT 201 contains specific guidance on how practitioners should present their conclusions on the results of the agreed-upon procedures in their report. Which of the following best describes that guidance?
- a. In describing the procedures performed, practitioners should generally use terms of uncertain meaning such as *general review*, *limited review*, *check*, or *test*.
 - b. In reporting findings, practitioners may use any term they wish to describe their procedures and the resulting findings.
 - c. The concept of materiality does not apply unless the specified parties have specifically agreed that the practitioner should report only those amounts exceeding an agreed-upon materiality threshold. In those situations, the report should include a description of any agreed-upon materiality limits.
 - d. In reporting findings, the practitioner is required to report only selected findings detected as a result of the procedures.
38. When a client makes a request to change from another engagement to an agreed-upon procedures engagement, the practitioner may grant that change as long as **all but which** of the following conditions are met?
- a. The specified parties must acknowledge agreement to the procedures and assume responsibility for the sufficiency of the procedures.
 - b. The procedures performed as part of the other engagement are appropriate for an agreed-upon procedures engagement.
 - c. The original engagement procedures are substantially complete or the effort to complete the procedures is relatively insignificant.
 - d. There are valid reasons for changing from a general distribution report to a restricted use report.
39. Which of the following best describes a request for a change to or from an agreed-upon procedures engagement?
- a. If a practitioner agrees to change an engagement to an agreed-upon procedures engagement, the agreed-upon procedures report may include a reference to the original engagement.
 - b. If the reason for the request is a restriction placed on the performance of the original engagement, the practitioner should consider the effects of that restriction on his or her decision to change the nature of the engagement.
 - c. If the responsible party's refusal to furnish written representations in the original engagement is the reason for the change, the practitioner may perform the engagement as long as the responsible party is the client.
 - d. The agreed-upon procedures report should describe any performance limitations that resulted in the change from a consulting engagement.
40. The engagement review is for firms that are not required to undergo a system review and do not qualify for a report review. Which of the following statements about an engagement review is **not** correct?
- a. Firms subject to an engagement review are those that perform SSARS compilations of financial statements that do not omit substantially all disclosures required by GAAP, SSARS reviews, or services under SSAEs (except those that are subject to a system review).
 - b. An engagement review provides a basis for expressing assurance on the firm's quality control system.
 - c. One of the objectives of an engagement review is ensure that the reviewed firm's documentation conforms in all material respects with professional standards.
 - d. An engagement review does not involve the review of any other workpapers the reviewed firm may have prepared that are not required by professional standards.

GLOSSARY

Acquisition assistance: A term used to describe engagements in which a practitioner is asked to assist a client in looking over a prospective target.

Agreed-upon procedures engagement: One in which a practitioner is engaged by a client to perform specific procedures and report findings. The practitioner does not perform an audit or provide an opinion relating to the subject matter or assertion about the subject matter. Rather the practitioner performs only those procedures that have been agreed to and reports findings.

ASB clarity project: ASB in October, 2007 announced a large-scale “clarity” project to revise its auditing standards and make them easier to read and understand.

Assertion: Any declaration or set of related declarations about whether the subject matter is based on or in conformity with the criteria selected.

AT 101, Attestation Standards: The umbrella standard that governs all types of attestation engagements, of which there are three: examinations, reviews, and agreed-upon procedures engagements.

AT 201, Agreed-upon Procedures Engagements: The specific guidance on performing agreed-upon procedures engagements.

Attestation interpretations: Recommendations on applying the SSAEs in specific circumstances.

Attestation standards: Consist of the 11 general, field work, and reporting standards and Statements on Standards for Attestation Engagements (SSAEs) issued by the AICPA's Auditing Standards Board (ASB).

Business risk: The risk that an action or event will adversely affect an organization's ability to successfully achieve its objectives and execute its strategies.

Code of Professional Conduct: ET 91.02 and ET 92.11 applies to all professional services the practitioner provides while holding out as a CPA, except for very limited exceptions.

Criteria: The subject matter must have an objective parameter by which it is measured—this basis is called the criteria.

Engagement review: This is for firms that are not required to undergo a system review and do not qualify for a report review. It is for firms that perform SSARS compilations of financial statements that do not omit substantially all disclosures required by GAAP, SSARS reviews, or services under SSAEs.

Financial statement: Something that looks like a financial statement, but is not a tax return.

Hold out as a CPA: A practitioner holds out as a CPA if he or she informs others of his or her status as a CPA or AICPA-accredited specialist.

Nontraditional engagement: Any engagement other than the traditional compilation, review, or audit of financial statements.

Other attestation publications: Have no authoritative status but may help practitioners understand and apply the SSAEs.

Performance measurement: A process of considering whether a client's performance measures are consistent with its overall business strategy.

Presumptively mandatory requirements: Those that a practitioner is expected to comply with if the circumstances apply to the requirement. If the requirement uses the words *should consider* for a procedure, the consideration of the procedure is presumptively required.

Report review: A review for firms (or individual CPAs in non-CPA-owned firms) that perform only SSARS compilations of financial statements that omit substantially all disclosures required by GAAP.

Responsible party: Someone, other than the practitioner, who takes responsibility for the subject matter. Generally, this is the management of the entity whose subject matter is being measured. Generally the responsible party is a group, rather than an individual. It can be the client, but need not be.

Risk assessment standards: The ASB in March 2006 issued eight new statements on auditing standards (SAS Nos. 104–111) related to the auditor's risk assessment process.

Safeguards: Controls that mitigate or eliminate threats to independence.

Specified party: Third parties such as banks, regulatory agencies, prospective investors, and prospective purchasers who may ask for enhanced credibility of client provided information. In many cases, the client is also a specified party.

Subject matter: What the engagement is made about. What the practitioner applies procedures to.

Submitting financial statements: Presenting to a client or third parties financial statements that the practitioner has prepared either manually or through the use of computer software.

System review: A review that is required for firms that perform engagements under SASs, Government Auditing Standards, and/or examinations of prospective financial statements under the SSAEs.

Unconditional requirements: Those that a practitioner must follow in all cases if the circumstances apply to the requirement. These requirements use the words *must* or *is required*.

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COURSE 2

PERFORMING EXAMINATION AND REVIEW ENGAGEMENTS UNDER THE ATTESTATION STANDARDS (NTETG102)

OVERVIEW

COURSE DESCRIPTION: This interactive self-study course discusses attestation engagements and provides guidance on examination and review engagements performed under the attestation standards. Specifically, this course provides an overview of an attestation engagement and describes the standards that apply to it. It also discusses the relationship between the attestation standards to the statements on auditing standards and the statements on standards for accounting and review services. In addition it describes how to perform an engagement acceptance, planning, attestation procedures, wrap-up, supervision, and administration. Finally, this course discusses the required elements of the auditor's attestation report.

PUBLICATION/REVISION DATE: December 2010

RECOMMENDED FOR: Users of *PPC's Guide to Nontraditional Engagements*

PREREQUISITE/ADVANCE PREPARATION: Basic knowledge of auditing

CPE CREDIT: 6 QAS Hours, 6 Registry Hours

Check with the state board of accountancy in the state in which you are licensed to determine if they participate in the QAS program and allow QAS CPE credit hours. This course is based on one CPE credit for each 50 minutes of study time in accordance with standards issued by NASBA. Note that some states require 100-minute contact hours for self study. You may also visit the NASBA website at www.nasba.org for a listing of states that accept QAS hours.

FIELD OF STUDY: Auditing

EXPIRATION DATE: Postmark by **December 31, 2011**

KNOWLEDGE LEVEL: Basic

Learning Objectives:

Lesson 1—Overview of Attestation Engagements

Completion of this lesson will enable you to:

- Identify the aspects of an attestation engagement and the applicability of the standards to an engagement.
- Describe concepts relevant to an attestation engagement, including the subject matter, assertion, and responsible party.
- Determine which factors to assess when deciding whether to accept an attestation engagement.
- Explain factors affecting engagement planning, including establishing the terms of the engagement, understanding the subject matter, materiality, and attestation risk.
- Describe the purpose and basic requirements of workpapers in an attestation engagement, as well as the practitioner's responsibilities for workpaper retention and providing access to regulators and others.

Lesson 2—Examination Engagements under the Attestation Standards

Completion of this lesson will enable you to:

- Identify the guidance provided about the required level of testing in an examination engagement performed under the attestation standards.

- Describe the approach to testing of numerical and nonnumeric information required in a particular examination engagement.
- Identify procedures necessary when using the work of a specialist, obtaining a representation letter from the responsible party, and discovering subsequent events.
- Describe the guidance provided on the elements included in the practitioner's examination report.

Lesson 3—Review Engagements under the Attestation Standards

Completion of this lesson will enable you to:

- Assess factors to determine whether to perform a review engagement; identify the procedures to perform in a review engagement; and describe the effect of subsequent events.
- Describe each element in the practitioner's review report.
- Identify required workpapers and determine procedures to perform when wrapping up the engagement, including when part of the work is performed by other practitioners; acceding to a client request to change the level of service; and withdrawing from the engagement.

TO COMPLETE THIS LEARNING PROCESS:

Send your completed **Examination for CPE Credit Answer Sheet, Course Evaluation**, and payment to:

**Thomson Reuters
Tax & Accounting—R&G
NTETG102 Self-study CPE
36786 Treasury Center
Chicago, IL 60694-6700**

See the test instructions included with the course materials for more information.

ADMINISTRATIVE POLICIES:

For information regarding refunds and complaint resolutions, dial (800) 431-9025 for Customer Service and your questions or concerns will be promptly addressed.

Lesson 1: Overview of Attestation Engagements

INTRODUCTION

This lesson provides an overview of attestation engagements, including a discussion of when such standards apply to a particular engagement. In addition, the lesson describes the attestation standards a practitioner is required to follow when performing an examination or a review attestation engagement, as well as a comparison with other professional standards. Specifically, this lesson describes each element of an attestation engagement, the eleven attestation standards, and the factors a practitioner should consider when engaged to perform an attestation engagement.

Learning Objectives:

Completion of this lesson will enable you to:

- Identify the aspects of an attestation engagement and the applicability of the standards to an engagement.
- Describe concepts relevant to an attestation engagement, including the subject matter, assertion, and responsible party.
- Determine which factors to assess when deciding whether to accept an attestation engagement.
- Explain factors affecting engagement planning, including establishing the terms of the engagement, understanding the subject matter, materiality, and attestation risk.
- Describe the purpose and basic requirements of workpapers in an attestation engagement, as well as the practitioner's responsibilities for workpaper retention and providing access to regulators and others.

Purpose of This Lesson

A client might specifically ask a practitioner to examine or review an assertion, or, as often happens, the client's needs might be imprecisely defined. Regardless of the form of the request or the subject matter of the engagement, the service is an attestation engagement if the practitioner is engaged to issue or issues an examination, review, or agreed-upon procedures report on the subject matter (or on an assertion about the subject matter). Accordingly, many unusual engagements fall under the attestation standards umbrella. This course provides guidance for examination and review engagements performed under the attestation standards.

Although agreed-upon procedures engagements are subject to the attestation standards, they are unique because the practitioner reports findings rather than a conclusion. Also, the practitioner performs the procedures specified by the report users rather than using his or her judgment to determine the appropriate procedures. Consequently, many of the topics discussed in this course require unique considerations when applied in agreed-upon procedures engagements. This course covers only examination and review attestation engagements.

Certain types of examination and review engagements are subject to more detailed requirements. Those requirements are not covered in this course. The guidance in this course establishes the foundation for the examination and review services.

Overview of an Attestation Engagement

What Is an Attestation Engagement? The shorthand definition of an attestation engagement is one in which a practitioner issues a specific type of report on subject matter that is the responsibility of another party. (The precise definition is later in this lesson.) There are two parts to this definition:

- The practitioner's report.
- The responsible party's subject matter.

How Does the Practitioner Report? By providing a professional service and issuing a report that provides independent support for the subject matter, the practitioner adds credibility. The practitioner can perform any of three types of engagements:

- Examination.

- Review.
- Agreed-upon procedures.

Compilations of prospective financial statements are also covered by the attestation standards. That is the only type of compilation covered by the attest standards, and it was included when the already-existing standard on forecasts and projections was absorbed into the attestation standards. Services on forecasts and projections are not covered in this course. For guidance on services that might be provided in connection with prospective financial information, see *PPC's Guide to Forecasts and Projections*.

Who Is the Responsible Party? The responsible party is someone, other than the practitioner, who takes responsibility for the subject matter. Generally, the responsible party is the management of the entity with subject matter being measured. The responsible party is generally a group—akin to management—rather than an individual. The responsible party need not be the practitioner's client.

What Is Subject Matter? All engagements are made about something; that is the subject matter. The subject matter is what the practitioner applies procedures to. In an audit of financial statements, the subject matter is the financial results portrayed in the financial statements. In an examination regarding the effectiveness of a company's internal control over financial reporting, the subject matter is the internal control over financial reporting.

The subject matter may or may not be related to the financial statements, and it may or may not be numeric. For example, a subject matter might be compliance with certain laws, an entity's rate of return on invested assets, or the quantity of gallons of wastewater processed. The subject matter might or might not be reduced to writing and, if it is, it might or might not accompany the practitioner's report.

What Are Criteria? Criteria are standards against which the subject matter is measured. For example, the financial statements represent the subject matter of financial results; GAAP are the criteria against which they are measured. In an attestation engagement, the client asserts that the subject matter is in conformity with criteria. The criteria might or might not be formally established, like GAAP. But they generally need to be suitable and available to users. Additional guidance on determining whether criteria are both suitable and available to users is provided later in this lesson.

Sometimes, simple logic provides the criteria. For example, the number of square feet in a warehouse seems to be based on nothing more than accepted concepts of length and arithmetic. However, there may be questions about whether the area includes or excludes unusable space such as elevator shafts. Such ambiguities should be clarified before performing the engagement.

An attestation interpretation, *Responding to Requests for Reports on Matters Relating to Solvency*, (AT 9101.23–.33) provides an example of criteria that are too subjective to be reported on. The interpretation says that the practitioner cannot report that an entity is not insolvent, does not have unreasonably small capital, or has the ability to pay its debts as they mature. The interpretation reasons that these matters “are subject to legal interpretations under, and varying legal definition in, the Federal Bankruptcy Code. . . . Because these matters are not clearly defined in an accounting sense, and are therefore subject to varying interpretations, they do not provide the practitioner with the suitable criteria. . . .” It notes that, in addition, users “are concerned with legal issues on matters relating to solvency and the practitioner is generally unable to evaluate or provide assurance on these matters of legal interpretation.” The interpretation suggests substituting a more traditional service, such as an audit, in these cases.

What Is an Assertion? An assertion is a statement made by responsible party that the subject matter conforms with or is based on the criteria.

Must a Written Assertion Be Obtained from the Responsible Party? In general, the practitioner is required to obtain a written assertion from the responsible party. If the responsible party does not provide a written assertion, the practitioner should restrict the report. Also, there may be a scope limitation resulting from the lack of a written

assertion. Additional guidance on the impact of a lack of a written assertion on the practitioner's report is provided later in this lesson.

APPLICABILITY OF THE ATTESTATION STANDARDS

The attestation standards are contained in the AICPA's Statements on Standards for Attestation Engagements (SSAE). Technically, the standards can be issued by the AICPA Auditing Standards Board, the Accounting and Review Services Committee, or the Consulting Services Executive Committee. In practice, however, the Auditing Standards Board generally issues them. The standards' authority is the same regardless of which of those committees issues them.

Providing an attestation service is a professional service as defined in the AICPA *Code of Professional Conduct*, and the provisions of the attestation standards are enforceable under the Code. In fact, the standards themselves bear the following notice:

Rule 202 of the Institute's *Code of Professional Conduct* requires compliance with these standards.

Purpose of the Standards

The AICPA's original rationale in issuing the attestation standards was threefold:

- *To Recognize the Expansion of the Practitioner's Function.* Practitioners are often called on to attest to many things other than historical financial statements. The practitioner's report adds credibility and reduces information risk to users, thus providing a valuable service.
- *To Provide Consistency among Practitioners.* The standards were intended to promote consistency among practitioners in performing services and reporting on them.
- *To Increase Public Acceptance and Understandability.* The standards narrowed available services to a common set of functions understandable to the public.

The SSAEs establish the basic standards for all attestation work that practitioners undertake. All practitioners have to adhere to the 11 attestation standards, consisting of the general standards, the standards of fieldwork, and the reporting standards (similar to the 10 generally accepted audit standards). The 11 basic attestation standards are listed later in this lesson.

SSAE No. 13, *Defining Professional Requirements in Statements on Standards for Attestation Engagements*, defines terms used in the SSAEs to impose professional requirements. An unconditional requirement is designated by the terms *must* or *is required*. A presumptively mandatory requirement is designated by the term *should*. The term *should consider* means that consideration of the procedure or action is presumptively required, but carrying out the procedure is not.

Relationship to SASs and SSARS

The attestation standards do not affect GAAS (the SASs) or SSARS. For engagements covered by SASs and SSARS, practitioners should follow those pronouncements even though they may conflict in certain respects with the attestation standards.

The "risk assessment" standards, SAS Nos. 104–111, made significant additions to procedures and documentation required under GAAS but did not affect engagements done under the SSAEs (attestation standards). Throughout this course, it is suggested importing into attestation engagements concepts more meticulously developed in GAAS as a way of operationalizing the more general requirements in the attestation standards. However, the use of the guidance in SASs is not required in engagements performed under the attestation standards (except when the attestation standards specifically incorporate them). Moreover, students should not infer a conclusion that all analogous SAS guidance is necessarily appropriate for attestation engagements.

Organization of the Standards

The first SSAE, *Attestation Standards*, was issued in 1986 but was not numbered. In 1989, that standard, along with standards on prospective financial statements and pro forma financial statements, was codified into AICPA *Professional Standards*, Volume 1. In 1993, the codification became officially designated SSAE No. 1, *Attestation Standards*. SSAE Nos. 2 through 9 were issued to cover new situations, and they imposed new requirements. In 2001, SSAE No. 10 was issued to revise the existing standards and recodify them into new sections. Since then, additional SSAEs were issued. Exhibit 1-1 summarizes the current attestation standards.

Exhibit 1-1

Statements on Standards for Attestation Engagements

SSAE No. 10, *Attestation Standards: Revision and Recodification*:

- AT 101, *Attest Engagements*. (This is the umbrella standard that governs all types of attestation engagements.)
- AT 201, *Agreed-upon Procedures Engagements*.
- AT 301, *Financial Forecasts and Projections*.
- AT 401, *Reporting on Pro Forma Financial Information*.
- AT 501, *Reporting on an Entity's Internal Control over Financial Reporting*.^a
- AT 601, *Compliance Attestation*.
- AT 701, *Management's Discussion and Analysis*.

SSAE No. 11, *Attest Documentation*.^b

SSAE No. 12, *Amendment to Statement on Standards for Attestation Engagements No. 10, Attestation Standards: Revision and Recodification*.^b

SSAE No. 13, *Defining Professional Requirements in Statements on Standards for Attestation Engagements (AT 20)*.

SSAE No. 14, *SSAE Hierarchy (AT 50)*.

SSAE No. 15, *An Examination of an Entity's Internal Control Over Financial Reporting That Is Integrated With an Audit of Its Financial Statements (AT 501)*.^a

SSAE No. 16, *Reporting on Controls at a Service Organization (AT 801)*.

Note:

- ^a SSAE No. 15, superseded SSAE No. 10 (AT 501, *Reporting on an Entity's Internal Control over Financial Reporting*), for integrated audits for periods ending on or after December 15, 2008.
- ^b SSAE Nos. 11 and 12 are amendments to SSAE No. 10 and are not separately codified in the AT section of the authoritative standards. All references to SSAE No. 10 in this course are to SSAE No. 10, as amended by SSAE Nos. 11 and 12.

* * *

Are Attestation Engagements Subject to Peer Review?

Yes. Attest services are included in the definition of an accounting and auditing practice for purposes of performing and reporting on peer reviews.

SQCS No. 7, *A Firm's System of Quality Control*, which requires that firms establish quality control systems, also covers attestation engagements. The attest standards (AT 101) clarify that a firm should establish quality control policies and procedures to provide it with reasonable assurance of conforming with the attestation standards in all of its attest engagements. Furthermore, in today's litigious society, firms should require standardized quality control procedures on all types of accounting, auditing, and attestation services. *PPC's Guide to Quality Control* provides a quality control system that includes attestation engagements.

As part of its clarity initiative, the AICPA has redrafted SQCS No. 7. At its July, 2010 meeting, the Auditing Standards Board agreed to ballot on the issuance of a final SQCS No. 7, *A Firm's System of Quality Control (Redrafted)*, which, when effective, will supersede SQCS No. 7 of the same name.

ATTESTATION ENGAGEMENTS (EXAMINATION AND REVIEW ENGAGEMENTS)

Definition of an Attestation Engagement

SSAE No. 10 (AT 101.01) says that the attestation standards apply when the practitioner:

is engaged to issue or does issue an examination, review, or an agreed-upon procedures report on the subject matter, or an assertion about the subject matter, that is the responsibility of another party.

The paragraphs that follow explore the definition in further detail as it relates to examination or review engagements. When the attestation standards do not apply, the engagement will probably be subject to the less onerous, but less definitive, requirements of other standards such as the consulting standards.

Report. The attest standards ordinarily apply only when the practitioner has been specifically engaged to provide an attest report, which means the practitioner has been engaged to provide an attest service. In some cases, the practitioner cannot complete the engagement or is required to withdraw without rendering a report. In those cases, the attest standards apply because the practitioner was engaged to provide the report.

The practitioner who issues the form of report described in the SSAEs is subject to the standards, even if not specifically engaged to do so. The standard warns that a report that looks like an attestation report might be reasonably inferred to be one, causing users to reasonably believe that the standards apply. Therefore, a report not intended to be an attestation report should be *clearly distinguishable* from the standard forms of report.

The standards do not provide any guidance on how different the nonattest reports need to be. It is believed that, at a minimum, a report that provides assurance, but is not intended to be an examination or review attest report, should not:

- Call the service provided an examination or review.
- Claim to comply with AICPA standards (unless other standards are clearly identified).
- Provide positive or negative assurance about the subject matter's conformity with criteria.

In addition, it might be helpful to explicitly state that the report is not intended to be a report under the AICPA attestation standards.

AT 101.06 states that, "Any professional service resulting in the expression of assurance must be performed under AICPA professional standards that provide for the expression of assurance." There are only three sets of profes-

sional standards that provide for the expression of assurance: SASs, SSARs, and SSAEs; all the other professional standards are silent on the matter. Thus, this paragraph could be read literally to say that a report, other than one issued under the SASs or SSARs, that expresses any type of assurance must be an SSAE No. 10 examination or review report. Based on discussions with AICPA staff, it is not believed the Board intended to prohibit all assurance reports other than those described in the three sets of standards. It is believed the standard does not use the term *assurance* in a broad sense (the term is not defined in the standard) but, rather, to mean examination-like or review-like reports. Accordingly, the belief is that the standard intends only to prohibit the accountant from issuing an examination-like report, or a review-like report, that does not conform to the SASs, SSARs, or SSAEs. It is believed the standard did not intend to bar reports that express other types of assurance. Such reports would be permitted as long as they are clearly distinguishable from attestation reports. It is believed such engagements will generally be performed under the consulting standards. An example would be a due diligence assistance engagement. Also, if a practitioner accepts an engagement to estimate the value of a business, business interest, security, or intangible asset, he or she should follow the requirements in Statement on Standards for Valuation Services No. 1, *Valuation of a Business, Business Ownership Interest, Security, or Intangible Asset*.

Do the Standards Apply If the Practitioner Is Engaged to Apply Examination Procedures and Report Orally?

No. If the practitioner is not engaged to provide a written report and does not provide one, the attestation standards do not apply. However, the practitioner might find some of the guidance on judging criteria and selecting tests in the remainder of this lesson helpful in that situation.

What Is the Subject Matter?

The subject matter is what the accountant applies procedures to, such as historical performance, systems, or behavior. Some of the forms the subject matter might take include the following:

- Historical or prospective performance or condition (e.g., historical or prospective financial information, performance measurements, and backlog data).
- Physical characteristics (e.g., narrative descriptions, square footage of facilities).
- Historical events (e.g., price of a market basket of goods on a certain date).
- Analyses (e.g., break-even analyses).
- Systems and processes (e.g., internal control).
- Behavior (e.g., corporate governance, compliance with laws and regulations, and human resource practices).

The subject matter may be as of a point in time or for a period of time.

Does the Subject Matter Need to Be in Writing? No. In some cases, like summaries of results, the subject matter might be in writing and accompany the practitioner's report. In others, such as behavior, it is not. In most cases, however, it will be easier for the practitioner to test the subject matter if it has been reduced to writing.

What Is an Assertion?

An assertion is a statement by the responsible party that the subject matter is in conformity with the criteria being used. For example, when testing investment performance, the subject matter is the investment performance itself; the assertion is that the performance is measured in conformity with the relevant criteria (such as that developed by the CFA Institute). On an engagement to examine the effectiveness of internal control, the subject matter is internal control; the assertion is that control is effective based on the COSO criteria. (A financial statement analogy is that the subject matter is the company's financial results, while the assertion is that the financial statements are in conformity with GAAP.)

Is a Written Assertion Required in All Engagements? An assertion is not integral to determining whether the engagement is an attestation engagement. However, in most cases, the practitioner is required to obtain a written assertion while performing the engagement. The following paragraph discusses the impact of the lack of a written assertion on the practitioner's report.

As indicated in the following chart, the ramifications of the accountant's inability to obtain a written assertion depend on whether or not the client is the responsible party.

	Client is the responsible party	Client is not the responsible party
Effect on scope	Results in a scope limitation sufficient to preclude an unqualified opinion. In an examination engagement, the practitioner should generally disclaim, qualify the opinion, or withdraw. In a review engagement, the practitioner should withdraw from the engagement.	The practitioner may be able to conclude that there is sufficient evidence to form a conclusion about the subject matter.
Focus of opinion	If an opinion is issued, it should be on the subject matter rather than on the assertion about the subject matter. (That is because there is no assertion on which to report.)	If an opinion is issued, it should be on the subject matter rather than on the assertion about the subject matter. (That is because there is no assertion on which to report.)
Report restriction	Report should be restricted to specified parties.	Report should be restricted to specified parties.

Who Is the Responsible Party?

In an attestation engagement, the subject matter, or the assertion about it, is the responsibility of someone other than the practitioner. The client or other party who has responsibility for the subject matter (generally management of the entity whose performance is being measured) is called the *responsible party*.

A practitioner who helps assemble the subject matter should not claim to be the responsible party in an attestation engagement. Nor should the responsible party base its assertion solely on the practitioner's procedures.

The responsible party is the person or group whose actions, plans, or assumptions are reflected in the subject matter. A practitioner can be hired by one party to provide an attestation service on someone else's subject matter. Clearly, however, it is logistically easier when the responsible party is also the client.

What If the Responsible Party Is Not the Client? The practitioner may accept an engagement when the responsible party is not the client. In that case, the practitioner needs to obtain evidence of that third party's responsibility for the subject matter. For example, in an eldercare engagement, the adult children of a person in a nursing home might engage the practitioner to provide an attestation report about the level of care given to their parent. In that case, the children are ordinarily the clients. The management of the nursing home is the responsible party, as they are the people responsible for the subject matter (the subject matter being the level of care given to the parent). The practitioner can obtain evidence of management's responsibility by, for example, reading the nursing home's contract with the parent.

Documents that might provide evidence of a nonclient's responsibility for the subject matter include:

- An engagement letter.
- A representation letter.
- A statement within a presentation of the subject matter.
- A separate written assertion.

- Contracts or correspondence between the client and the responsible party.
- Relevant laws or regulations.

What If There Is No Responsible Party? Occasionally, there simply is no one responsible for the subject matter. For example, a local tourist bureau might want to make a claim about the annual days of sunshine or inches of snow per season. Neither it nor anyone else can realistically claim to be responsible for the sunshine or snowfall. In that case, the client may assume the role of responsible party as long as it has a reasonable basis for doing so. In this example, the local tourist bureau would have a reasonable basis for assuming the role of responsible party.

Use of the Report. The intended use of the report does not affect the standards that apply. So the applicability of the standards does not depend on whether the report is intended for general distribution, limited third-party use, or internal use, although some services, like agreed-upon procedures, are only permitted for limited use.

Engagements That Are Not Attestation Engagements

The following types of engagements are not attestation engagements:

- Services performed in accordance with Statements on Auditing Standards.
- Services performed in accordance with the Statement on Standards for Accounting and Review Services.
- Services performed in accordance with the Statement on Standards for Consulting Services, such as engagements in which the practitioner's role is solely to assist the client (for example, acting as the company accountant in preparing information other than financial statements).
- Services performed in accordance with the Statement on Standards for Valuation Services.
- Engagements in which a practitioner is engaged to testify as an expert witness in accounting, auditing, taxation, or other matters, given certain stipulated facts.
- Engagements in which the practitioner is engaged to advocate a client's position—for example, tax matters being reviewed by the Internal Revenue Service.
- Tax engagements in which a practitioner is engaged to prepare tax returns or provide tax advice.

SSAE No. 10's applicability is engagement-oriented. It only applies if the client engages the practitioner to apply it or if the practitioner provides a form of report that would imply that it applies. However, questions about applicability of standards might arise in the following types of engagements.

- *Compilations.* SSARS apply to compilations of historical financial statements of nonpublic companies. Compilations of prospective financial information, however, are covered by the attestation standards because standards for forecasts and projections have been codified into the attestation standards, as shown in Exhibit 1-1.
- *Consulting Services.* The result of a consulting engagement is advice or recommendations rather than a report that expresses an examination opinion or review conclusion on the subject matter. In that case, the Statements on Standards for Consulting Services (SSCS) apply to the consulting service. Occasionally, a consulting engagement might have elements that resemble an agreed-upon procedures engagement. When a practitioner provides both attest and consulting services to a client, he or she should issue separate reports on the two engagements. If the reports are in a common binder, the reports should be clearly identified and segregated.
- *Litigation Support Services.* Courts generally do not request reports in the form specified in the attestation standards. Accordingly, the standards generally do not apply. However, if the practitioner provides the standard form of report required by the standards, the attestation standards do apply. In general, SSCS generally apply to litigation services.

- *Most Tax Engagements.* Providing tax advice or preparing tax returns are not intended to add credibility to the subject matter, and defending a client's position before the IRS is similar to litigation support services. Statements on Standards for Tax Services generally apply to those types of engagements.
- *Assurance Services.* The concept of assurance services as defined by the Special Committee on Assurance Services (Elliott Committee) is economic, not standards-based. It encompasses a spectrum of services that might be delivered under different standards. For example, CPA *WebTrust* is an assurance service delivered as an attest service and, thus, is subject to the attestation standards. Direct provision of eldercare services, however, is generally structured as a consulting service rather than an attestation service.
- *Other Engagements That Provide a Conclusion about the Subject Matter.* The standards do not apply to engagements that result in reports that are clearly distinguishable from attest reports, as long as the practitioner was not engaged to apply the attest standards. So, a report that is clearly distinguishable from an attest report but that provides a written conclusion about the reliability, relevance, or other aspect of the subject matter is beyond the purview of the attestation standards. It is believed that this type of engagement would generally be structured as a consulting engagement. An example of such an engagement would be a due diligence assistance engagement.

What Standards Apply?

Most engagements, excluding tax services, fall under one of the following sets of standards:

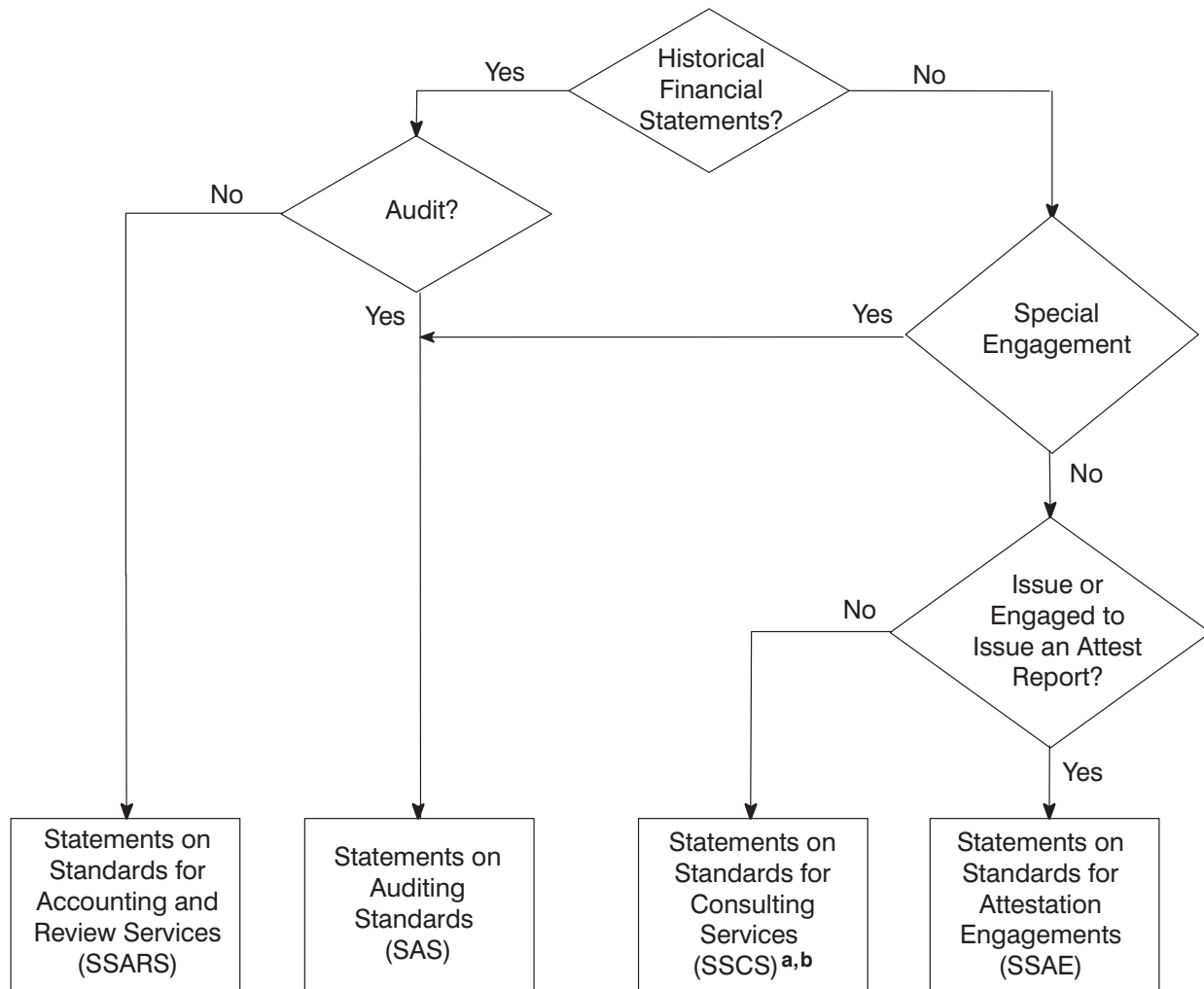
- Statements on Auditing Standards (SAS).
- Statements on Standards for Accounting and Review Services (SSARS).
- Statements on Standards for Attestation Engagements (SSAE).
- Statements on Standards for Consulting Services (SSCS).
- Statements on Standards for Valuation Services.

Exhibit 1-2 can aid in deciding which set of standards applies to an engagement for a nonpublic entity.

In some cases, an engagement may not be subject to a particular set of standards. In those cases, practitioners should look to the general standards set forth in Rule 201 of the AICPA *Code of Professional Conduct*. In addition, it may be advisable to follow the consulting standards because the standards are not burdensome and they provide good guidance to practitioners.

Exhibit 1-2 includes a decision box reading "Special Engagement." Those consist primarily of nonaudit engagements addressed in the auditing standards, including the following:

- Reports on the processing of transactions of service organizations—SAS No. 70 (AU 324).
- Condensed financial statements and selected financial data—SAS No. 42 (AU 552).
- Compliance with aspects of contractual agreements related to an audit—SAS No. 62 (AU 623).
- Special-purpose financial presentations to comply with contractual agreements or regulatory requirements—SAS No. 62 (AU 623).
- Financial information in prescribed forms—SAS No. 62 (AU 623).
- Reports on the application of accounting principles—SAS No. 50 (AU 625).
- Letters for underwriters—SAS No. 72 (AU 634).
- Compliance auditing for governmental entities—SAS No. 117 (AU 801).

Exhibit 1-2**Deciding Which Standards Apply To an Engagement for a Nonpublic Entity****Notes:**

- ^a If a practitioner accepts an engagement to estimate the value of a business, business interest, security, or intangible asset, he or she should follow the requirements of Standards for Valuation Services No. 1, *Valuation of a Business, Business Ownership Interest, Security, or Intangible Asset*.
- ^b There may be engagements that are not subject to a particular set of standards. In those cases, practitioners should look to Rule 201 of the AICPA *Code of Professional Conduct* and may also follow the consulting standards.

* * *

The 11 Attestation Standards

The General, Fieldwork, and Reporting Standards. SSAE No. 10 (AT 101), as amended by SSAE No. 14, *SSAE Hierarchy*, establishes 11 attestation standards similar to the 10 generally accepted auditing standards. They are—

a. General Standards

- (1) The practitioner must have adequate technical training and proficiency to perform the attestation engagement.
- (2) The practitioner must have adequate knowledge of the subject matter.
- (3) The practitioner must have reason to believe that the subject matter is capable of evaluation against criteria that are suitable and available to users.
- (4) The practitioner must maintain independence in mental attitude in all matters relating to the engagement.
- (5) The practitioner must exercise due professional care in the planning and performance of the engagement and the preparation of the report.

b. Standards of Fieldwork

- (1) The practitioner must adequately plan the work and must properly supervise any assistants.
- (2) The practitioner must obtain sufficient evidence to provide a reasonable basis for the conclusion that is expressed in the report.

c. Standards of Reporting

- (1) The practitioner must identify the subject matter or the assertion being reported on and state the character of the engagement in the report.
- (2) 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.
- (3) 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.
- (4) 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:
 - 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.
 - When the criteria used to evaluate the subject matter are available only to specified parties.
 - When reporting on subject matter and a written assertion has not been provided by the responsible party.
 - When the report is on an attestation engagement to apply agreed-upon procedures of the subject matter.

Types of Attestation Engagements

There are three types of attestation engagements:

- Examination.
- Review.
- Application of agreed-upon procedures.

An examination is the highest level of service. It is analogous to an audit of historical financial statements. It requires the practitioner to reduce the risk of undetected material misstatement to a low level and involves substantial evidence gathering. As a result of the examination, the practitioner provides an opinion about the conformity of the subject matter with the criteria.

A review, like a review of historical financial statements under SSARS, provides limited assurance. It requires the practitioner to reduce the risk of undetected material misstatement to a moderate level and primarily involves inquiries and analytical procedures. The review report provides negative assurance (that is, it says that nothing caused the practitioner to believe the subject matter did not conform to the presentation criteria). Generally providing review services is not recommended.

Agreed-upon procedures engagements involve applying procedures specified by the users of the report. The users take responsibility for the adequacy of the procedures, which, within certain guidelines, can be as limited or extensive as the users desire. The practitioner's report describes the procedures applied and the results of their application (the findings). No general assurance about the subject matter or assertion is provided in the report.

SELF-STUDY QUIZ

Determine the best answer for each question below. Then check your answers against the correct answers in the following section.

1. Which of the following best describes the meaning of the term *subject matter* in an attestation engagement?
 - a. The subject matter is what the practitioner applies procedures to.
 - b. In an audit of financial statements, the subject matter is the effectiveness of a company's internal control over financial reporting.
 - c. The subject matter is always related to the financial statements.
 - d. The subject matter is always numeric.
2. In an attestation engagement, the client asserts that the subject matter is in conformity with criteria. Criteria are standards against which the subject matter is measured. Generally, criteria need to be both suitable and available to users. In which of the following situations might the criteria **not** be suitable for use in an attestation engagement?
 - a. Financial statements are measured against GAAP.
 - b. The number of square feet in a warehouse measured against accepted concepts of length and arithmetic.
 - c. A client's "solvency" based on whether the client has unreasonably small capital or the ability to pay its debts as they mature.
 - d. Percentage rents in a lease agreement measured against the definition of sales in a lease agreement.
3. Which of the following best describes the relationship between the attestation standards (SSAEs), the statements on standards for auditing services (SASs), and the statements on standards for accounting and review services (SSARSs)?
 - a. For accounting and review services, practitioners should follow the attestation standards, even though they conflict with the SSARS.
 - b. The "risk assessment" standards, SAS Nos. 104–111, affect procedures and documentation required under GAAS as well as the attestation standards.
 - c. The use of the guidance in the SASs is not required in engagements performed under the attestation standards (except when the attestation standards specifically incorporate them).
 - d. Practitioners are cautioned against importing into attestation engagements concepts more meticulously developed in GAAS as a way of operationalizing the more general requirements in the attestation standards.

4. The attest standards ordinarily apply only when the practitioner has been specifically engaged to provide an attest report, which means the practitioner has been engaged to provide an attest service. Which of the following best describes a report in accordance with the attestation standards?
- a. A practitioner who issues the form of report described in the SSAEs is subject to the standards unless he or she has not been specifically engaged to provide an attest service.
 - b. A report that looks like an attestation report might be reasonably inferred to be one, causing users to reasonably believe that the standards apply.
 - c. A report not intended to be an attestation report may still refer to the service as an examination or review, if that is the term that best describes the procedures performed.
 - d. A nonattest report may provide positive assurance about the subject matter's conformity with criteria.
5. Which of the following statements concerning the term *subject matter* is correct?
- a. The subject matter could be physical characteristics or historical events.
 - b. The subject matter is always as of a point in time.
 - c. Behavior cannot be the subject matter of an attest service since testing it would be too subjective.
 - d. In order for the practitioner to issue a report, the subject matter must be in writing and accompany the report.
6. Which of the following engagements is **not** covered by the attestation standards?
- a. Examination of internal control over financial reporting.
 - b. Compilation of prospective financial information.
 - c. Application of agreed-upon procedures.
 - d. Review of historical financial statements.
7. In which of the following circumstances could the practitioner issue a report that is **not** restricted to the specified parties?
- a. When reporting on subject matter and a written assertion has not been provided by the responsible party.
 - b. 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.
 - c. When the criteria used to evaluate the subject matter are considered to be well understood by or available to users.
 - d. When the report is on an attest engagement to apply agreed-upon procedures to the subject matter.

8. Use the following information for questions 8–11: Youth Ministries, a not-for-profit organization working with inner city youths, opened its first drug rehabilitation facility last year in Kansas City, Kansas. It wants to expand its services into the neighboring city of Kansas City, Missouri, by opening a drug rehabilitation facility there by year-end, but the city is concerned that such a facility in the area will lead to an increase in drug traffic and crime. Because the city of Kansas City, Kansas, had similar concerns prior to the opening of Youth Ministries' first drug rehab center, they entered into a contract in which Youth Ministries agreed to implement and pay for certain security services. In addition, the contract stipulated a number of other matters with which Youth Ministries agreed to comply. To entice the city of Kansas City, Missouri, to allow it to open a facility in the area, Youth Ministries engaged Ken Thompson, CPA, to perform an engagement to provide assurance that it has complied with the terms of its contract with the city of Kansas City, Kansas. The following four questions pertain to this fact situation. Which of the following best describes the subject matter of the engagement?
- a. The financial results of Youth Ministries for the year ended Dec. 31, 20XX.
 - b. The financial results of the contract with the city of Kansas City, Kansas.
 - c. Compliance with the federal laws governing not-for-profit organizations.
 - d. Compliance with the terms of the contract with the city of Kansas City, Kansas.
9. Using the information provided in question #8, who is the responsible party in this engagement?
- a. The city of Kansas City, Kansas.
 - b. Ken Thompson, CPA.
 - c. Youth Ministries.
 - d. The city of Kansas City, Missouri.
10. Which of the following best describes the effect on Thompson's report if Youth Ministries does **not** provide a written assertion?
- a. If Thompson issues an opinion, it should be on the subject matter rather than on the assertion about the subject matter because there is no assertion on which to report.
 - b. The report should be restricted to the specified parties.
 - c. Youth Ministries' refusal to provide a written assertion in an agreed-upon procedures engagement requires the practitioner to withdraw from the engagement.
11. Using the information provided in question #8, which type of engagement should Thompson perform to best achieve the stated objectives?
- a. Audit of the financial statements of Youth Ministries under the SASs.
 - b. Review of Youth Ministries' compliance with the terms of the contract with Kansas City, Kansas.
 - c. Agreed-upon procedures on Youth Ministries' compliance with the terms of the contract with Kansas City, Kansas.
 - d. Examination of Youth Ministries' compliance with the terms of the contract with Kansas City, Kansas.

SELF-STUDY ANSWERS

This section provides the correct answers to the self-study quiz. If you answered a question incorrectly, reread the appropriate material. **(References are in parentheses.)**

1. Which of the following best describes the meaning of the term *subject matter* in an attestation engagement? **(Page 136)**
 - a. **The subject matter is what the practitioner applies procedures to. [This answer is correct. In other way, the subject matter is what the engagement is about and it is what the practitioner applies procedures to.]**
 - b. In an audit of financial statements, the subject matter is the effectiveness of a company's internal control over financial reporting. [This answer is incorrect. In an audit of financial statements, the subject matter is *the financial results portrayed in the financial statements*. In an examination regarding the effectiveness of a company's internal control over financial reporting, the subject matter is the internal control over financial reporting.]
 - c. The subject matter is always related to the financial statements. [This answer is incorrect. The subject matter may or may not be related to the financial statements. For example, a subject matter might be an entity's rate of return on invested assets or the quantity of gallons of wastewater processed.]
 - d. The subject matter is always numeric. [This answer is incorrect. The subject matter might or might not be numeric. For instance, the subject matter might be compliance with certain laws.]
2. In an attestation engagement, the client asserts that the subject matter is in conformity with criteria. Criteria are standards against which the subject matter is measured. Generally, criteria need to be both suitable and available to users. In which of the following situations might the criteria **not** be suitable for use in an attestation engagement? **(Page 136)**
 - a. Financial statements are measured against GAAP. [This answer is incorrect. If the financial statements represent the subject matter of financial results, GAAP are the criteria against which they are measured. Criteria used in other types of engagements might or might not be formally established, like GAAP. But they generally need to be suitable and available to users.]
 - b. The number of square feet in a warehouse measured against accepted concepts of length and arithmetic. [This answer is incorrect. This criteria is suitable based on simple logic. However, there may be questions about whether the area includes or excludes unusable space such as elevator shafts. The practitioner should clarify such ambiguities before performing the engagement.]
 - c. **A client's "solvency" based on whether the client has unreasonably small capital or the ability to pay its debts as they mature. [This answer is correct. An attestation interpretation, *Responding to Requests for Reports on Matters Relating to Solvency*, provides an example of criteria that are too subjective to be reported on. The interpretation says that the practitioner cannot report that an entity is not insolvent. The interpretation reasons that these matters "are subject to legal interpretations under, and varying legal definition in, the Federal Bankruptcy Code. . . . Because these matters are not clearly defined in an accounting sense, and are therefore subject to varying interpretations, they do not provide the practitioner with the suitable criteria. . . ." It notes that, in addition, users "are concerned with legal issues on matters relating to solvency and the practitioner is generally unable to evaluate or provide assurance on these matters of legal interpretation." The interpretation suggests substituting a more traditional service, such as an audit, in these cases.]**
 - d. Percentage rents in a lease agreement measured against the definition of sales in a lease agreement. [This answer is incorrect. Although such criteria may not pass the suitability test because the definition of sales used as the basis of the rents varies substantially from the GAAP meaning of the word, the practitioner can examine the calculation and report on it as long as the landlord and tenant agreed to the criteria and understand them.]

3. Which of the following best describes the relationship between the attestation standards (SSAEs), the statements on standards for auditing services (SASs), and the statements on standards for accounting and review services (SSARSs)? **(Page 137)**
- a. For accounting and review services, practitioners should follow the attestation standards, even though they conflict with the SSARS. [This answer is incorrect. According to the Standards, practitioners should follow the SSARS, even when those pronouncements may conflict in certain respects with the attestation standards.]
 - b. The “risk assessment” standards, SAS Nos. 104–111, affect procedures and documentation required under GAAS as well as the attestation standards. [This answer is incorrect. The risk assessment standards made significant additions to procedures and documentation required under GAAS but did not affect engagements done under the SSAEs, per the Standards.]
 - c. The use of the guidance in the SASs is not required in engagements performed under the attestation standards (except when the attestation standards specifically incorporate them). [This answer is correct. Although this is recommended, practitioners should not assume that all similar SAS guidance is necessarily appropriate for attestation engagements.]**
 - d. Practitioners are cautioned against importing into attestation engagements concepts more meticulously developed in GAAS as a way of operationalizing the more general requirements in the attestation standards. [This answer is incorrect. Generally, the Standards suggest importing into attestation engagements concepts more meticulously developed in GAAS as a way of operationalizing the more general requirements in the attestation standards.]
4. The attest standards ordinarily apply only when the practitioner has been specifically engaged to provide an attest report, which means the practitioner has been engaged to provide an attest service. Which of the following best describes a report in accordance with the attestation standards? **(Page 139)**
- a. A practitioner who issues the form of report described in the SSAEs is subject to the standards unless he or she has not been specifically engaged to provide an attest service. [This answer is incorrect. According to the Standards, practitioner who issues an attest form of report is subject to the standards, even if not specifically engaged to do so. Therefore, a report not intended to be an attestation report should be *clearly distinguishable* from the standard forms of report.]
 - b. A report that looks like an attestation report might be reasonably inferred to be one, causing users to reasonably believe that the standards apply. [This answer is correct. For this reason, a report not intended to be an attestation report should not, among other things, claim to comply with AICPA standards.]**
 - c. A report not intended to be an attestation report may still refer to the service as an examination or review, if that is the term that best describes the procedures performed. [This answer is incorrect. According to the Standards, such a report should not refer to the service in this manner as that might cause users to infer that an attestation service was performed.]
 - d. A nonattest report may provide positive assurance about the subject matter's conformity with criteria. [This answer is incorrect. Standards suggest that a nonattest report not provide either positive or negative assurance about the subject matter's conformity with criteria so as not to confuse users about the type of service performed.]

5. Which of the following statements concerning the term *subject matter* is correct? (Page 140)

- a. **The subject matter could be physical characteristics or historical events. [This answer is correct. Subject matter is what the practitioner applies procedures to. Examples of these two types of subject matter are square footage of the client's facilities or the market price of inventory on a certain date.]**
- b. The subject matter is always as of a point in time. [This answer is incorrect. According to the Standards, the subject matter may be as of a point in time or for a period of time.]
- c. Behavior cannot be the subject matter of an attest service since testing it would be too subjective. [This answer is incorrect. Subject matter might take the form of behavior per the Standards. For example, a practitioner could be engaged to test certain assertions about corporate governance, compliance with laws and regulations, and human resource practices.]
- d. In order for the practitioner to issue a report, the subject matter must be in writing and accompany the report. [This answer is incorrect. In some cases, like summaries of results, the subject matter might be in writing and accompany the practitioner's report. In others, such as behavior, it is not. In most cases, however, the Standards state that it will be easier for the practitioner to test the subject matter if it has been reduced to writing.]

6. Which of the following engagements is **not** covered by the attestation standards? (Page 142)

- a. Examination of internal control over financial reporting. [This answer is incorrect. Examinations of internal control over financial reporting are covered by SSAE No. 10, *Attestation Standards: Revision and Recodification*, as amended.]
- b. Compilation of prospective financial information. [This answer is incorrect. Compilations of prospective financial information are covered by AT 301, *Financial Forecasts and Projections*, which is included in SSAE No. 10.]
- c. Application of agreed-upon procedures. [This answer is incorrect. Agreed-upon procedures engagements are covered by various sections of SSAE No. 10. Some types of agreed-upon procedures engagements also fall under SAS No. 62, *Special Reports*]
- d. **Review of historical financial statements. [This answer is correct. A review of historical financial statements is covered by SSARS No. 1, *Compilations and Reviews of Financial Statements*.]**

7. In which of the following circumstances could the practitioner issue a report that is **not** restricted to the specified parties? (Page 145)

- a. When reporting on subject matter and a written assertion has not been provided by the responsible party. [This answer is incorrect. According to the Attestation Standards, in this situation, the practitioner must restrict the use of the report to the specified parties.]
- b. 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. [This answer is incorrect. According to the Attestation Standards, in this situation, the practitioner must restrict the use of the report to the specified parties.]
- c. **When the criteria used to evaluate the subject matter are considered to be well understood by or available to users. [This answer is correct. Criteria used in a general-use report is considered to be well understood and/or available to users. For example, users typically understand GAAP, which is the criteria against which financial results often are measured. For that reason, reports on GAAP financial statements are appropriate for all users.]**
- d. When the report is on an attest engagement to apply agreed-upon procedures to the subject matter. [This answer is incorrect. According to the Attestation Standards, in this situation, the practitioner must restrict the report to the specified users since they are the ones who determine the criteria to be used and accept responsibility for the appropriateness of the criteria for their purposes.]

8. Use the following information for questions 8–11: Youth Ministries, a not-for-profit organization working with inner city youths, opened its first drug rehabilitation facility last year in Kansas City, Kansas. It wants to expand its services into the neighboring city of Kansas City, Missouri, by opening a drug rehabilitation facility there by year-end, but the city is concerned that such a facility in the area will lead to an increase in drug traffic and crime. Because the city of Kansas City, Kansas, had similar concerns prior to the opening of Youth Ministries' first drug rehab center, they entered into a contract in which Youth Ministries agreed to implement and pay for certain security services. In addition, the contract stipulated a number of other matters with which Youth Ministries agreed to comply. To entice the city of Kansas City, Missouri, to allow it to open a facility in the area, Youth Ministries engaged Ken Thompson, CPA, to perform an engagement to provide assurance that it has complied with the terms of its contract with the city of Kansas City, Kansas. The following four questions pertain to this fact situation. Which of the following best describes the subject matter of the engagement? **(Page 140)**
- a. The financial results of Youth Ministries for the year ended Dec. 31, 20XX. [This answer is incorrect. Although the specified parties might be interested in these financial results, according to the Standards, the main focus of this engagement is not financial performance per the terms of the engagement with the CPA.]
 - b. The financial results of the contract with the city of Kansas City, Kansas. [This answer is incorrect. Although the specified parties might be interested in these financial results, according to the Standards, the main focus of this engagement is not financial performance. The CPA was not engaged to report on the financial results of the contract with the city.]
 - c. Compliance with the federal laws governing not-for-profit organizations. [This answer is incorrect. According to the Standards, although the engagement involves compliance, compliance with federal laws is not the subject matter and not what the CPA was engaged to provide assurance on.]
 - d. **Compliance with the terms of the contract with the city of Kansas City, Kansas. [This answer is correct. The subject matter of this engagement is Youth Ministries' compliance with terms of the contract with the city of Kansas City, Kansas, since Ken Thompson was engaged to perform an engagement to provide assurance to the city that youth ministries complied with the terms of the contract.]**
9. Using the information provided in question #8, who is the responsible party in this engagement? **(Page 141)**
- a. The city of Kansas City, Kansas. [This answer is incorrect. The city of Kansas City, Kansas, is not the one responsible for the subject matter, per the Standards.]
 - b. Ken Thompson, CPA. [This answer is incorrect. Even if the CPA helps to obtain information about the subject matter, it still remains the responsibility of the responsible party, per the Standards.]
 - c. **Youth Ministries. [This answer is correct. Youth Ministries is responsible for its compliance with the terms of the contract with the city of Kansas City, Kansas, per the Standards.]**
 - d. The city of Kansas City, Missouri. [This answer is incorrect. The city of Kansas City, Missouri, is not the one responsible for the subject matter, per the Standards.]
10. Which of the following best describes the effect on Thompson's report if Youth Ministries does **not** provide a written assertion? **(Page 141)**
- a. If Thompson issues an opinion, it should be on the subject matter rather than on the assertion about the subject matter because there is no assertion on which to report. [This answer is incorrect. According to the Standards, there is no opinion issued in an agreed-upon procedures engagement.]
 - b. The report should be restricted to the specified parties. [This answer is incorrect. An agreed-upon procedures report is always restricted to the specified parties.]
 - c. **Youth Ministries' refusal to provide a written assertion in an agreed-upon procedures engagement requires the practitioner to withdraw from the engagement. [This answer is correct. Although a**

practitioner is not required to obtain a written assertion in some types of agreed-upon procedures engagements, Thompson should obtain from one in an engagement related to compliance with specified requirements. Since Youth Ministries is both the client as well as the responsible party, its refusal to provide a written assertion requires Thompson to withdraw from the engagement.]

11. Using the information provided in question #8, which type of engagement should Thompson perform to best achieve the stated objectives? **(Page 146)**

- a. Audit of the financial statements of Youth Ministries under the SASs. [This answer is incorrect. Although the city of Kansas City, Missouri, might be interested in Youth Ministries' financial results, that is not the subject of this engagement nor is an audit an attestation engagement. In this engagement, the specified parties are interested in compliance with the terms of a contract. The objective of an audit is to express an opinion about whether the financial statements are fairly presented in conformity with generally accepted accounting principles (GAAP) or an other comprehensive basis of accounting (OCBOA).]
- b. Review of Youth Ministries' compliance with the terms of the contract with Kansas City, Kansas. [This answer is incorrect. A review, like a review of historical financial statements under SSARS, provides limited assurance. By performing a review, Thompson would be able to provide only negative assurance (that is, it says that nothing caused the practitioner to believe the subject matter did not conform to the presentation criteria). For this and other reasons, it is generally recommended against providing review services. In addition, SSAE No. 10 (AT 601) prohibits practitioners from performing review engagements or otherwise providing negative assurance in attestation engagements regarding compliance.]
- c. **Agreed-upon procedures on Youth Ministries' compliance with the terms of the contract with Kansas City, Kansas. [This answer is correct. In this situation, an agreed-upon procedures engagement would probably be the best answer for several reasons. First, the city of Kansas City, Missouri is likely to want information about Youth Ministries' compliance with the terms of its contract with Kansas City, Kansas, before allowing it to open a new location in the area. Since all three would be specified users of the report, Youth Ministries; city of Kansas City, Kansas; and city of Kansas City, Missouri, would take responsibility for the adequacy of the procedures, which, within certain guidelines, could be as limited or extensive as the users desire. By agreeing on the procedures to perform, Thompson would be able to provide the specified users with assurance that Youth Ministries complied with the terms of its contract. Second, although Thompson would not be able to provide general assurance about the subject matter or assertion in the report, he would be able to describe the procedures applied and the results of those procedures, including any instances of noncompliance. Finally, the criteria used in the agreed-upon procedures engagement would be the covenants included in the contract with the city of Kansas City, Kansas, which are not generally available to general users. Thus, an engagement to examine Youth Ministries' compliance with the terms of the contract would result in a restricted use report anyway. Thompson probably should perform the engagement under SSAE No. 10 (AT 601, *Compliance Attestation*), which applies to agreed-upon procedures engagements related to compliance with specified requirements.]**
- d. Examination of Youth Ministries' compliance with the terms of the contract with Kansas City, Kansas. [This answer is incorrect. Although an examination engagement would enable Thompson to provide the highest level of assurance on whether Youth Ministries complied with the terms of its contract with the city of Kansas City, Kansas, such an engagement would likely be very expensive to perform since it would require Thompson to reduce the risk of undetected material misstatement to a low level and obtain substantial evidence. Since the purpose of the engagement is basically to provide to the city of Kansas City, Missouri, that Youth Ministries has met its end of the deal (that is, complied with the terms of its contract with city of Kansas City, Kansas) to entice the city of Kansas City, Missouri, to enter into a similar agreement with them, it seems that objective can be better served using a different type of engagement.]

ACCEPTING AN ATTESTATION ENGAGEMENT

An attestation engagement can come from an existing client or from a potential new client. In either case, the practitioner should conscientiously consider the benefits and risks of accepting the engagement.

New clients (with whom the practitioner has no experience) involve potential risks for the practitioner, for example, questions regarding management's integrity and dependability that have usually already been addressed for existing clients. On the other hand, there are often additional potential rewards, such as the opportunity to provide recurring services in addition to the attestation engagement.

With an existing client, the practitioner must consider the risk involved in performing a *nontraditional* engagement. The potential risk of being involved in such an engagement may outweigh the potential rewards. However, the practitioner must also consider the potential risk of rejecting such an engagement for an existing client. That is, the practitioner might risk forfeiting recurring services currently provided for an existing client if the attestation engagement is refused. In either case, the practitioner should consider two general questions in deciding whether to accept an attestation engagement:

- Can I accept it?
- Should I accept it?

Can I Accept the Engagement?

The attestation standards create three hurdles to accepting an attestation engagement:

- Competence.
- Criteria.
- Independence.

Competence. The first general attestation standard requires the practitioner to have adequate technical training and proficiency in the attest function. The practitioner must be able to design tests and evaluate evidence. This is probably the most transferable of the skills practitioners develop in auditing. It generally does not present a significant barrier to providing an attestation service.

The second general standard states that the practitioner must have adequate knowledge of the subject matter. The practitioner must have or obtain an understanding of the subject matter to which he or she is to attest. Knowledge of the subject matter varies by engagement. Sometimes it requires little more than common sense, such as in an engagement to attest to the number of square feet in a warehouse. Other times it requires substantial familiarity with complex subjects, such as actuarial data. The practitioner can obtain this knowledge through formal education, experience, or by using a specialist. The specific subject matter might be outside the practitioner's expertise even though the practitioner might have substantial knowledge of the client's business and industry. Accordingly, this factor should be seriously considered before accepting the engagement, even for a recurring client. If the practitioner decides to use a specialist, the practitioner must have sufficient knowledge of the subject matter to both:

- Communicate the objectives of the work to the specialist.
- Evaluate the specialist's work.

Use of a specialist is discussed further in lesson 2.

As a practical matter, practitioners are not required to have the necessary knowledge in the subject matter before accepting an engagement. That knowledge can be obtained after acceptance. However, in making the acceptance decision, practitioners must consider whether they have, or will be able to obtain, the requisite knowledge.

Criteria. GAAP is a set of criteria against which financial statements can be measured, and *Internal Control—Integrated Framework* (the COSO Report) provides criteria for internal control. Sometimes simple logic provides the

criteria or measurement basis. For example, the number of square feet in a warehouse seems to be based on nothing more than simple length and arithmetic. However, there may be questions about whether the measurement should include or exclude unusable space such as elevator shafts. Such ambiguities should be clarified before performing the engagement.

The third general attestation standard requires that the criteria used to judge the subject matter be suitable in the circumstances. The practitioner cannot provide an attestation service when the criteria are ill-defined or unsuitable. Unsuitable criteria serve no useful purpose and, accordingly, a practitioner's professional opinion based on such criteria would be meaningless and possibly misleading.

The third general standard requires that the practitioner perform an engagement only if he or she has reason to believe the following conditions exist:

- The criteria are suitable.
- The criteria are available to users.
- The subject matter is capable of evaluation using the criteria.

Suitability. Certain criteria are presumed to be suitable. These criteria have been established by—

- a group that has been designated by AICPA Council to establish criteria (always presumed to be suitable), or
- a body composed of experts that follow due-process procedures, including procedures for distribution of proposed criteria for public comment (ordinarily presumed to be suitable).

As a practical matter, though, anyone (including industry groups, the client, or the responsible party) can create criteria for use in an attestation engagement. To determine whether such criteria are suitable for the engagement, the practitioner needs to consider whether they are:

- Objective—that is, whether they are free from bias.
- Measurable—that is, whether they permit reasonably consistent measurements, qualitative or quantitative, of the subject matter.
- Complete—that is, whether they are sufficiently complete so that those relevant factors that would alter a conclusion about the subject matter are not omitted.
- Relevant—that is, whether they are relevant to the subject matter.

For any subject matter, there may be more than one set of criteria that could be used. The choice among alternative criteria often involves trade-offs among the four attributes discussed in the preceding paragraph. For example, to use an analogy from financial reporting, the cash basis of accounting is more reliably measured than GAAP, as it includes no estimates or contingencies that must be reported before they are settled. On the other hand, GAAP is generally considered more relevant for certain types of decisions because it captures noncash assets and liabilities. Thus, each set of criteria is considered suitable for measuring financial results; the choice between the two criteria is generally made based on the ultimate use of the financial statements. Similar judgments must be made for other types of subject matter, particularly when there are no established criteria. For example, customer satisfaction might be usefully measured based on the number of customer complaints, on the number of repeat purchases, or on other bases. Or, measuring speed of a computer's operating system might involve measuring how fast the computer boots, how fast it accepts data, how fast it processes data, or some combination of those activities.

The need for suitable criteria is unrelated to the level of service the practitioner provides. If, for example, the criteria are unsuitable for an examination, they cannot be used for a review either. Thus, the practitioner cannot solve the problem of unsuitable criteria by providing a lower level of service. The only options in that case are (a) selecting better criteria or (b) obtaining the user(s) agreement with the criteria.

The users may agree on any criteria they believe useful for their purposes, even if the practitioner is not satisfied that it meets the four-part test presented above. Such criteria might be useful for the users' purposes, but not for use by other persons. In that case, the presentation and the practitioner's report should be restricted to the use of those who agreed on the criteria or those whom the practitioner can presume to have an adequate understanding of them. For example:

- The calculation of the percentage rents in a lease agreement may not pass the suitability test because the definition of *sales* used as the basis of the rents varies substantially from the GAAP meaning of the word. Nonetheless, the practitioner can examine the calculation and report on it because the landlord and tenant agreed to the criteria and understand them.
- Certain performance measures commonly used in specific industries might not be complete because they omit certain factors. The practitioner might be able to examine them, however, if the report is to be restricted to those in the industry who understand and use them.

Availability. The criteria used in the engagement should be available to users so that they can understand how the subject matter is measured. In some cases, like GAAP for financial reporting, the criteria are published and easily accessed by the public. When the criteria are not publicly available, they should be available in one of the following ways:

- Available to all users through inclusion in a clear manner in the presentation of the subject matter or in the assertion. (The criteria should be described in sufficient detail to be understood by a knowledgeable reader.)
- Available to all users through inclusion in a clear manner in the practitioner's report. (The criteria should be described in sufficient detail to be understood by a knowledgeable reader.)
- Well understood by most users, although not formally available (for example, "The distance between points A and B is 20 feet").
- 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). In this case, the report should not be used by those who do not have access to the criteria.

If the criteria require certain disclosures (similar to financial statement disclosures required by GAAP), such disclosures should be provided in the presentation of the subject matter or the assertion.

Exhibit 1-3 presents a flowchart depicting the factors a practitioner should use when determining criteria are suitable and available for use in an attestation engagement.

Determining Suitability and Availability of Criteria for Use in an Attestation Engagement



Reasonably Consistent Estimation. Prior to SSAE No. 10, SSAE No. 1 established a separate requirement—that the subject matter be capable of reasonably consistent estimation or measurement using the criteria. SSAE No. 10 modified this, requiring only that the subject matter be capable of evaluation and that the *criteria* be sufficiently measurable to allow for reasonably consistent measurement when used. It is believed practitioners should separately consider whether the subject matter itself is consistently measurable. That is, different persons using the criteria should be able to obtain materially similar estimates or measurements. This is a separate consideration from the need for suitable criteria. In some cases, the criteria might be adequate, but the subject matter too soft to measure consistently. For example, in reporting on forecasts, the criteria are established in the *AICPA Guide for Prospective Financial Information* and, accordingly, are presumed to be suitable. Nonetheless, the AICPA Guide generally prohibits accountants from examining forecasts that extend more than five years out, reasoning that expectations at such distant dates are not capable of reasonably consistent estimation.

Sometimes, it is hard to tell whether the problem exists in the criteria or with the subject matter. For example, an engagement involving the number of minutes of news in a local news broadcast is hard to measure because the definition of news is so vague. Even by sharpening it, there are inevitable measurement problems. For example, should one count the time on-air reporters banter back and forth, time spent on consumer features, or time showing file footage of events reported earlier? The practitioner would need to resolve the problems to perform an attest engagement on that subject matter.

If the criteria have changed since a previous period's report, the practitioner should also consider consistency issues. Lesson two discusses consistency.

Independence. The fourth general standard requires the practitioner to maintain an independence in mental attitude. Practitioners performing attestation engagements must be independent pursuant to Rule 101 of the AICPA *Code of Professional Conduct* (ET 101). In general terms, that means that there must be an absence of financial interest in both the entity and the outcome of the engagement. For example, the practitioner cannot accept the engagement if he or she has:

- A direct or indirect financial interest in the entity. See Rule 101 of the *Code of Professional Conduct* (ET 101).
- A contingent fee arrangement with the client for this engagement or any other engagement the practitioner performs for the client. See Rule 302 of the *Code of Professional Conduct* (ET 302).
- An interest in the subject matter of the engagement. (For example, the practitioner should not examine and report on the effectiveness of computer software if he or she also planned to be a licensed distributor of that software.)

As in traditional accounting and auditing services, the practitioner may assist the client in developing the subject matter and still remain independent. However, SSAE No. 10 requires management to accept responsibility for the subject matter or provide evidence of a third party's responsibility for the subject matter. If the practitioner is providing nonattest services for an attest client, he or she should follow Ethics Interpretation 101-3, "Performance of Nonattest Services," (ET 101.05) from the AICPA *Code of Professional Conduct*.

The practitioner also needs to consider ET section 100, *Conceptual Framework for AICPA Independence Standards*. The framework discusses seven types of potential threats to independence and, if they exist on a particular engagement, the need to consider and document whether safeguards sufficiently mitigate them.

In some attestation engagements (for example, a proposed acquisition), the client may not be the responsible party. When that is the case, must the practitioner be independent of both the client and the responsible party? It is believed that the practitioner should be independent of both. Otherwise, the practitioner may be seen as being biased in the performance of his or her procedures. Also, professional standards seem to require independence of both the client and the responsible party. ET 92.03 states that the term *client* includes both the entity that engages the CPA and the entity with respect to which professional services are performed. In an attestation engagement, it is the responsible party with respect to which professional services are performed.

Interpretation 101-11 of Rule 101 (ET 101.13) provides guidance about the application of Rule 101 to attest engagements when the report is restricted to specified parties (that is, agreed-upon procedures reports or reports

that are restricted because the criteria are appropriate only for specified parties). Interpretation 101-11 does not require that all members of the firm be independent of the responsible party. Instead, it requires that the members of the engagement team, individuals who directly supervise or manage the attest engagement, and individuals who consult with the attest engagement team regarding issues specific to the related engagement be independent. Independence is not required for other individuals in the firm. Independence would also be considered impaired if the firm has a financial relationship with the responsible party that is covered by Interpretation 101-1A (ET 101.02) and is material to the firm.

Other Engagement Alternatives. If the practitioner cannot meet all of the performance requirements of an attest engagement, he or she might be able to provide other services that will meet the client's needs under the consulting standards. In a consulting engagement, the practitioner does not provide an opinion on the client's information but generally states his or her own recommendations.

Practitioners are cautioned to take care when preparing the consulting report to ensure that the report does not mislead users into thinking an attest engagement was performed (and, therefore, that the requirements for performing such an engagement as discussed earlier were met).

Furthermore, if a practitioner's lack of independence precluded him or her from providing an attest engagement, it is recommended that the practitioner state the lack of independence in his or her consulting report (even though it is not required under the consulting standards).

Should I Accept the Engagement?

Risks and Rewards. The decision to accept an engagement is a professional judgment made after considering the potential risks and rewards. Rewards are generally related to the profit to be realized from the engagement. Profits may be immediate based on the fee involved, or they may be more long-term. For example, in order to gain exposure to a class of potential clients that may provide additional engagements later on, a practitioner might accept an engagement that initially is not very profitable.

Risks generally arise from:

- Clients of questionable integrity.
- Subject matter outside the internal control over financial reporting.
- Subject matter that is highly subjective.
- Criteria that are highly subjective.

Prospective Client's Reputation. The practitioner should consider the reputation of the prospective client and its management. Statement on Quality Control Standard No. 7 (QC 10.27) requires CPA firms to establish policies and procedures to provide the firm with reasonable assurance that it will undertake or continue relationships and engagements only where the firm has considered the integrity of the client. If ownership or operational control is concentrated in one or a few individuals, a primary consideration in client acceptance is the general honesty and good faith of the owner/manager.

Factors to Consider When Evaluating Integrity. When evaluating the integrity of the client, paragraph 30 of SQCS No. 7 offers the following factors to consider:

- Nature of operations and specific business practices.
- Attitude towards aggressive accounting and internal control matters.
- Length of the relationship with the client.

Gathering Evidence of Integrity. It is recommended that the firm consider conducting a thorough and complete screening of any current and prospective clients. For small firms and acceptance of relatively small clients,

cost-benefit considerations are involved in determining the extent to which the firm would ordinarily perform client screening. However, SQCS No. 7 requires firms to consider current and prospective client integrity, and it is believed that firms should consider performing thorough client screening procedures whenever feasible.

Communication with a Predecessor or Primary Practitioner. It is suggested that the practitioner who is considering accepting a new attestation engagement apply procedures similar to those in SAS No. 84 (AU 315), *Communications Between Predecessor and Successor Auditors*. The practitioner should obtain the prospective client's permission for communicating with the predecessor or primary practitioner. (This is necessary because of the ethical requirement for confidentiality.) The practitioner should also request that the client authorize the predecessor or primary practitioner to respond fully. If the prospective client refuses to provide this permission, the practitioner should find out why. Such a refusal is considered by many practitioners to be sufficient reason to turn down an engagement.

The precise form of the communication with a predecessor is not specified by SQCS No. 7. For example, a written communication is not required—simply talking with the predecessor is enough. If the client is currently served by another practitioner for recurring accounting or auditing services, it is suggested making inquiries of that practitioner regarding:

- Facts that may bear on the integrity of management.
- Significant disagreements with management.
- Communications to the audit committee (or its equivalent) regarding fraud or other illegal acts performed by the client or its employees, and internal control related matters.
- Whether the current practitioner refused to provide this attestation service and, if so, why.

If the client has previously used another accountant for recurring accounting and auditing services, but the firm is now picking up all of the client's work, the practitioner should inquire regarding the items discussed in the preceding paragraph. In addition, the practitioner should also ask about matters that may affect the conduct of the engagement, such as areas that required inordinate amounts of time or unusual items, and the predecessor's understanding of the reasons for the change in practitioners.

Depending on the nature of the subject matter, the practitioner might also need to review the workpapers of the predecessor or primary accountant.

Assessment of Required Services. A preliminary discussion with the prospective client is usually necessary to become familiar with the services that will be required. This allows the practitioner to consider whether the firm's resources are adequate to provide those services.

The preliminary discussion should include consideration of the following:

- *Expected Use of the Report.* Is the report needed to meet contractual requirements, to meet the requirements of a government agency, for the information of absentee owners, or for use in negotiating a sale of the business?
- *Need for an Examination or Review.* Is an examination or review essential for the intended use of the report? Does the prospective client understand the differing scopes, levels of assurance, and costs associated with examinations, reviews, and agreed-upon procedures?
- *Need for Other Services.* If an examination or review is needed, are other services such as consulting services or assistance with developing the assertion or subject matter also needed?
- *Reporting Deadlines.* Is the report needed at a particular date to meet the client's needs? Does the date allow sufficient time to perform the necessary testwork?

Engagement Acceptance and Continuation Forms. Before accepting an engagement, some firms find it useful to complete checklists that summarize relevant considerations.

Annual Evaluation for Continuing Engagement. SQCS No. 7 (QC 10.27) requires policies and procedures for assessing a continuing association with a client. Thus, if the attestation engagement is a recurring one, the practitioner should make the considerations discussed in this lesson and reassess the desire and ability to retain the engagement.

Should I Restrict the Use of My Report?

The attestation standards call for report restrictions in the following situations:

- 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. In this case, the report should be restricted to the client and those users who participated in the establishment of the criteria or are presumed to understand them.
- When the criteria used to evaluate the subject matter are available only to specified parties. The report should be restricted to the client and those who have access to the criteria.
- When reporting on subject matter and a written assertion has not been provided by the responsible party. In this case, it is believed the report should be restricted to the client, except when there are exceptions for certain regulatory requirements.
- When the report is on an attestation engagement to apply agreed-upon procedures to the subject matter. The report should be restricted to the client and those who agreed to the procedures.

The standards suggest that the practitioner consider informing the client that restricted-use reports are not intended for distribution to nonspecified parties, regardless of whether they are included in a document containing a separate general-use report. AT 101.79 also notes that the practitioner is not responsible for controlling a client's distribution of restricted-use reports. In addition, it notes that a restricted-use report filed with a regulatory agency may be required by law or regulation to be made available to the public as a matter of public record. A restricted-use report should alert readers by indicating that the report is not intended to be and should not be used by anyone other than the specified parties.

Including a restricted-use report in a document that includes a general-use report does not affect the intended use of either report. However, if two such reports are combined into a single report, it should be restricted to the specified parties.

Unless circumstances other than those addressed above exist, a practitioner is not required to restrict the use of the attestation report. However, the practitioner is not *prohibited* from restricting the use of any report. It is suggested that a practitioner who believes that restriction may be desirable consider the following issues:

- Are the criteria really suitable, or is the desired restriction a response to criteria that are questionable in the circumstances?
- Will the proposed restriction mitigate the practitioner's risk of lawsuits? (The answer to this may depend on the accountancy laws or legal climate in the practitioner's state.)
- Will the client accept the proposed restriction?

SELF-STUDY QUIZ

Determine the best answer for each question below. Then check your answers against the correct answers in the following section.

12. A practitioner performing an attestation engagement must be competent to do so. Which of the following statements best describes the practitioner's competence?
 - a. The requirement in the attestation standards to have adequate technical training and proficiency in the attest function is probably the least transferable of the skills practitioners develop in auditing.
 - b. The attestation standards call for the practitioner to have adequate knowledge of the subject matter to which he or she is to attest.
 - c. Practitioners are required to have the necessary knowledge in the subject matter before accepting an engagement.
 - d. Knowledge of the subject matter is consistent from engagement to engagement.
13. According to the third general attestation standard, a practitioner can perform an engagement only if he or she has reason to believe the criteria to be used in the engagement are suitable, among other things. Which of the following statements best describes the suitability of criteria?
 - a. Criteria established by a group that has been designated by AICPA Council to establish criteria is sometimes presumed to be suitable.
 - b. For any subject matter, there is only one criteria that is suitable for use in an attestation engagement.
 - c. Criteria established by a body composed of experts that follow due-process procedures, including procedures for distribution of proposed criteria for public comment, is always presumed to be suitable.
 - d. To determine if criteria are suitable for the engagement, the practitioner needs to consider whether they are objective, measurable, complete, and relevant.
14. The fourth general standard requires the practitioner to maintain an independence in mental attitude when performing an attestation engagement. Which of the following statements best describes the independence requirement?
 - a. The practitioner can assist the client in developing the subject matter and still remain independent.
 - b. Rule 101 of the AICPA *Code of Professional Conduct* allows the practitioner to have up to a 10% financial interest in the entity without affecting his or her independence.
 - c. A contingent fee arrangement with the client would not affect a practitioner's independence as long as the possible fee does not exceed 20%.
 - d. When the client is not the responsible party, the practitioner must be independent of the client.
15. The attestation standards require a practitioner to restrict the use of the report in a number of circumstances. Which of the following statements about restricted-use reports is correct?
 - a. Restricted-use reports are not intended for distribution to nonspecified parties, unless they are included in a document containing a separate general-use report.
 - b. The practitioner is responsible for controlling a client's distribution of restricted-use reports.
 - c. A restricted-use report filed with a regulatory agency may be required by law or regulation to be made available to the public as a matter of public record.
 - d. A restricted-use report is inadequate to alerting readers that the report is not intended to be and should not be used by anyone other than the specified parties.

SELF-STUDY ANSWERS

This section provides the correct answers to the self-study quiz. If you answered a question incorrectly, reread the appropriate material. **(References are in parentheses.)**

12. A practitioner performing an attestation engagement must be competent to do so. Which of the following statements best describes the practitioner's competence? **(Page 155)**
 - a. The requirement in the attestation standards to have adequate technical training and proficiency in the attest function is probably the least transferable of the skills practitioners develop in auditing. [This answer is incorrect. In fact, this requirement is probably the most transferable skill the practitioner learns from providing auditing services, per the Standards.]
 - b. The attestation standards call for the practitioner to have adequate knowledge of the subject matter to which he or she is to attest. [This answer is correct. According to the Attestation Standards, the second general standard calls for the practitioner to have adequate knowledge of the subject matter. The practitioner must have or obtain an understanding of the subject matter to which he or she is to attest. Knowledge of the subject varies by engagement.]**
 - c. Practitioners are required to have the necessary knowledge in the subject matter before accepting an engagement. [This answer is incorrect. That knowledge can be obtained after acceptance. However, in making the acceptance decision, practitioners must consider whether they have, or will be able to obtain, the requisite knowledge.]
 - d. Knowledge of the subject matter is consistent from engagement to engagement. [This answer is incorrect. The required knowledge varies by engagement. Sometimes it requires little more than common sense, such as in an engagement to attest to the number of square feet in a warehouse. Other times it requires substantial familiarity with complex subjects, such as actuarial data. The practitioner can obtain this knowledge through formal education, experience, or by using a specialist.]
13. According to the third general attestation standard, a practitioner can perform an engagement only if he or she has reason to believe the criteria to be used in the engagement are suitable, among other things. Which of the following statements best describes the suitability of criteria? **(Page 156)**
 - a. Criteria established by a group that has been designated by AICPA Council to establish criteria is sometimes presumed to be suitable. [This answer is incorrect. According to the Standards, criteria established by such a group is *always* presumed to be suitable.]
 - b. For any subject matter, there is only one criteria that is suitable for use in an attestation engagement. [This answer is incorrect. There is often a number of suitable criteria that can be used. The choice among alternative criteria often involves trade-offs. For example, to use an analogy from financial reporting, the cash basis of accounting is more reliably measured than GAAP, as it includes no estimates or contingencies that must be reported before they are settled. On the other hand, GAAP is generally considered more relevant for certain types of decisions because it captures noncash assets and liabilities. Thus, each set of criteria is considered suitable for measuring financial results; the choice between the two criteria is generally made based on the ultimate use of the financial statements. Similar judgments must be made for other types of subject matter, particularly when there are no established criteria. For example, customer satisfaction might be usefully measured based on the number of customer complaints, on the number of repeat purchases, or on other bases. Or, measuring speed of a computer's operating system might involve measuring how fast the computer boots, how fast it accepts data, how fast it processes data, or some combination of those activities.]**
 - c. Criteria established by a body composed of experts that follow due-process procedures, including procedures for distribution of proposed criteria for public comment, is always presumed to be suitable. [This answer is incorrect. According to the Standards, criteria established by such a group is presumed to *ordinarily* be suitable.]

- d. **To determine if criteria are suitable for the engagement, the practitioner needs to consider whether they are objective, measurable, complete, and relevant. [This answer is correct. However, the users may agree on any criteria they believe useful for their purposes, even if the practitioner is not satisfied that it meets this four-part test. Such criteria might be useful for the users' purposes, but not for use by other persons. In that case, the presentation and the practitioner's report should be restricted to the use of those who agreed on the criteria or those whom the practitioner can presume to have an adequate understanding of them.]**
14. The fourth general standard requires the practitioner to maintain an independence in mental attitude when performing an attestation engagement. Which of the following statements best describes the independence requirement? **(Page 159)**
- a. **The practitioner can assist the client in developing the subject matter and still remain independent. [This answer is correct. The practitioner may assist the client in developing the subject matter and still remain independent. However, SSAE No. 10 requires management to accept responsibility for the subject matter or provide evidence of a third party's responsibility for the subject matter.]**
- b. Rule 101 of the AICPA *Code of Professional Conduct* allows the practitioner to have up to a 10% financial interest in the entity without affecting his or her independence. [This answer is incorrect. Rule 101 of the *Code of Professional Conduct* prohibits the practitioner from having a direct or indirect financial interest in the entity.]
- c. A contingent fee arrangement with the client would not affect a practitioner's independence as long as the possible fee does not exceed 20%. [This answer is incorrect. Rule 302 of the *Code of Professional Conduct* prohibits the practitioner from having any contingent fee arrangement with the client for an attest engagement or any other engagement the practitioner performs for the client.]
- d. When the client is not the responsible party, the practitioner must be independent of the client. [This answer is incorrect. Best practices indicate that the practitioner should be independent of both. Otherwise, the practitioner may be seen as being biased in the performance of his or her procedures. Also, professional standards seem to require independence of both the client and the responsible party. ET 92.03 states that the term *client* includes both the entity that engages the CPA and the entity with respect to which professional services are performed.]
15. The attestation standards require a practitioner to restrict the use of the report in a number of circumstances. Which of the following statements about restricted-use reports is correct? **(Page 162)**
- a. Restricted-use reports are not intended for distribution to nonspecified parties, unless they are included in a document containing a separate general-use report. [This answer is incorrect. According to the Standards, restricted-use reports are not intended for and should not be distributed to nonspecified parties, regardless of whether they are included in a document containing a separate general-use report.]
- b. The practitioner is responsible for controlling a client's distribution of restricted-use reports. [This answer is incorrect. According to the Standards, practitioner cannot control a client's report distribution. All he or she can do is communicate to the client that such reports should not be distributed to nonspecified parties.]
- c. **A restricted-use report filed with a regulatory agency may be required by law or regulation to be made available to the public as a matter of public record. [This answer is correct. Laws or regulations can require certain restricted-use reports to become a matter of public record if it is filed with a regulatory agency.]**
- d. A restricted-use report is inadequate to alerting readers that the report is not intended to be and should not be used by anyone other than the specified parties. [This answer is incorrect. Restricted use reports are required to include language that warns nonspecified users that the report is not intended to be and should not be used by anyone other than the specified parties. Accordingly, the report is adequate to warn users of the risk of relying on the report for their own purposes.]

ENGAGEMENT PLANNING

Establishing the Terms of the Engagement

Required Understanding. SSAE No. 10 requires the practitioner to obtain an understanding with the client, which should include:

- *The Objectives of the Engagement.* The practitioner should address the objectives of the engagement and any limitations thereon primarily through discussions with the client about the level of services the practitioner will provide. An attestation engagement might comprise an examination, review, or application of agreed-upon procedures. The practitioner should also consider whether a consulting engagement, while not resulting in an attestation report, might meet the client's needs at a lower cost. The practitioner should discuss the various alternatives with the client to determine the client's needs and preference.
- *Client's Responsibilities.* In an examination or review attestation engagement, the client must select the criteria and determine that it is appropriate for its purposes. If the client is the responsible party, the client is also responsible for the subject matter (or related assertion) to which the practitioners will perform their procedures. Furthermore, a client who is also the responsible party must provide the practitioner with a written assertion.
- *Practitioner's Responsibilities.* The practitioner's responsibilities are linked closely to the services he or she will provide. Practitioners are encouraged to describe those services as precisely as possible to avoid misunderstandings that might arise. Depending on the types of services to be rendered, those responsibilities might include performing specific procedures on a monthly basis, providing certain services on an as-needed basis, and reporting the results either informally or in writing.
- *Limitations of the Engagement.* The limitations that practitioners should address relate to at least two aspects of each engagement: (a) limitations of the types of services to be performed and (b) use limitations based on the type of service. For example, in a review engagement, the practitioner provides only moderate assurance that the subject matter is in conformity with the criteria against which it is measured. The client should understand the difference between the opinion the practitioner issues in an examination and the report in a review engagement.

In addition, the client should understand that, in some cases, the use of the practitioner's report would be limited. For instance, if a written assertion is not obtained from the responsible party, the practitioner's report would be restricted. If a restricted-use report is not acceptable to the client, the practitioner should discuss engagement alternatives that would provide a practitioner's report appropriate for general use.

Other Matters. Other matters practitioners should consider discussing with the client include:

- *Subject Matter to Which Procedures Are to Be Applied.* The practitioner should determine specifically the subject matter to be reported on. This understanding should be used to determine that the practitioner has, or can acquire, sufficient expertise to perform the engagement. The practitioner should also understand whether he or she will report directly on the subject matter or on the assertion about the subject matter. (As discussed in lesson 2, this is primarily a reporting issue.)
- *Criteria.* The criteria to be used must be both suitable and available to users. (See discussion earlier in this lesson.)
- *Users of the Practitioner's Report.* Knowing who the potential users are helps the practitioner assess the risks in the engagement and also provides information regarding the appropriateness of the service to be provided. Certain classes of users generally pose greater risk to the practitioner. High-risk users include those who are likely to view the report as a guarantee such as those who will use the report as a basis for the sales price of a business or government regulators.

The practitioner should also understand how broadly the report will be used. The report might be relied on by many potential users, such as in a report on a mutual fund's investment performance. Or, it might be

for the benefit of a limited number of users, such as a report on sales to be used to calculate rent under a lease agreement. This information serves two purposes:

- It helps the practitioner assess exposure to litigation or other claims. The information might suggest that the presentation and report will be relied on for purposes other than those for which it was intended.
- It helps the practitioner determine the appropriateness of the presentation and form of report. For example, the practitioner may report using criteria that, although not otherwise suitable, have been agreed to by the user and the client. But such a report should be restricted to the users who agreed on the criteria or who can be presumed to understand it. The report is not appropriate for general use.
- *Logistics.* The practitioner should ascertain whether the client has the necessary personnel and expertise to develop the subject matter. The practitioner may assist the client in developing the subject matter, including the related disclosures or underlying data. However, the level of practitioner involvement in this exercise may affect the timing of the engagement and the nature and extent of the attestation procedures applied. The use of client personnel or internal auditors in an agreed-upon procedures engagement requires additional considerations.

Larger clients might provide internal audit assistance to the practitioner. In such cases, it is suggested that the practitioner look to SAS No. 65 (AU 322), *The Auditor's Consideration of the Internal Audit Function in the Audit of Financial Statements*, for general guidance on the competence and objectivity of internal auditors, the nature, timing, and extent of work to be performed, and other matters.

- *Fees.* The practitioner should determine that the fee arrangements are appropriate. Considerations include:
 - The size of the fee relative to the amount of effort required and risk assumed.
 - The form of the fee (for example, contingent fees).
 - The timing of the payment (for example, whether retainers or progress payments are required).

When the Client Is Not the Responsible Party. A practitioner can perform an attestation service when the engaging entity is not the party responsible for the subject matter. This might occur, for example, when a potential buyer of a business wants the seller's information examined. The logistics of such an engagement are more difficult. The practitioner needs to apply procedures, make inquiries, and obtain representations from the responsible party because that is the entity that takes responsibility for the presentation of the subject matter (or related assertion). The AICPA has identified the failure to clearly identify the responsible party and/or the failure to have the responsible party accept responsibility for its assertions or subject matter as a significant engagement deficiency.

When the client is not the responsible party, the practitioner is required to obtain evidence of the responsible party's responsibility for the subject matter or assertion. This evidence might be, for example, in an engagement letter or representation letter, within the presentation of the subject matter (including notes), in a written assertion, or stated in legislation, regulation, or contracts.

The respective responsibilities and expectations should ideally be made clear in the engagement letter. Also, best practices indicate that the practitioner should be independent of both the client and the responsible party.

Engagement Letters. The use of engagement letters in attestation engagements is strongly recommended. Engagement letters are particularly important in nontraditional engagements because of the increased risk of misunderstanding the nature of the practitioner's responsibilities. Additionally, when the practitioner provides a service more limited than an examination, the need for an engagement letter that explains the limitation of the service becomes more important. (When engagement letters are not obtained, the understanding of the engagement should be obtained and documented in the workpapers.)

Given the nature of attestation engagements, some practitioners may include language in their engagement letters that allows or requires disagreements with the client to be settled through alternative dispute resolution (ADR). ADR

is an increasingly popular way of attempting to resolve client disputes without exposing the firm to the cost and uncertainty of litigation. ADR takes less time than litigation and provides a better chance of preserving the client/accountant relationship. There are basically two types of ADR techniques—arbitration and mediation. ADR techniques apply primarily to client disputes (for example, fee disputes) rather than third-party users. However, ADR also has potential drawbacks. Some practitioners believe it provides a *free shot* to a claimant since there is little or no cost to bringing a claim. Also, there is no guarantee that the losing party might not choose to pursue the claim in litigation. Practitioners should consult with both legal counsel and their insurance carriers before including ADR clauses in their engagement letters.

Some firms have included language in engagement letters requiring the client to indemnify them if they are sued by a third-party for misstatements in assertions resulting from false representations made to the practitioner by the client. AICPA Ethics Ruling No. 94 under Rule 101 (ET 191.188–189) states that including such a clause in the engagement letter will not impair an auditor's independence. While the SEC has concluded that these clauses impair the independence of auditors of public companies, some firms still use them in audits of nonpublic companies. Practitioners might consider including such clauses in attestation engagements. However, including an indemnification clause may create client resistance, so the practitioner must apply professional judgment. Practitioners should consult with both legal counsel and their insurance carriers before including indemnification clauses in their engagement letters.

Practitioners may refer to *PPC's Guide to Managing an Accounting Practice* and *PPC's Guide to Audits of Nonpublic Companies* for a more detailed discussion of protective language in engagement letters and alternative dispute resolution.

Understanding the Subject Matter

The practitioner must understand the subject matter on which he or she is to report. This includes understanding both its nature and the transactions or events that give rise to its measurement. It may also involve understanding the client's industry and how its business operates.

For example, in a report on income per square foot in a building, the practitioner would need to understand whether the square feet to be measured include only usable area, rentable area, or total area. In addition, the practitioner would need to determine whether rental income is to include only basic rent or whether it should also include common area charges.

When engaged to examine or review complex or controversial matters, the practitioner may need assistance in determining the correct interpretation in the circumstances. In that case, the practitioner might consider reports of outside consultants, legal interpretations, regulatory requirements, industry practice, or similar sources of information. The practitioner may also enlist the aid of a specialist when confronted with the need for particular expertise. Lesson 2 provides guidance on using a specialist in an examination engagement.

Materiality

The concept of materiality applies to attestation engagements as it does to traditional engagements on financial statements. AT 101.67 defines materiality as the magnitude of omissions or misstatements—individually or when aggregated with others—that would influence a reasonable person. The relative, rather than absolute, size of an omission or misstatement determines whether it is material in a given situation.

Practitioners generally consider materiality at two different phases of the engagement: the planning stage and the evaluation stage. The planning stage is discussed in the following paragraphs. The evaluation stage is discussed in lesson 2.

In the planning stage, the practitioner considers materiality in order to plan the scope of the attestation procedures so that they will detect misstatements that would be considered material. The practitioner considers, based on a preliminary estimate of the subject matter to be presented, what level would be likely to be considered material to the presentation when the engagement is completed.

When the assertion is expressed in financial amounts, the tables presented in Exhibit 1-4 can generally be used for estimating materiality for planning purposes. However, the practitioner might conclude that, based on user needs,

materiality should be lower for the presentation of the subject matter, or for some elements of it, than indicated in the tables.

Materiality is related to the subject matter, rather than to the level of service. The same materiality measures apply to both examination and review engagements. What differs between the two services is the nature and extent of procedures applied.

When the subject matter is not expressed in financial amounts, but is nonetheless numeric (for example, the number of tons of trash processed), it is believed that table 1 shown in Exhibit 1-4 can still be used. Although the table is based on judgments regarding financial statements taken as a whole, the overall percentages are also considered appropriate for determining materiality for numeric subject matter (that is, the percentages begin at 4% and decrease as the materiality base increases).

Exhibit 1-4

Guidelines for Determining Planning Materiality

Table 1—Benchmark Is Total Assets or Total Revenue

If the total dollar amount of the assertion (the <i>base</i>) is:		Planning materiality is:
Over	But less than	Amount + (Percent × Base)
0	100 thousand	0 + 4.0%
100 thousand	500 thousand	2,000 + 2.0%
500 thousand	1 million	7,000 + 1.0%
1 million	5 million	8,000 + 0.9%
5 million	10 million	13,000 + 0.8%
10 million	50 million	23,000 + 0.7%
50 million	100 million	73,000 + 0.6%
100 million	500 million	153,000 + 0.52%
500 million		503,000 + 0.45%

Table 2—Other Benchmarks and Illustrative Percentages

Benchmark	Illustrative Percentage
Total revenue/total assets	1/2%–1%
Gross profit	1%–2%
Pretax income	5%–10%
Net income	3%–5%
Equity	1%–2%

* * *

Subject matter that is not numeric (for example, the effectiveness of a piece of software) presents more complex materiality judgments. In those cases, the practitioner might try to quantify some aspect of the subject matter as a

basis for a materiality judgment. For example, the practitioner might be able to quantify a tolerable rate (such as failures per 1,000 transactions). Lesson 2 presents a sampling approach for nonnumeric subject matter that incorporates this approach to determining planning materiality. This approach can also be used for numeric subject matter if the practitioner is concerned with the rate of misstatements rather than the amount (for example, dollar amount) of misstatements.

In some cases, the nature of the subject matter may require that materiality be determined using some method other than those described here. If the client's assertion is such that the practitioner's primary concern is understatement (for example, an assertion that rejected production units do not exceed 5% of total units produced), the practitioner's materiality amount may need to be based on a reciprocal population of the subject matter (for example, units produced rather than units rejected). Also, if the client's assertion is that no occurrences of an event took place (for example, no production units were rejected), the occurrence of only one such event might be considered material. The practitioner's materiality judgment must be appropriate for the purpose of the engagement. The methods discussed in this section should be viewed only as guidelines for making that decision.

Attestation Risk

Attestation risk is the risk that the practitioner will fail to detect a material misstatement in the subject matter. It is analogous to the concept of audit risk discussed in SAS No. 107 (AU 312), *Audit Risk and Materiality in Conducting an Audit*. In an examination engagement, the practitioner is required to reduce this risk to a low level. In a review engagement, risk must be reduced to a moderate level.

Attestation risk, like audit risk, is composed of three components:

- *Inherent Risk*. The susceptibility of the subject matter to material misstatement.
- *Control Risk*. The risk that a material misstatement that did occur would not be prevented or detected by the client.
- *Detection Risk*. The risk that a material misstatement that eludes the client will also elude the practitioner.

The first two components reflect the likelihood that the subject matter contains a material misstatement. The practitioner can assess these two risks but cannot control them. The third component is the likelihood that the practitioner fails to detect a misstatement that does exist. The practitioner controls this risk through the selection and application of tests. When the first two risks are high, the practitioner's tests must be more effective to reduce detection risk and adequately control attestation risk. When they are lower, the practitioner may do correspondingly less work to reduce detection risk.

Inherent and control risks can be assessed separately or in combination (when combined, they are called *risk of material misstatement* in SAS No. 107). Also, as in an audit, they can be assessed in either qualitative or quantitative terms. It is recommended that a qualitative assessment be used and that the two risk assessments be combined to determine an overall risk of material misstatement. Exhibit 1-5 provides an example of how qualitative levels of inherent risk and control risk could be combined to establish an overall risk of material misstatement. Based on the practitioner's judgment, other combinations may also be appropriate. Unlike under GAAS, documenting the risk of material misstatement is not required, though it is needed to apply the sampling approach discussed in lesson 2.

Exhibit 1-5
Combining Inherent Risk and Control Risk

Inherent Risk	×	Control Risk	=	Risk of Material Misstatement
High		High		High
High		Moderate		High
High		Low		Moderate
Moderate		High		Moderate
Moderate		Moderate		Low
Moderate		Low		Low
Low		High		Low
Low		Moderate		Low
Low		Low		Low

Note:

- ^a How the practitioner combines inherent and control risk to assess the risk of material misstatement is subject to the practitioner's judgement.

* * *

Administrative Aspects of Planning

SSAE No. 10 does not detail the procedures to be applied in planning the engagement, but the practitioner might consider the following procedures:

- Reviewing correspondence files, prior year workpapers and reports, and permanent files.
- Discussing matters that may affect the engagement with firm personnel responsible for other services to the entity.
- Inquiring about current business developments affecting the entity.
- Reading the current year's financial statements (or, in an attestation engagement, the current year's subject matter).
- Discussing the type, scope, and timing of the engagement with the entity's management, board of directors, or audit committee.
- Coordinating the assistance of entity personnel in data gathering.
- Determining the extent of involvement, if any, of consultants, specialists, and internal auditors.
- Establishing and coordinating staffing assignments.

Adequate supervision of an attestation engagement includes guiding assistants and reviewing their work. Assistants should be informed about their responsibilities, including the objectives of the procedures they are to perform and matters that affect the nature, extent, and timing of the procedures. They should also be directed to bring to the practitioner's attention any significant questions raised during the engagement.

Planning the Procedures

It is recommended that the practitioner prepare a written work program specifying the procedures necessary to complete the engagement. The actual program used depends on the type of engagement and firm policy, but the

authors believe the program should be in sufficient detail to enable assistants to understand the procedures they are to apply and allow the partner or manager to determine if the scope of testing is appropriate in the circumstances.

Reports

As a result of the attestation engagement, the practitioner issues a report. In an examination, the standard report states the practitioner's opinion that either (a) the assertion about the subject matter is fairly stated, in all material respects, based on the criteria or (b) the subject matter is in conformity with the selected criteria, in all material respects. In a review, the standard report states that nothing came to the practitioner's attention to indicate the subject matter is not presented, in all material respects, based on the criteria or a statement that nothing came to the practitioner's attention to indicate the assertion about the subject matter is not based on the criteria, in all material respects.

SSAE No. 10 requires modified reports when:

- The scope of an examination engagement has been restricted (no report is issued when a review engagement's scope has been restricted).
- The practitioner believes the subject matter is materially misstated.
- The report is to be restricted to the use of specified parties when any of the circumstances discussed under Report Restrictions in lesson 2 exist.

Applicability of Risk Assessment SASs to Attest Engagements

SAS No. 99 (AU 316), *Consideration of Fraud in a Financial Statement Audit*, requires the auditor to identify and assess risks of material misstatement due to fraud and to design the audit to provide reasonable assurance of detecting fraud that results in the financial statements being materially misstated. It also requires certain specific procedures.

The risk-assessment standards, SAS Nos. 104–111, like SAS No. 99, apply only to audits of financial statements, not attestation engagements. The standards are effective for audits of financial statements for periods beginning on or after December 15, 2006. The procedure and documentation requirements of those SASs tend to be more rigorous than their attestation counterparts.

Some practitioners have asked whether they should consider the requirements of SAS No. 99 and the risk assessment standards when performing an examination engagement under the attestation standards. Because the SASs apply only to audits of financial statements, the practitioner is not required to follow—or even consider—their requirements when performing an engagement under the attestation standards. Often, many of the aspects of the SASs are not relevant to the subject matter of the attestation engagement. However, nothing precludes the practitioner from considering their requirements and performing analogous procedures if they are relevant to the engagement and, in the practitioner's judgment, helpful in planning or performing the attest engagement. Throughout this course, it has been suggested importing into attestation engagements concepts more meticulously developed in GAAS as a way of operationalizing the more general requirements in the attestation standards. However, as previously stated, the use of the guidance in SASs is not required in engagements performed under the attestation standards (except when the attestation standards specifically incorporate them). Moreover, readers should not infer the conclusion that all analogous SAS guidance is necessarily appropriate for attestation engagements.

Engagements to perform *audits* of specified elements must be performed in accordance with GAAS.

SELF-STUDY QUIZ

Determine the best answer for each question below. Then check your answers against the correct answers in the following section.

16. Practitioners performing attestation engagements also must consider the concept of materiality. Which of the following best describes the practitioner's responsibility for materiality in an attestation engagement?
 - a. The absolute size of an omission or misstatement determines whether it is material in a given attestation engagement.
 - b. Practitioners generally consider materiality at two different phases of the engagement: the planning stage and the evaluation stage.
 - c. Materiality is related to the level of service rather than the subject matter.
 - d. Subject matter that is numeric presents the practitioner with more complex materiality judgments.
17. Which of the following statements about attestation risk is correct?
 - a. In a review engagement, the practitioner is required to reduce this risk to a low level.
 - b. Control risk is the susceptibility of the subject matter to material misstatement.
 - c. The practitioner can assess detection risk but cannot control it.
 - d. When inherent and control risks are high, the practitioner's tests must be more effective to reduce detection risk and adequately control attestation risk.
18. As a result of the attestation engagement, the practitioner issues a report. SSAE No. 10 requires a modified report in **all but which** of the following situations?
 - a. The scope of a review engagement has been restricted.
 - b. The practitioner believes the subject matter is materially misstated.
 - c. The report is to be restricted to the use of specified parties.
 - d. The scope of an examination report has been restricted.

SELF-STUDY ANSWERS

This section provides the correct answers to the self-study quiz. If you answered a question incorrectly, reread the appropriate material. **(References are in parentheses.)**

16. Practitioners performing attestation engagements also must consider the concept of materiality. Which of the following best describes the practitioner's responsibility for materiality in an attestation engagement? **(Page 168)**
- a. The absolute size of an omission or misstatement determines whether it is material in a given attestation engagement. [This answer is incorrect. The concept of materiality applies to attestation engagements as it does to traditional engagements on financial statements. The attestation standards define materiality as *the magnitude of omissions or misstatements—individually or when aggregated with others—that would influence a reasonable person*. Thus, it is the relative, rather than absolute, size of an omission or misstatement determines whether it is material in a given situation.]
 - b. Practitioners generally consider materiality at two different phases of the engagement: the planning stage and the evaluation stage. [This answer is correct. The practitioner's consideration of materiality in a review or examination attestation engagement is the same as it is in traditional engagements on financial statements and should be considered at two different phases of the engagement.]**
 - c. Materiality is related to the level of service rather than the subject matter. [This answer is incorrect. Materiality relates to the subject matter, not the level of service. For example, the same materiality measures apply to both examination and review engagements. What differs between the two services is the nature and extent of procedures applied.]
 - d. Subject matter that is numeric presents the practitioner with more complex materiality judgments. [This answer is incorrect. Subject matter that is not numeric presents greater challenges. In those cases, the practitioner might try to quantify some aspect of the subject matter as a basis for a materiality judgment. For example, the practitioner might be able to quantify a tolerable rate (such as failures per 1,000 transactions).]
17. Which of the following statements about attestation risk is correct? **(Page 170)**
- a. In a review engagement, the practitioner is required to reduce this risk to a low level. [This answer is incorrect. According to the Standards, the practitioner is required to reduce attestation risk only to a moderate level in a review engagement but to a low level in an examination engagement.]
 - b. Control risk is the susceptibility of the subject matter to material misstatement. [This answer is incorrect. As discussed in the Standards, inherent risk is the susceptibility of the subject matter to material misstatement. Control risk is the risk that a material misstatement that did occur would not be prevented or detected by the client.]
 - c. The practitioner can assess detection risk but cannot control it. [This answer is incorrect. According to the Standards, the practitioner can assess both inherent and control risks but cannot control them. He or she can only control detection risk, which is the risk that a material misstatement that eludes the client will also elude the practitioner. The practitioner controls detection risk through the selection and application of tests.]
 - d. When inherent and control risks are high, the practitioner's tests must be more effective to reduce detection risk and adequately control attestation risk. [This answer is correct. The practitioner's tests must be more effective when these risks are high to help discover any material misstatements affecting the engagement. When they are lower, the practitioner may do correspondingly less work to reduce detection risk.]**

18. As a result of the attestation engagement, the practitioner issues a report. SSAE No. 10 requires a modified report in all but which of the following situations? **(Page 172)**
- a. **The scope of a review engagement has been restricted. [This answer is correct. Although a practitioner may issue a modified report when the scope of an examination report has been restricted, no report is issued when a review engagement's scope has been restricted per SSAE No. 10.]**
 - b. The practitioner believes the subject matter is materially misstated. [This answer is incorrect. According to SSAE No. 10, the practitioner should modify the report when he or she believes the subject matter is materially misstated.]
 - c. The report is to be restricted to the use of specified parties. [This answer is incorrect. According to SSAE No. 10, the practitioner should modify the report when it is to be restricted to the use of specified parties. In this case, the report would include language that states that the report is not intended to be and should not be used by anyone other than the specified parties.]
 - d. The scope of an examination report has been restricted. [This answer is incorrect. According to SSAE No. 10, if the scope of an examination has been restricted, the practitioner should modify the report.]

WORKPAPERS

Authoritative Literature

SSAE No. 10 (AT 101), as amended, establishes the documentation requirements for all engagements performed under the Statement on Standards for Attestation Engagements (SSAEs). SSAE No. 10, as amended, states that *attest documentation* is commonly referred to as workpapers.

Purpose and Basic Requirements of Workpapers

The main purposes of attest documentation are identified in AT 101.101 as follows:

- Providing the principal support for the practitioner's report, including the representation on observance of the standards of fieldwork, which is implicit in the reference in the report to the attestation standards.
- Aiding the practitioner in the conduct and supervision of the attest engagement.

In addition to these purposes identified in AT 101, workpapers are important to the conduct of peer reviews by outside parties.

Support for Practitioner's Report. Naturally, the need to use workpapers to support the attest report only arises if the quality of the attest engagement is questioned, e.g., in litigation where a practitioner has to defend the quality of the engagement. A practitioner's defense, however, is not limited to what is in the attest documentation.

Workpapers are the principal record of the work done and conclusions reached, but a practitioner may support the attest report by other means. According to SSAE No. 10, as amended (AT 101.100 and related footnote 21):

Attest documentation is the principal record of the attest procedures applied, information obtained, and the conclusions reached by the practitioner in the engagement.

However, there is no intention to imply that the practitioner would be precluded from supporting his or her report by other means in addition to attest documentation.

If a practitioner can demonstrate by means other than workpapers that sufficient procedures were applied, the mere failure to record those procedures and the related evidence in the workpapers is not a failure to conform with professional standards. However, it is believed these "other means" should merely supplement the workpapers (for example, providing additional detail or clarifying ambiguities), not be the principal support for the practitioner's procedures and findings.

Aid to Conduct and Supervision. Good workpapers provide an organized framework for the attest engagement. According to AT 101.103, "attest documentation should be sufficient to (a) enable members of the engagement team with supervision and review responsibilities to understand the nature, timing, extent, and results of attest procedures performed, and the information obtained and (b) indicate the engagement team members who performed and reviewed the work."

Signatures and Sign-offs. Signatures and sign-offs are important in an attest engagement. They are used by engagement team members to indicate they have performed or reviewed work. In a paper environment, workpapers are signed or initialed by engagement team members to indicate they have completed or reviewed the workpaper. In an electronic environment, the same or similar type of sign-off is needed. In most cases, initials and names may simply be typed. Some electronic engagement software applications provide for an automatic and controlled sign-off by preparers and reviewers.

Basic Requirements for Content. According to SSAE No. 10, as amended, the form, quantity, and content of working papers should be designed to meet the circumstances of the particular engagement and are matters of the practitioner's professional judgment. Working papers are the principal record of the procedures applied, information obtained, and practitioner's conclusions or findings in the engagement. They may consist of work programs,

analyses, memoranda, letters of confirmation and representation, abstracts or copies of entity documents, and schedules or commentaries prepared or obtained by the practitioner. They may be in paper form, electronic form, or other media.

Workpapers should be sufficient to show that the standards of fieldwork have been observed as follows:

- The work has been adequately planned and supervised.
- Sufficient evidence has been obtained to provide support for the conclusion expressed in the report.

In addition, AT 101 requires documentation of the following:

- The engagement understanding, including the nature of the engagement, the responsible party's responsibilities, the practitioner's responsibilities, and limitations of the engagement.
- The nature, timing, and extent of the procedures applied.
- The results of the procedures applied.
- The information obtained.
- The engagement team members who performed and reviewed the work.

Finally, SSAE No. 13 requires that the practitioner document the justification for any departure from a presumptively mandatory requirement and a description of how the practitioner achieved its objectives.

Other Workpaper Considerations

Workpaper Ownership, Access, and Retention. Attest documentation is the practitioner's property. He or she should adopt reasonable procedures to retain it for a period of time sufficient to meet the needs of his or her practice and to satisfy any applicable legal or regulatory requirements for records retention. The procedures should enable the practitioner to access electronic attest documentation throughout the retention period.

AT 101 does not provide guidance on how long workpapers should be retained for attestation engagements. However, SAS No. 103, *Audit Documentation*, states that audit documentation for financial statement audits should be retained for at least five years. In addition, the procedures adopted should enable the practitioner to access electronic workpapers throughout the retention period. The Sarbanes-Oxley Act requires that workpapers for public company audit clients be maintained for seven years. This requirement is incorporated into PCAOB Auditing Standard No. 3, *Audit Documentation*. In the wake of the Act, several states have adopted similar provisions applicable to both public and nonpublic company audits, while other states and regulatory agencies have been actively considering appropriate documentation requirements. In addition, NASBA amended the UAA Model Rules to include a five-year record retention requirement unless otherwise specified by professional standards. Practitioners should monitor their state requirements, the activities of the ASB, and the PCAOB requirements, and establish appropriate workpaper retention policies for attestation as well as other types of engagements.

Record retention policies should generally correspond with the longest statute of limitations that prevails in states in which the firm does business. Records related to pending legal proceedings must be kept until the proceedings are completed. If workpapers are destroyed, that destruction should be in accordance with an established firm policy that is consistently applied.

The practitioner has an ethical, and in some situations a legal, obligation to maintain the confidentiality of client information or information of the responsible party. The practitioner is also required to adopt reasonable procedures to:

- Maintain the confidentiality of that information.
- Prevent unauthorized access to workpapers.

Certain working papers can serve as a useful reference source for the client, but they should not be regarded as a part of, or a substitute for, the client's records.

Access by Regulators to Workpapers. An attestation interpretation provides guidance to practitioners who are required to provide access or copies of workpapers to a regulator. According to the interpretation, practitioners who are requested to provide access or copies of workpapers to regulators should follow the guidance in AU 9339.01–.15. The following summarizes the guidance provided by the interpretation.

- a. If the practitioner is required by law, regulation, or engagement contract to provide access to workpapers to regulators, the auditor may wish (and in some cases be required) to include in the engagement letter an acknowledgment by the client that the workpapers are the property of the practitioner but that regulators may be provided access. The following language suggested in the interpretation and included in the engagement letters throughout this course can be used for this acknowledgment:

The attest documentation for this engagement is the property of [CPA Firm's Name] and constitutes confidential information. However, we may be requested to make certain attest documentation available to [Name of Regulator] pursuant to authority given to it by law or regulation. If requested, access to such attest documentation will be provided under supervision of [CPA Firm's Name] personnel. Furthermore, upon request, we may provide copies of selected attest documentation to [Name of Regulator]. The Name of Regulator may intend, or decide, to distribute the copies or information contained therein to others, including governmental agencies.

- b. If a regulator has requested access to workpapers pursuant to law, regulation, or engagement contract, the practitioner should:
 - (1) Consider notifying the client that a regulator has requested access (and in some cases photocopies of) the workpapers and the practitioner intends to comply with the request.
 - (2) Make the necessary arrangements for the review with the regulator.
 - (3) Maintain control over the original workpapers.
 - (4) Consider submitting a letter to the regulator before allowing access that:
 - (a) States the practitioner's understanding of the purpose for which access has been requested.
 - (b) Discusses the engagement process and the limitations inherent in the attestation engagement.
 - (c) Discusses the purpose for which the workpapers were prepared and explains that any individual conclusions must be interpreted in the context of the accountant's report.
 - (d) Communicates, except when not applicable, that the engagement was not planned or conducted contemplating the purpose for which access is being granted or to assess the client's compliance with laws and regulations.
 - (e) Communicates that workpapers and the attestation engagement should not substitute for other inquiries and procedures that should be performed by the regulator for its purposes.
 - (f) Requests confidential treatment under the Freedom of Information Act or similar laws or regulations when a request is made for the workpapers and that the practitioner be notified in writing before any information contained in the workpapers is transmitted to others, including other governmental agencies, unless such transfer is required under law or regulation.
 - (g) Requests that if any copies are to be provided by the practitioner, they will be identified as "Confidential Treatment Requested by [CPA Firm's Name, address, and telephone number]."

In an attestation engagement, the letter to the regulator should be tailored to meet the individual engagement characteristics. The attestation interpretation provides example letters the practitioner can use to communicate the above information to the regulator.

- c. If the practitioner has been requested to grant access to workpapers by a regulator and the practitioner is not required by law, regulation, or engagement contract to provide such access, the practitioner may wish to confer with his or her legal counsel regarding the request. In addition, the practitioner should obtain the client's consent, preferably in writing, before granting access to the regulator.

The audit interpretation at AU 9339.01–.15 also provides guidance to practitioners who have been requested to provide access to workpapers before the engagement is complete and the report has been issued. In addition, the interpretation notes that the practitioner should obtain an acknowledgment from the regulator that any third parties acting on behalf of the regulator, such as another CPA firm, are bound by the same restrictions on disclosure and use of the information in the workpapers as the regulator.

Access to Records by Clients and Former Clients. Ethics Interpretation 501-1 provides guidance on access to records by clients or former clients. It provides the following requirements for the various types of documents:

Type of Document	Description	Requirement to Provide to Client or Former Client
Client-provided	Document actually provided by the client or its representative	Return as soon as practicable, within 45 days
Client record prepared by practitioner	Record the practitioner was engaged to prepare	Provide as soon as practicable, within 45 days unless the engagement is incomplete or fees are unpaid for preparation of the document
Supporting record	Record prepared by the practitioner during the engagement	
Workpaper	Documentation of practitioner's work	No obligation to provide

For those documents the practitioner is required to provide, the practitioner—

- Is required to provide them only once, except in case of natural disaster or act of war.
- May charge a reasonable fee for retrieval and copying and require prepayment before providing the documents.
- May provide the document in any usable form, unless the practitioner was engaged to provide it in a specific form.
- May make and retain copies.

SELF-STUDY QUIZ

Determine the best answer for each question below. Then check your answers against the correct answers in the following section.

19. SSAE No. 10 establishes the documentation requirements for all engagements performed under the SSAEs. According to SSAE No. 10, which of the following best describes the purpose of workpapers in an attestation engagement?
- a. Workpapers are used as planning tools to determine the work to be done and who should do it.
 - b. A practitioner must have workpapers to support the attest report.
 - c. Workpapers should be sufficient to (a) enable members of the engagement team with supervision and review responsibilities to understand the nature, timing, extent, and results of attest procedures performed, and the information obtained and (b) indicate the engagement team members who performed and reviewed the work.
 - d. In a litigation situation where a practitioner has to defend the quality of the engagement, the practitioner's defense is limited to what is in the workpapers.
20. Jane Jones, CPA, has just opened up her new CPA firm. One of the first things Jane wants to do is develop policies and procedures for performing a number of different engagements, including attest engagements. Among the policies and procedures Jane wants to address is workpaper retention. Accordingly, Jane should consider **all but which** of the following in the new firm's policies and procedures?
- a. Because attest documentation is the practitioner's property, he or she should adopt reasonable procedures to retain it for a period of time sufficient to meet the needs of his or her practice and to satisfy any applicable legal or regulatory requirements for records retention.
 - b. Policies and procedures for workpaper retention should ensure that the practitioner can access electronic attest documentation throughout the retention period.
 - c. The attestation standards state that attest documentation should be retained for at least five years.
 - d. Practitioners should monitor their state requirements, the activities of the ASB, and the PCAOB requirements when establishing workpaper retention policies for attestation as well as other types of engagements.
21. Use the following information for questions 21–22: Rennan Windows, a former client of Lou Ann Hughes, CPA, requests certain workpapers from Ms. Hughes. Ms. Hughes consults the relevant ethics interpretation to determine whether she has a responsibility to comply with that request. Use this fact pattern to answer the following two questions. Ethics Interpretation 501-1 provides guidance on access to workpapers by clients or former clients. According to the interpretation, which of the following best describes Ms. Hughes' responsibilities to comply with the client's request?
- a. Ms. Hughes has no obligation to provide any workpaper prepared to document the firm's work.
 - b. Ms. Hughes should provide documents prepared by Rennan Windows' personnel as soon as practicable (within 45 days), unless the engagement is incomplete or fees are unpaid for preparation of the document.
 - c. For documents prepared by Ms. Hughes or her employees, Ms. Hughes should always provide them as soon as practicable, within 45 days.

22. Using the information included in question #21, for those documents which Ms. Hughes is required to turn over, which of the following best describes Ms. Hughes' responsibilities?
- a. Ms. Hughes is required to provide the workpapers as many times as the client requests them.
 - b. Ms. Hughes should not charge a fee for document retrieval.
 - c. Ms. Hughes must provide the documents in electronic format.
 - d. Ms. Hughes may make and retain copies.

SELF-STUDY ANSWERS

This section provides the correct answers to the self-study quiz. If you answered a question incorrectly, reread the appropriate material. **(References are in parentheses.)**

19. SSAE No. 10 establishes the documentation requirements for all engagements performed under the SSAEs. According to SSAE No. 10, which of the following best describes the purpose of workpapers in an attestation engagement? **(Page 176)**
- a. Workpapers are used as planning tools to determine the work to be done and who should do it. [This answer is incorrect. Workpapers are a record of the work actually done and conclusions actually reached and is not used to plan the engagement.]
 - b. A practitioner must have workpapers to support the attest report. [This answer is incorrect. The attestation standards state that there is no intention to imply that the practitioner would be precluded from supporting his or her report by other means in addition to attest documentation. Other means can be used to demonstrate that sufficient procedures were applied.]
 - c. **Workpapers should be sufficient to (a) enable members of the engagement team with supervision and review responsibilities to understand the nature, timing, extent, and results of attest procedures performed, and the information obtained and (b) indicate the engagement team members who performed and reviewed the work. [This answer is correct. Good workpapers provide an organized framework for the attest engagement.]**
 - d. In a litigation situation where a practitioner has to defend the quality of the engagement, the practitioner's defense is limited to what is in the workpapers. [This answer is incorrect. Per the Standards, if a practitioner can demonstrate by means other than workpapers that sufficient procedures were applied, the mere failure to record those procedures and the related evidence in the workpapers is not a failure to conform to professional standards. However, it is believed these "other means" should merely supplement the workpapers.]
20. Jane Jones, CPA, has just opened up her new CPA firm. One of the first things Jane wants to do is develop policies and procedures for performing a number of different engagements, including attest engagements. Among the policies and procedures Jane wants to address is workpaper retention. Accordingly, Jane should consider **all but which** of the following in the new firm's policies and procedures? **(Page 177)**
- a. Because attest documentation is the practitioner's property, he or she should adopt reasonable procedures to retain it for a period of time sufficient to meet the needs of his or her practice and to satisfy any applicable legal or regulatory requirements for records retention. [This answer is incorrect. According to the Standards, Jane should consider this when developing her firm's workpaper retention policy.]
 - b. Policies and procedures for workpaper retention should ensure that the practitioner can access electronic attest documentation throughout the retention period. [This answer is incorrect. According to the Standards, Jane's workpaper retention policy should consider electronic media as well as paper.]
 - c. **The attestation standards state that attest documentation should be retained for at least five years. [This answer is correct. AT 101 does not provide guidance on how long workpapers should be retained for attestation engagements. However, SAS No. 103, *Audit Documentation*, states that audit documentation for financial statement audits should be retained for at least five years.]**
 - d. Practitioners should monitor their state requirements, the activities of the ASB, and the PCAOB requirements when establishing workpaper retention policies for attestation as well as other types of engagements. [This answer is incorrect. The Sarbanes-Oxley Act requires that workpapers of public company audit clients be maintained for seven years. This requirement is incorporated into PCAOB Auditing Standard No. 3, *Audit Documentation*. Although these requirements apply only to public companies, they have caused several states to adopt similar provisions applicable to both public and nonpublic company audits. Other states and regulatory agencies have been actively considering

appropriate documentation requirements. Therefore, Jane should consider all of these factors when developing the firm's policies and procedures.]

21. Use the following information for questions 21–22: Rennan Windows, a former client of Lou Ann Hughes, CPA, requests certain workpapers from Ms. Hughes. Ms. Hughes consults the relevant ethics interpretation to determine whether she has a responsibility to comply with that request. Use this fact pattern to answer the following two questions. Ethics Interpretation 501-1 provides guidance on access to workpapers by clients or former clients. According to the interpretation, which of the following best describes Ms. Hughes' responsibilities to comply with the client's request? **(Page 179)**
- a. **Ms. Hughes has no obligation to provide any workpaper prepared to document the firm's work. [This answer is correct. According to Ethics Interpretation 501-1, Ms. Hughes is not bound to give her former client copies of workpapers prepared by her firm to document their procedures.]**
 - b. Ms. Hughes should provide documents prepared by Rennan Windows personnel as soon as practicable (within 45 days), unless the engagement is incomplete or fees are unpaid for preparation of the document. [This answer is incorrect. Ms. Hughes should return any document actually prepared by the client or its representative as soon as practicable and within 45 days. It is not dependent on the fees being paid.]
 - c. For documents prepared by Ms. Hughes or her employees, Ms. Hughes should always provide them as soon as practicable, within 45 days. [This answer is incorrect. Per Ethics interpretation 501-1, Ms. Hughes should provide such documents within the 45 day period, *unless the engagement is incomplete or fees are unpaid for preparation of the document.*]
22. Using the information included in question #21, for those documents which Ms. Hughes is required to turn over, which of the following best describes Ms. Hughes' responsibilities? **(Page 179)**
- a. Ms. Hughes is required to provide the workpapers as many times as the client requests them. [This answer is incorrect. Unless there is a case of natural disaster or an act of war, Ms. Hughes is required to provide the workpapers only once per Ethics interpretation 501-1.]
 - b. Ms. Hughes should not charge a fee for document retrieval. [This answer is incorrect. According to Ethics Interpretation 501-1, Ms. Hughes may charge a reasonable fee for retrieval and copying and require prepayment before providing the documents.]
 - c. Ms. Hughes must provide the documents in electronic format. [This answer is incorrect. Ms. Hughes may provide the document in any usable form, unless the practitioner was engaged to provide it in a specific form.]
 - d. **Ms. Hughes may make and retain copies. [This answer is correct. Ms. Hughes is entitled to keep copies of even those workpapers that she has to return to the client as stated in Ethics interpretation 501-1.]**

EXAMINATION FOR CPE CREDIT**Lesson 1 (NTETG102)**

Determine the best answer for each question below. Then mark your answer choice on the Examination for CPE Credit Answer Sheet located in the back of this workbook or by logging onto the Online Grading System.

1. Which of the following is the only type of compilation that is covered by attest standards?
 - a. Compilations of historical financial statements of nonpublic companies.
 - b. Compilations of cash basis financial statements.
 - c. Compilations of tax basis financial statements.
 - d. Compilations of prospective financial statements.
2. Which of the following technical committees of the AICPA can issue attestation standards?
 - a. The Accounting and Review Services Committee.
 - b. The Peer Review Board.
 - c. The Special Committee on Assurance Services.
 - d. The Professional Ethics Executive Committee.
3. Which of the following statements about the attestation standards is **incorrect**?
 - a. The SSAEs establish the basic standards for all attestation work that practitioners undertake.
 - b. An unconditional requirement in the attestation standards is designated by the term *should*.
 - c. All practitioners have to adhere to the 11 attestation standards.
 - d. The attestation standards consist of the general standards, the standards of fieldwork, and the reporting standards.
4. **All but which** of the following AICPA professional standards provide for the expression of assurance?
 - a. Statements on Auditing Standards.
 - b. Statements on Standards for Accounting and Review Services.
 - c. Statements on Standards for Attestation Engagements.
 - d. Statements on Standards for Consulting Services.
5. An assertion is not integral to determining whether the engagement is an attestation engagement. However, in most cases, the practitioner is required to obtain a written assertion while performing the engagement. Which of the following best describes the lack of a written assertion on the practitioner's report?
 - a. Only when the client is *not* the responsible party, the lack of a written assertion generally results in a scope limitation sufficient to preclude unqualified opinion.
 - b. Only when the client *is* the responsible party, the practitioner may be able to conclude that there is sufficient evidence to form a conclusion about the subject matter.
 - c. Whether or not the client is the responsible party, the attest report should be restricted to specified parties.
 - d. Only when the client is *not* the responsible party, the opinion should be on the subject matter rather than on the assertion about the subject matter, because there is no assertion on which to report.

6. Which of the following best describes the meaning of the term *responsible party* in an attestation engagement?
- a. The responsible party is always management of the entity whose performance is being measured.
 - b. A practitioner who helps assemble the subject matter is the responsible party in an attestation engagement.
 - c. The responsible party is the person or group whose actions, plans, or assumptions are reflected in the subject matter.
 - d. A practitioner cannot be hired by one party to provide an attestation service on someone else's subject matter. Thus, the responsible party must always be the client.
7. Sallie Mae has accepted an engagement to audit Rolling Meadows Nursing Home. Myron Neville, the adult child of Lucille Neville, a resident of Rolling Meadows, has engaged Sallie to provide an attestation report regarding the level of care being given to Lucille. What is the best way Sallie can obtain evidence regarding management's responsibility for the subject matter of the engagement?
- a. Interviewing the staff of Rolling Meadows.
 - b. Reviewing Rolling Meadow's contract with Lucille Neville.
 - c. Becoming an advocate for Lucille and Myron.
 - d. Provide tax advice for Lucille and Myron.
8. Which of the following types of engagements is an attestation engagement?
- a. Compilations of prospective financial information.
 - b. Engagements in which a practitioner is engaged to testify as an expert witness in accounting, auditing, taxation, or other matters, given certain stipulated facts.
 - c. Engagements in which the practitioner is engaged to advocate a client's position—for example, tax matters being reviewed by the Internal Revenue Service.
 - d. Tax engagements in which a practitioner is engaged to prepare tax returns or provide tax advice.
9. The three types of attestation engagements include examination, application of agree-upon procedures, and review. Which of these engagements generally is **not** recommended, according to the text?
- a. Examination.
 - b. Review.
 - c. Agreed-upon procedures.
 - d. Do not select this answer choice.

10. Which of the following statements regarding the criteria when accepting an attestation engagement is most accurate?
- a. A client is allowed to create criteria.
 - b. The level of service the practitioner provides is related to the need for suitable criteria.
 - c. GAAP and the COSO Report are the only sets of suitable criteria for attest engagements.
 - d. Do not select this answer choice.
11. When determining the availability and suitability of criteria used in an attestation engagement, which of the following will occur when the criteria is published by a group designated by the AICPA Council?
- a. The criteria is publicly available.
 - b. The criteria is unsuitable.
 - c. The criteria is suitable for restricted-use report.
 - d. The criteria are suitable for general use.
12. The Statement on Quality Control Standard No. 7 requires which of the following concerning the investigating of a potential client?
- a. Duration of the relationship with the client.
 - b. Nature of operations and specific business practices.
 - c. Attitude toward aggressive accounting and internal control matters.
 - d. Establish policies and procedures to provide the firm with reasonable assurance that it will engage in or continue relationships and engagements only where the firm has considered the client's integrity.
13. SSAE No. 10 requires the practitioner to obtain an understanding with the client that includes all of the following situations, **except**:
- a. The practitioner determines if the consulting engagement will meet the client's needs at a lower cost.
 - b. The practitioner performs specific procedures on a monthly basis or an as-needed basis.
 - c. The practitioner is responsible for the subject matter to which procedures are performed.
 - d. The practitioner is responsible for anything linked closely to the services the practitioner provides.
14. When addressing the objectives of the engagement with a larger client, best practices indicate that the practitioner refer to which of the following for general guidance on the internal auditor's skills, objectivity, nature, timing, and extent of work to be performed?
- a. SAS No. 65.
 - b. SAS No. 99.
 - c. SAS No. 103.
 - d. SAS No. 109.

15. Given the nature of attestation engagements, some practitioners may include language in their engagement letters that allows or requires disagreements with the client to be settled through alternative dispute resolution (ADR). Which of the following statements about ADR is correct?
- a. ADR attempts to resolve client disputes without exposing the firm to the cost and uncertainty of litigation.
 - b. The disadvantage of ADR is it takes more time than litigation but the advantage is it provides a better chance of preserving the client/accountant relationship.
 - c. There are basically three types of ADR techniques—arbitration, counseling, and mediation.
 - d. ADR techniques apply primarily to third-party users.
16. Attestation risk is the risk that the practitioner will fail to detect a material misstatement in the subject matter. Which component is concerned with the subject matter's susceptibility to material misstatement?
- a. Control risk.
 - b. Inherent risk.
 - c. Detection risk.
 - d. Do not select this answer choice.
17. Which of the following statements regarding record retention is **least** accurate?
- a. Practitioners should not regard certain workpapers as a substitute for the client's records.
 - b. Practitioners are ethically obligated to maintain client information confidentiality.
 - c. The practitioner is required to prevent unauthorized access to workpapers.
 - d. Practitioners generally are not legally obligated to maintain client information confidentiality.
18. Sometimes, practitioners are required to provide access or copies of workpapers to a regulator. Which of the following best describes a practitioner's responsibilities in this situation, according to the attest interpretation on that topic?
- a. Practitioners who are requested to provide access or copies of workpapers to regulators should obtain an acknowledgment from the regulator that any third parties acting on behalf of the regulator, such as another CPA firm, are bound by the same restrictions on disclosure and use of the information in the workpapers as the regulator.
 - b. If the practitioner has been requested to grant access to workpapers by a regulator and the practitioner is not required by law, regulation, or engagement contract to provide such access, the practitioner should not grant access to the regulator.
 - c. Even if a regulator has requested access to workpapers pursuant to law, regulation, or engagement contract, the practitioner should grant access to the regulator only after the client provides written consent.
 - d. If the practitioner is required by law, regulation, or engagement contract to provide access to workpapers to regulators, the auditor must include in the engagement letter an acknowledgment by the client that the workpapers are the property of the practitioner but that regulators may be provided access.

Lesson 2: Examination Engagements under the Attestation Standards

INTRODUCTION

In an examination engagement, the practitioner applies tests sufficient to reduce the risk of an undetected material misstatement to an appropriately low level. Accordingly, the level of testing is similar to an audit of financial statements. Therefore, in determining the scope of testing for an examination, it may be helpful to draw analogies to the auditing literature and common applications of auditing procedures.

Although this is a conceptually sound approach, audit requirements established by SASs do not generally apply to attestation engagements—statements on standards for attestation engagements do. Thus, this lesson describes how to determine the level of testing in an examination engagement performed under the attestation standards. It also describes the effect of test results on the practitioner's examination report and discusses other matter that might affect an examination engagement, including the practitioner's responsibilities when using the work of a specialist, discovering subsequent events, and including other information in a document that contains the practitioner's report. Finally, this lesson describes the matters commonly included in a representation letter, which specific workpapers are ordinarily included in an examination engagement, and all required elements of the practitioner's examination report.

Learning Objectives:

Completion of this lesson will enable you to:

- Identify the guidance provided about the required level of testing in an examination engagement performed under the attestation standards.
- Describe the approach to testing of numerical and nonnumeric information required in a particular examination engagement.
- Identify procedures necessary when using the work of a specialist, obtaining a representation letter from the responsible party, and discovering subsequent events.
- Describe the guidance provided on the elements included in the practitioner's examination report.

EXAMINATION ENGAGEMENTS

Internal Control. The attestation standards do not incorporate any specific requirement to obtain an understanding of internal control in an attestation engagement. Nonetheless, the guidance in SAS No. 109 (AU 314), *Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement*, may be helpful to the practitioner examining an assertion.

The subject matter of the engagement derives from client information. To examine and report on it, the practitioner should consider the sources of the data and how the information was derived. While the system that develops the data might not fit the prototype of internal control envisioned by the auditing literature, it nonetheless contains some of the same components. For example, information must be gathered, summarized, and reported. Often it is subject to internal accuracy checks and reviewed by responsible employees.

The system that produces the data consists of:

- *The Control Environment.* Management's attitudes, actions, and awareness about the importance of presenting reliable subject matter.
- *Risk Assessment.* The process of identifying potential risks relevant to misstatements in an organization's subject matter and developing actions to address those risks.
- *Control Activities.* The policies and procedures, whether automated or manual, management applies to provide discipline over the processing of information (which might include, for example, reviews, comparison, and segregation of duties).

- *Information and Communication.* The identification, capture, and exchange of information in a form and time frame that enable people to carry out their responsibilities. The information system includes the procedures, whether automated or manual, and records management uses to initiate record, process, summarize, and report the subject matter.
- *Monitoring.* A process that assesses the quality of the internal control's performance over time.

It is recommended that practitioners consider understanding the components of internal control in sufficient detail to:

- understand the areas of increased risk,
- understand the types of misstatements that could occur in the data, and
- design tests of the data to detect material misstatements.

The practitioner need not obtain or document the level of understanding required by the auditing literature. However, such documentation may be considered helpful in planning and reviewing the engagement.

Testing Controls. The attestation standards do not require the practitioner to test controls or even apply walk-through procedures to confirm the understanding of the controls. The practitioner, however, is not prohibited from testing the controls. If the subject matter is subject to effective controls, the practitioner may test those controls and use the results as a basis for reducing the level of detection procedures applied to the assertion.

Although testing of controls is not common in most attestation engagements, it might be considered if it is cost-effective. That is, if the controls are effective, and it is more efficient to test controls and reduce the detection tests than merely to apply more extensive detection tests, the practitioner should consider this approach. To be effective, the client's controls must be designed to prevent or detect misstatements and should be in effect for the period that affects the assertions.

To apply tests of controls, the practitioner applies inquiry, observation, inspection, or reperformance procedures to determine how, by whom, and how consistently a procedure was applied.

Considering Inherent Risk. Inherent risk is the susceptibility of the subject matter to a material misstatement. As in an audit, the practitioner's consideration of inherent risk in an examination is an intuitive process based on the practitioner's knowledge of the client and the subject matter. When considering inherent risk, the practitioner might consider the influence of factors such as the following:

- *Experience with the Client.* The level of knowledge of the client from past engagements or from communications with the predecessor or primary accountant/auditor.
- *Reputation of the Client.* The client's reputation in the business community.
- *Measurement Issues.* The complexity and contentiousness of accounting or measurement issues affecting the subject matter.
- *Testing Difficulties.* The frequency or significance of difficult-to-test transactions affecting the subject matter.
- *Prior Misstatements or Misrepresentations.* The nature, cause, and materiality of misstatements detected in prior engagements, or indications of misrepresentations by management in prior engagements.
- *Susceptibility to Fraud.* The susceptibility of the subject matter to fraud.
- *External Circumstances.* Factors such as industry conditions or technological developments.
- *Personnel.* The competence and experience of personnel assigned to process data that affects the subject matter.

- *Need for Judgment.* The extent of judgment involved in developing the subject matter.
- *Nature of Items.* The size and volume of individual items comprising the subject matter.
- *Complexity.* The complexity of calculations affecting the subject matter.

Detection Procedures. When designing procedures to test the subject matter, the practitioner should identify the test objectives. Using the guidance in the auditing standards, the following objectives can be derived:

- The information included in the subject matter actually exists or the underlying events occurred. (Is everything that is there supposed to be there?)
- The information includes everything it purports to. (Is everything that is supposed to be there really there?)
- The information is what it purports to be. (Is it really what it says it is?)
- The explicit amounts or value judgments about the information are appropriate. (Is it measured appropriately?)
- The presentation and disclosure is in conformity with the criteria. (Is it presented clearly, understandably, and fairly?)

When testing the subject matter, those are the five objectives (or questions) that should be addressed. The nature and extent of procedures applied for each objective depends on the practitioner's assessment of risk of misstatement. When the practitioner judges there to be little risk of misstatement for one or more of the objectives, either because the matters do not lend themselves to misstatement (inherent risk) or because tests of controls indicate that the client's procedures would prevent or detect misstatements (control risk), the level of testing for those objectives can be lower. In that case, the practitioner's procedures should focus on the other objectives.

Nature of Tests. In general, the available tests, in descending order of effectiveness, are:

- Independent confirmation.
- Inspection.
- Observation.
- Recalculation/reperformance.
- Analytical procedures.
- Inquiries.

The practitioner chooses among available types of detection procedures, selecting those that are more effective. When choosing among different tests of acceptable effectiveness, the practitioner generally chooses the tests that are most efficient in the circumstances.

In general, it is suggested that auditing literature can provide useful guidance to practitioners performing examinations. For example, when testing an outside party's obligation to the client, the practitioner would be well-advised to consider the guidance in SAS No. 67 (AU 330), *The Confirmation Process*, and when applying analytical procedures, the practitioner should consider SAS No. 56 (AU 329), *Analytical Procedures*, as amended.

SSAE No. 10 provides the following general presumptions about examination evidence:

- When evidence can be obtained from independent sources outside an entity, it provides greater assurance than that secured solely within an entity.

- The practitioner's direct personal knowledge, obtained through physical examination, observation, computation, operating tests, or inspection is more persuasive than information obtained indirectly.
- The more effective the system used to develop the information (that is, the internal control), the more assurance it provides about the information.

In addition, SAS No. 106 (AU 326), *Audit Evidence*, notes that evidence is more reliable when it exists in documentary form and that original documents are more reliable than copies.

Timing of Tests. Due to the nature of attestation engagements, the practitioner's procedures will generally be performed after the date of the subject matter or assertion. In designing the procedures, the practitioner should also consider the period it covered. The subject matter or assertion will be "as of . . ." or "for the year (two years, quarter, or month) ended. . . ." The period covered may significantly affect the procedures necessary to test the assertion.

Extent of Tests—Numeric Information

The extent of tests to be applied depends on the risk of material misstatement. This, in turn, depends on the measure of materiality. How the practitioner judges materiality varies based on whether the information is numeric. The approach described here, including the sampling approach, is more effective for testing overstatement than understatement. If the client's assertion is such that the practitioner's primary concern is understatement, the practitioner's materiality amount may need to be based on a reciprocal population. In that case, it is the reciprocal population that will be tested (that is, the approach described in this lesson should be applied to the reciprocal population).

A Basic Approach. The following approach can generally be used to determine the extent of tests of numeric information.

- Step 1** *Determine Tolerable Misstatement.* This is the amount of misstatement that the practitioner can accept in a population subject to sampling and still conclude that it is not materially misstated. It is suggested using 75% of planning materiality as tolerable misstatement.
- Step 2** *Identify the Amount of Individually Significant Items in the Population.* It is suggested that all items more than one-third of tolerable misstatement (that is, 25% of planning materiality) be designated as individually significant items. However, any amount up to tolerable misstatement may be used. These items will be tested individually.
- Step 3** *Identify Unusual Items.* Identify any other unusual items in the population that should be looked at individually either because they are unlike the rest of the population or because they present increased risk.
- Step 4** *Consider the Remaining Population.* Subtract the amounts identified in Steps 2 and 3 from the population. If the remainder is greater than tolerable misstatement, additional testing is generally necessary. This may involve application of analytical procedures, selecting more individually significant items, or sampling from the remaining population.

Sampling. SAS No. 39 (AU 350), *Audit Sampling*, provides useful guidance on the extent of tests. If the remaining population (that is, the residual amount from Step 4 in the preceding paragraph) is to be sampled, the following method is suggested to determine sample size:

- Step 1** *Divide the Remaining Population by the Tolerable Misstatement.* This establishes a basic sample size.
- Step 2** *Select a Risk Factor.* Multiply the result of Step 1 by the appropriate factor shown in Exhibit 2-1. This adjusts the sample size for (a) the risk of material misstatement (that is, the combined assessed level of inherent and control risk) and (b) the risk that other procedures, if any, that the practitioner plans to apply to the same amounts will fail to detect a material misstatement. Other procedures risk is inversely related to the effectiveness of the

other procedures (that is, the more effective the other procedure, the lower the risk assessment). If no other procedures will be performed, other procedures risk should be assessed as high.

- Step 3** *Consider Stratification.* If the population is not stratified [that is, it is not segregated into relatively homogeneous groups (such as size or other attributes)], increase the result in Step 2 by 20% to recognize increased risk. One useful approach to stratifying is to determine the average amount of an item in the population, select two-thirds of the sample from items that exceed the average, and select the remaining third of the sample from items below the average.

Exhibit 2-1

Risk Factors

Risk of Material Misstatement	Other Procedures Risk		
	High	Moderate	Low
High	3.0	2.3	1.9
Moderate	2.3	1.6	1.2
Low	1.9	1.2	0.9

* * *

Selecting the Sample. The sample items should be selected in such a manner that all items have an opportunity to be selected. The following are some of the more commonly used methods of selecting representative samples:

- *Random Selection.* A random selection provides each item in the population an equal chance to be selected. A random number table or generator (available in many commercial software packages) is required. Random selection is required only when statistical sampling is used.
- *Systematic Sampling.* Under this method, a sampling interval is determined by dividing the population by the number of items to be sampled. Every nth item is then selected.
- *Haphazard Selection.* In this sense, haphazard does not mean “careless”; it means “without conscious bias.” Under this method, sampling items are selected in no specific pattern without bias for or against any items in the population.

Projecting the Misstatement. The practitioner may use one of several methods to project the sample misstatement to the population. Two commonly used methods are as follows:

- *Ratio(or Rate of Misstatement) Method.* The ratio of sample quantity (the total of all items selected) to population quantity (the total of the population from which the sample was selected) is used to project the sample misstatement as follows:

$$\frac{\text{Amount of sample misstatement}}{\text{Sample quantity}} \times \text{Population quantity} = \text{Projected population misstatement}$$

- *Difference Method.* Using this method, the practitioner calculates the average amount of misstatement in the sample and multiplies that average by the number of items in the population, as follows:

$$\frac{\text{Sample misstatement}}{\text{Sample items}} \times \text{Population items} = \text{Projected population misstatement}$$

The ratio and difference methods produce the same result if the proportion of the number of sample items to population items is the same as the ratio of sample quantity to population quantity. Usually, the two methods do not produce the same results. The practitioner should select one of the methods based on whether there is reason to expect a relationship between the amount of the misstatement and the amount of the item.

<u>Factor</u>	<u>Method</u>
Misstatement relates to size of the item	Ratio (or rate of misstatement) method
Misstatement relatively constant for all items	Difference method

The practitioner should calculate the projected misstatement from the sample separately for each individual group (or stratum) used. The projected misstatement for such groups should then be added to determine the projected misstatement for the sample. Also, the testing of individually significant items is not considered sampling, and thus misstatements in individually significant items should not be projected.

The AICPA Sampling Guide discusses the ratio and difference methods (Paragraphs 4.76–4.78) as well as a third method—the MUS method (Paragraph 4.79). The MUS method uses tainting factors (that is, the ratio of each detected misstatement to the book value of that item) to project the sample misstatement. The sum of the tainting factors is multiplied by the sampling interval (that is, the total population amount in dollars divided by the sample size) to obtain an estimate of the total misstatement.

Considering Sampling Risk. Sampling risk is the risk that the practitioner may reach a different conclusion if the procedures are applied to a sample than if they are applied to all items in a population. For example, if tolerable misstatement is \$28,000, the practitioner might conclude that the sampling risk with a projected misstatement of \$5,000 would be acceptable. However, if the projected misstatement is close to, or exceeds, tolerable misstatement, the practitioner would conclude that there is an unacceptably high risk that the true misstatement in the population exceeds tolerable misstatement.

In a statistical sample, actual sampling risk can be measured based on sample results. In a nonstatistical sample, precise measurement is not possible. However, using the sampling model discussed here, the auditor may consider sampling risk in the following ways:

- If the projected misstatement is less than the expected misstatement, the practitioner can usually conclude that sampling risk is low and the results can be accepted.
- If the projected misstatement exceeds one-third of tolerable misstatement, the practitioner would normally assume there is an unacceptable risk that true misstatement exceeds tolerable misstatement. Unacceptable sampling risk is discussed below.
- If projected misstatement exceeds expected misstatement, but is less than one-third of tolerable misstatement, sampling risk is generally acceptable. However, the practitioner must use judgment in these situations. For example, in some cases, the practitioner may conclude that sampling risk is unacceptably high if the projected misstatement is only slightly less than one-third of tolerable misstatement.

Considering Qualitative Characteristics. The size or frequency of misstatements in a sampling application are not the only factors that should be considered. A practitioner should also consider the following qualitative factors:

- Nature and cause of any misstatements:
 - Were the wrong measurement criteria used or were the correct criteria misapplied?
 - Is the misstatement intentional or unintentional?
 - If the misstatement is unintentional, is it due to carelessness or misunderstanding of instructions?
- Relationship of misstatements to other phases of the engagement.

If a practitioner detects an intentional misstatement, it would normally require further effort and more careful consideration than an error caused by mistake or misunderstanding.

Unacceptable Sampling Risk. When the sample results indicate that sampling risk is unacceptable, the practitioner should first recognize that the sampling approach does not provide a sufficiently precise estimate to record the projected misstatement. In other words, the practitioner should not propose that the subject matter be adjusted

based on the projected misstatement. Instead, the practitioner should attempt to isolate the nature and cause of the misstatements found in the sample. The practitioner should then look for additional misstatements in the population that may have arisen from that same cause. Once those misstatements are identified, the subject matter can be corrected. However, if the nature and cause of the misstatements in the sample cannot be isolated (if there is no detectable pattern to them), the practitioner should consider performing additional tests or expanding the sample.

Extent of Tests—Nonnumeric Information

When the information is not numeric, the sampling approach cannot be based solely on a numeric measure of materiality. In that case, attribute sampling may be used. The authors suggest the following approach:

- Step 1** *Determine the Amount of Assurance Needed to be Provided by the Test.* The necessary level of assurance increases when the item being tested is very important. It decreases when other tests are expected to provide additional information about the information being tested. It also decreases if controls over the development of the information are tested and found to be effective, or if the subject matter involves a relatively lower level of inherent risk. The authors suggest describing the amount of assurance needed in qualitative terms: high, moderate, or low. If the sample is the only test applied to the assertion and controls have not been tested, a high level of assurance is generally needed.
- Step 2** *Estimate Deviations.* Estimate the number of deviations expected to be found in the population to be sampled.
- Step 3** *Determine the Sample Size.* The sample size can be determined based on the following table:

Expected Number of Deviations	<u>Degree of Assurance Needed</u>		
	High	Moderate	Low
0	60	45	35
1	95	80	65
2	125	110	90
3	155	135	110

The table is based on a tolerable deviation rate (materiality) of 5% and a confidence level as follows:

High Degree of Assurance Needed	95%
Moderate Degree of Assurance Needed	90%
Low Degree of Assurance Needed	85%

If, for example, a sample of 60 items is tested and no deviations are found, the practitioner can be 95% sure that the deviation rate does not exceed 5%.

Evaluation of Results

After applying the examination procedures, the practitioner needs to evaluate the results and their effect on the subject matter. If, based on the tests, the practitioner believes that the subject matter is materially misstated, the practitioner should have it corrected or modify the examination report.

Numeric Information. As in a financial statement audit, if the presentation of the subject matter includes multiple items, the practitioner must consider the effect of aggregate misstatement on individual items, totals, and subtotals within the presentation. In that case, the same considerations that apply to an audit of financial statements also generally apply to the examination engagement. More often, however, only one item is involved, and it is tested primarily by applying tests of details. In that case, the practitioner's evaluation consists of the following:

- Quantitative considerations.

- Qualitative considerations.
- Consideration of the risk of further misstatement.

Quantitative Considerations. The practitioner should first aggregate total likely misstatement. Likely misstatement is the practitioner's best estimate, as a result of applying examination procedures, of total misstatement, and it consists of the following:

- *Known Misstatement.* A misstatement that the practitioner specifically identifies by performing examination procedures. For example, misstatements detected in items tested 100% (individually significant items) are known misstatements.
- *Projected or Estimated Misstatement.* Projected or estimated misstatement is determined when a practitioner uses certain sampling or analytical procedures.

Total likely misstatement should then be compared to the amount considered material to the subject matter. When only a single item is presented, this amount (evaluation materiality) will generally be the same as planning materiality. If total likely misstatement exceeds the amount considered material to the assertion, the practitioner should have the subject matter corrected or modify the examination report. If total likely misstatement is less than the amount considered material to the assertion, the practitioner should consider qualitative aspects of the misstatements and consider the risk of further misstatement.

Qualitative Considerations. After comparing total likely misstatement to the amount considered material, a practitioner should recognize that otherwise immaterial misstatements may be qualitatively material. Some examples of the influence of qualitative considerations on materiality are as follows:

- When testing an assertion that the client is in conformity with a debt covenant, a small error (affecting, for example, working capital) might be material if it would create a default under a debt covenant.
- An intentional misstatement, that is, fraud, may lead the practitioner to question the advisability of being associated with the engagement.

Naturally, qualitative considerations are very dependent on the circumstances, so these examples are not intended to suggest that these matters are always material.

Risk of Further Misstatement. After comparing the combined effect of misstatements to amounts appropriate for evaluation, the practitioner should consider the risk of further misstatement. In this case, based on the guidance in SAS No. 107, the practitioner recognizes that there is a risk that the subject matter may be materially misstated due to further misstatement remaining undetected. If total likely misstatement is very close to the amount the practitioner considers material, the risk of further misstatement may be considered unacceptable. In an examination engagement, however, if the subject matter is subjected to extensive detail testing, further uncorrected misstatement may not be significant. The concept of risk of further misstatement recognizes that judgment cannot be reduced to a simple quantitative calculation.

Nonnumeric Information. Even when the subject matter is not numerical, the practitioner must assess whether it is fairly stated, in all material respects, based on the criteria. If multiple items are presented and numerous tests are applied, the results of those tests must be judgmentally considered in the aggregate. If, on the other hand, only a single item is presented and it is tested primarily by applying tests of details, the practitioner's assessment is based on whether the deviation rate is too high. The practitioner should also consider whether the description of the subject matter is otherwise incorrect or misleading. If either is the case, the subject matter needs to be corrected or the practitioner should modify the examination report. Qualitative consideration and the risk of further misstatement, as discussed in the preceding paragraphs for numeric information, are also generally applicable to nonnumeric information.

SELF-STUDY QUIZ

Determine the best answer for each question below. Then check your answers against the correct answers in the following section.

23. Which of the following statements best describes the practitioner's consideration of internal control in an attest engagement?
- a. The attestation standards incorporate specific requirements for obtaining an understanding of internal control in an attestation engagement.
 - b. The guidance in SAS No. 109, *Understanding the Entity and Its Environment and Identifying the Risks of Material Misstatement*, may be helpful to the practitioner examining an assertion.
 - c. Practitioners are required to obtain an understanding of the components of internal control in sufficient detail to understand the areas of increased risk, understand the types of misstatements that could occur in the data, and design tests of the data to detect material misstatements.
 - d. The practitioner should document the level of understanding in the same way it is required to be documented by the auditing literature.
24. **All but which** of the following statements about the practitioner's considerations when designing tests in an attestation engagement are correct?
- a. When choosing among different tests of acceptable effectiveness, the practitioner generally chooses the tests that are most efficient in the circumstances.
 - b. Auditing literature rarely provides useful guidance to practitioners performing attestation engagements.
 - c. Evidence obtained from independent sources outside an entity provides greater assurance than that secured solely within an entity.
 - d. Evidence obtained through the practitioner's direct personal knowledge, obtained through physical examination, observation, computation, operating tests, or inspection is more persuasive than information obtained indirectly.
25. When using sampling techniques, the practitioner may use one of several methods to project the sample misstatement to the population. Two commonly used methods are the ratio (or rate of misstatement) method and the difference method. Which of the following best describes the practitioners' considerations when determining which method to use to project the sample results?
- a. The difference method involves projecting the sample misstatement by dividing the sample misstatement by the sample population quantity (the total of the population from which the sample was selected) and multiplying it by total population quantify.
 - b. Generally, the ratio and difference methods produce the same results from one engagement to the next; therefore, the practitioner can choose either method.
 - c. The practitioner should select the difference method if he or she expects the misstatement will remain relatively constant for all items throughout the population.
 - d. Because the testing of individually significant items is considered sampling, misstatements in individually such items should be projected to the total population.

26. Sampling risk is the risk that the practitioner may reach a different conclusion if the procedures are applied to a sample than if they are applied to all items in a population. Which of the following statements best describes how a practitioner can consider sampling risk in a nonstatistical sample?
- a. If the projected misstatement is close to, or exceeds, tolerable misstatement, the practitioner would conclude that there is an acceptable sampling risk.
 - b. If projected misstatement exceeds expected misstatement, but is less than one-third of tolerable misstatement, sampling risk is generally acceptable.
 - c. If the projected misstatement is less than two-thirds of tolerable misstatement, the practitioner can normally assume that sampling risk is acceptable.
 - d. If the projected misstatement is less than the expected misstatement, the practitioner would usually conclude that sampling risk is unacceptable.
27. After applying the examination procedures, the practitioner needs to evaluate the results and their effect on the subject matter. If, based on the tests, the practitioner believes that the subject matter is materially misstated, the practitioner should have it corrected or modify the examination report. Which of the following statements about that evaluation is **not** correct?
- a. As in a financial statement audit, if the presentation of the subject matter includes multiple items, the practitioner must consider the effect of aggregate misstatement on individual items, totals, and subtotals within the presentation.
 - b. Likely misstatement is the practitioner's best estimate, as a result of applying examination procedures, of total misstatement.
 - c. Likely misstatement includes known misstatement and projected misstatement.
 - d. Projected misstatement is a misstatement that the practitioner specifically identifies by performing examination procedures.

SELF-STUDY ANSWERS

This section provides the correct answers to the self-study quiz. If you answered a question incorrectly, reread the appropriate material. **(References are in parentheses.)**

23. Which of the following statements best describes the practitioner's consideration of internal control in an attest engagement? **(Page 189)**
- a. The attestation standards incorporate specific requirements for obtaining an understanding of internal control in an attestation engagement. [This answer is incorrect. The attestation standards do not provide any specific requirements related to obtaining an understanding of internal control.]
 - b. The guidance in SAS No. 109, *Understanding the Entity and Its Environment and Identifying the Risks of Material Misstatement*, may be helpful to the practitioner examining an assertion. [This answer is correct. The subject matter of the engagement derives from client information. To examine and report on it, the practitioner should consider the sources of the data and how the information was derived. While the system that develops the data might not fit the prototype of internal control envisioned by the auditing literature, it nonetheless contains some of the same components. For example, information must be gathered, summarized, and reported. Often it is subject to internal accuracy checks and reviewed by responsible employees. Therefore, the guidance in SAS No. 109 may be helpful to the practitioner examining an assertion.]**
 - c. Practitioners are required to obtain an understanding of the components of internal control in sufficient detail to understand the areas of increased risk, understand the types of misstatements that could occur in the data, and design tests of the data to detect material misstatements. [This answer is incorrect. There is no requirement in the attestation standards for the practitioner to obtain an understanding of internal control in an attestation engagement, although this is recommended.]
 - d. The practitioner should document the level of understanding in the same way it is required to be documented by the auditing literature. [This answer is incorrect. Although there are documentation requirements in SAS No. 109 that apply in audit engagements, there are no corresponding requirements in the attestation standards. Nevertheless, it is recommended that practitioners document their understanding of internal control in much the same way.]
24. **All but which** of the following statements about the practitioner's considerations when designing tests in an attestation engagement are correct? **(Page 191)**
- a. When choosing among different tests of acceptable effectiveness, the practitioner generally chooses the tests that are most efficient in the circumstances. [This answer is incorrect. Once the practitioner determines how effective the tests should be, he or she would consider which of the tests would be more effective to perform.]
 - b. Auditing literature rarely provides useful guidance to practitioners performing attestation engagements. [This answer is correct. Often, the SASs can be helpful when performing examinations. For example, when testing an outside party's obligation to the client, the practitioner would be well-advised to consider the guidance in SAS No. 67, *The Confirmation Process*, and when applying analytical procedures, the practitioner should consider SAS No. 56, *Analytical Procedures*, as amended.]**
 - c. Evidence obtained from independent sources outside an entity provides greater assurance than that secured solely within an entity. [This answer is incorrect. Generally, evidence obtained from employees is less reliable than evidence obtained from outside third parties.]
 - d. Evidence obtained through the practitioner's direct personal knowledge, obtained through physical examination, observation, computation, operating tests, or inspection is more persuasive than information obtained indirectly. [This answer is incorrect. Information the practitioner obtains second hand is generally less reliable than evidence he or she receives directly.]

25. When using sampling techniques, the practitioner may use one of several methods to project the sample misstatement to the population. Two commonly used methods are the ratio (or rate of misstatement) method and the difference method. Which of the following best describes the practitioners' considerations when determining which method to use to project the sample results? **(Page 193)**
- a. The difference method involves projecting the sample misstatement by dividing the sample misstatement by the sample population quantity (the total of the population from which the sample was selected) and multiplying it by total population quantify. [This answer is incorrect. The procedure described is known as the ratio method, not the difference method.]
 - b. Generally, the ratio and difference methods produce the same results from one engagement to the next; therefore, the practitioner can choose either method. [This answer is incorrect. The ratio and difference methods only produce the same result if the proportion of the number of sample items to population items is the same as the ratio of sample quantity to population quantity. Therefore, in most cases, the ratio and difference methods do not produce the same results.]
 - c. **The practitioner should select the difference method if he or she expects the misstatement will remain relatively constant for all items throughout the population. [This answer is correct. When using the difference method, the practitioner calculates the average amount of misstatement in the sample and multiplies that average by the number of items in the population. Therefore, if the practitioner believes the misstatements will remain relatively constant throughout the population, that is the method he or she should use when projecting the misstatement to the entire population.]**
 - d. Because the testing of individually significant items is considered sampling, misstatements in individually such items should be projected to the total population. [This answer is incorrect. The testing of individually significant items is not considered sampling; therefore, the practitioner should not project misstatement found during these tests to the entire population.]
26. Sampling risk is the risk that the practitioner may reach a different conclusion if the procedures are applied to a sample than if they are applied to all items in a population. Which of the following statements best describes how a practitioner can consider sampling risk in a nonstatistical sample? **(Page 194)**
- a. If the projected misstatement is close to, or exceeds, tolerable misstatement, the practitioner would conclude that there is an acceptable sampling risk. [This answer is incorrect. In this case, the practitioner should recognize that the sampling approach does not provide a sufficiently precise estimate to record the projected misstatement.]
 - b. **If projected misstatement exceeds expected misstatement, but is less than one-third of tolerable misstatement, sampling risk is generally acceptable. [This answer is correct. However, the practitioner must use judgment in these situations. For example, in some cases, the practitioner may conclude that sampling risk is unacceptably high if the projected misstatement is only slightly less than one-third of tolerable misstatement.]**
 - c. If the projected misstatement is less than two-thirds of tolerable misstatement, the practitioner can normally assume that sampling risk is acceptable. [This answer is incorrect. If the projected misstatement is more than *one-third* of tolerable misstatement, the practitioner would normally assume there is an unacceptable risk that true misstatement exceeds tolerable misstatement.]
 - d. If the projected misstatement is less than the expected misstatement, the practitioner would usually conclude that sampling risk is unacceptable. [This answer is incorrect. If the projected misstatement is less than the expected misstatement, the practitioner can usually conclude that sampling risk is low and the results can be accepted.]

27. After applying the examination procedures, the practitioner needs to evaluate the results and their effect on the subject matter. If, based on the tests, the practitioner believes that the subject matter is materially misstated, the practitioner should have it corrected or modify the examination report. Which of the following statements about that evaluation is **not** correct? **(Page 196)**
- a. As in a financial statement audit, if the presentation of the subject matter includes multiple items, the practitioner must consider the effect of aggregate misstatement on individual items, totals, and subtotals within the presentation. [This answer is incorrect. This is true if the subject matter involves more than one item.]
 - b. Likely misstatement is the practitioner's best estimate, as a result of applying examination procedures, of total misstatement. [This answer is incorrect. This is the definition of likely misstatement. Once the practitioner has developed likely misstatement, he or she should then compare it to the amount considered material to the subject matter.]
 - c. Likely misstatement includes known misstatement and projected misstatement. [This answer is incorrect. Known misstatement and projected or estimated misstatement make up likely misstatement.]
 - d. **Projected misstatement is a misstatement that the practitioner specifically identifies by performing examination procedures. [This answer is correct. Known misstatement is a misstatement that the practitioner specifically identifies by performing examination procedures. For example, misstatements detected in items tested 100% (individually significant items) are known misstatements. Projected or estimated misstatement is determined when a practitioner uses certain sampling or analytical procedures.]**

Use of a Specialist

The practitioner may need specialized expertise in the engagement, and may decide to rely on the work of an expert. When the practitioner uses the work of a specialist, the attestation standards require that he or she have sufficient knowledge of the subject matter to:

- Communicate to the specialist the objectives of the work and
- evaluate the specialist's work to determine if the objectives were achieved.

A specialist's assistance may be particularly valuable in questions regarding:

- Valuations of unusual assets.
- Determination of physical characteristics.
- Determination of amounts through use of statistical or actuarial techniques.
- Interpretations of technical or legal requirements.

It is recommended that practitioners using the work of a specialist refer to SAS No. 73 (AU 336), *Using the Work of a Specialist*. That standard recommends that the practitioner inquire about the competence and professional reputation of the specialist. Preferably, the specialist should be unrelated to the client. If the specialist is related to the client, the practitioner should assess the risk that the specialist's objectivity might be impaired. If the practitioner believes the specialist's objectivity might be impaired, the practitioner should either:

- a. Engage another specialist that is unrelated to the client; or
- b. perform additional procedures to test the specialist's assumptions, methods, or findings (or engage another specialist to do so).

In using a specialist, the practitioner should:

- Obtain an understanding of the methods or assumptions to be used by the specialist to see that they are consistent with the practitioner's purposes.
- Make appropriate tests of data supplied to the specialist.
- Determine that the specialist's findings support the subject matter.
- Consider whether the findings are unreasonable on the surface.
- Make no reference to the specialist in the attestation report.

Representation Letters

While it is recommended obtaining representation letters, such letters are not required by AT 101. It requires only that a practitioner consider obtaining a representation letter from the responsible party. Examples of matters that might appear in such a representation letter include the following:

- A statement acknowledging responsibility for the subject matter and, when applicable, the assertion.
- A statement acknowledging responsibility for selecting the criteria, when applicable.
- A statement acknowledging responsibility for determining that such criteria are appropriate for their purposes, when the client is the responsible party.

- The assertion about the subject matter based on the criteria selected.
- A statement that they have disclosed to the practitioner all known matters contradicting the assertion and any communication from regulatory agencies affecting the subject matter or the assertion.
- Availability of all records relevant to the subject matter.
- A statement that they have disclosed 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).
- Other matters as the practitioner deems appropriate.

The representation letter should be dated as of the date of the practitioner's report. The letter should be addressed to the practitioner and signed by members of management whom the practitioner believes are responsible for and knowledgeable, directly or through others in the organization, about matters covered by the representation. Normally the CEO should sign it. It should also be signed by the highest ranking officer under whose responsibility the subject matter falls. For example, if the subject matter is financial, the CFO should also sign the letter.

When the client is not the responsible party, the practitioner should also consider obtaining a representation letter from the client. Examples of matters that might appear in such a letter include the following:

- A statement that the client has disclosed 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).
- A statement acknowledging the client's responsibility for selecting the criteria and for determining that such criteria are appropriate for their purposes.
- Other matters as the practitioner deems appropriate.

If the responsible party or the client refuses to furnish all written representations that the practitioner deems necessary, the practitioner should consider the effects of the refusal on his or her ability to issue an opinion. If the practitioner believes that the representation letter is necessary to obtain sufficient evidence to issue a report, the responsible party's or the client's refusal to furnish the written representations constitutes a scope limitation sufficient to preclude an unqualified opinion; ordinarily it causes the practitioner to disclaim an opinion or withdraw from the engagement. However, based on the nature of the representations not obtained or on the circumstances of the refusal, the practitioner may conclude that a qualified opinion is appropriate. The practitioner should also consider the refusal's effects on his or her ability to rely on other representations.

Subsequent Events

The practitioner has no responsibility to detect events occurring after the date of the subject matter (or assertion) that might affect it. However, he or she should ask the responsible party (and the client, if it is not the responsible party) about whether it is aware of any events that occurred between the date of the subject matter or assertion and the date of the practitioner's report that would have a material effect on the subject matter or assertion. If the practitioner obtains a representation letter, this representation would ordinarily be included in it.

Subsequent events that provide information about conditions that existed at the date of the subject matter or assertion should be considered in determining whether the subject matter conforms to the criteria. Those that provide information only about conditions that arose after the date of the subject matter or assertion should be disclosed, if necessary, to keep the subject matter or assertion from being misleading.

If the practitioner becomes aware of events after the date of his or her report that might have affected the report had he or she known about them, the practitioner may wish to consider the guidance in AU 561, *Subsequent Discovery of Facts Existing at the Date of the Auditor's Report*.

Other Information in a Document Containing the Practitioner's Report

If a client includes the practitioner's report (a) in an annual report to holders of securities or beneficial interests, annual reports of organizations for charitable or philanthropic purposes distributed to the public, and annual reports filed with regulatory authorities under the Securities Exchange Act of 1934 or (b) in other documents to which the practitioner, at the client's request, devotes attention,

- The practitioner should read the other information not covered by the practitioner's report or covered by the report of another practitioner and consider whether it, or the manner of its presentation, is materially inconsistent with the information appearing in the practitioner's report.
- If the practitioner believes that the other information is inconsistent with the information appearing in his or her report, he or she should consider whether the report requires revision. If the practitioner concludes that the report does not require revision, he or she should request the client to revise the other information. If the other information is not revised to eliminate the material inconsistency, the practitioner should consider other actions, such as revising his or her report to include an explanatory paragraph describing the material inconsistency, withholding the use of his or her report in the document, or withdrawing from the engagement.
- If the practitioner becomes aware of information in the document that he or she believes is a material misstatement of fact that is not a material inconsistency, he or she should discuss the matter with the client. If the practitioner concludes that a material misstatement exists, the practitioner should propose that the client consult with some other party whose advice may be useful, such as the entity's legal counsel. If, after discussing the matter, the practitioner concludes that a material misstatement of fact remains, the action taken will depend on his or her judgment in the circumstances. The practitioner should consider steps such as notifying the client's management and audit committee in writing of his or her views concerning the information and consulting his or her legal counsel about further action appropriate in the circumstances.

Workpaper Documentation

SSAE No. 10, as amended, requires workpapers in an examination engagement. According to the standard, the quantity, type, and content of workpapers may vary from engagement to engagement. Lesson 1 contains a detailed discussion of the documentation requirements of SSAE No. 10, as amended.

It is believed that the practitioner's examination workpapers will, at a minimum, ordinarily include the following:

- Documentation of the acceptance or continuance decision.
- An engagement letter.
- A planning form documenting the practitioner's knowledge of the client and consideration of attestation risk.
- Documentation of the procedures performed.
- Support for data in the presentation.
- A discussion of unusual matters encountered (including the justification for any departure from a presumptively mandatory requirement and a description of how the practitioner achieved its objectives).
- A representation letter.
- Copies of reports from other accountants, if any, who have examined a component of the subject matter.
- Documentation that the workpapers were reviewed.
- Documentation of unusual matters encountered and their resolution.

Examination Reports

The accountant may report his or her conclusions about the subject matter directly or may report on the responsible party's assertion about the subject matter. The illustrative reports in the attestation literature contain examples

of both. For instance, the reports on prospective and pro forma financial statements have always been on the subject matter. Reports on internal control have been on either. The two alternative forms of opinion are illustrated as follows:

Opinion directly on the subject matter

In our opinion, W Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 20XX, based on criteria established in Internal Control—Integrated Framework by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

Opinion on the responsible party's assertion

In our opinion, management's assertion that W Company maintained effective internal control over financial reporting as of December 31, 20XX, is fairly stated, in all material respects, based on criteria established in Internal Control—Integrated Framework by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

The standards provide no guidance on deciding whether to report on the subject matter or on the responsible party's assertion about the subject matter. It is believed that users generally prefer a report directly on the subject matter because it is clearer and more direct. But this is, obviously, a generalization.

When the report is modified for material misstatements or the responsible party refuses to provide a written assertion, the accountant's report should be directly on the subject matter, not the assertion.

AT 101.87 makes clear that the accountant may examine the assertion and opine on the subject matter. That is, the introductory paragraph may refer to the assertion, while the opinion paragraph refers to the subject matter directly. It is believed the SSAE did not intend to preclude, alternatively, examining the subject matter and reporting on the assertion. It is believed that alternative is not mentioned in the standard because users are less likely to want it.

The attestation standards require the following for examination reports:

- a. A title that includes the word "independent."
- b. An identification of the subject matter and the responsible party. (When reporting on the assertion, the report should identify the assertion rather than the subject matter. If the assertion does not accompany the report, the first paragraph of the report should also contain a statement of the assertion.)
- c. A statement that the subject matter (or, if reporting on the assertion, the assertion) is the responsibility of the responsible party.
- d. A statement that the accountant's responsibility is to express an opinion on the subject matter (or, if reporting on the assertion, the assertion) based on his or her examination.
- e. A statement that the examination was made in accordance with attestation standards established by the AICPA, and accordingly, included procedures that the accountant considered necessary in the circumstances.
- f. A statement that the accountant believes the examination provides a reasonable basis for his or her opinion.
- g. An opinion on whether the subject matter is based on, or in conformity with, the criteria in all material respects (or, if reporting on the assertion, whether the assertion is presented, or fairly stated, in all material respects based on the criteria).
- h. A statement restricting the use of the report to specified parties under the following circumstances:
 - When the criteria used to evaluate the subject matter are determined by the accountant 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.
 - When the criteria used to evaluate the subject matter are available only to the specified parties.

- When a written assertion is not provided by the responsible party. The introductory paragraph should include a statement to this effect as well.
- i. The manual or printed signature of the accountant's firm.
 - j. The date of the examination report.

Exhibits 2-2 and 2-3 are examples of examination reports on the subject matter and the assertion about the subject matter, respectively. Practitioners should follow that example when no other specific report form has been prescribed in other authoritative literature.

Exhibit 2-2

Illustrative Examination Report (Examination of Subject Matter)

INDEPENDENT ACCOUNTANT'S REPORT

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 American Institute of Certified Public Accountants and, accordingly, included examining, on a test basis, evidence supporting [Identify the subject matter—for example, XYZ Company's schedule of investment returns.] and performing such other procedures as we considered necessary in the circumstances. We believe that our examination provides a reasonable basis for our opinion.

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

In our opinion, the schedule referred to above presents, in all material respects, [Identify the subject matter—for example, the investment returns of XYZ Company for the year ended December 31, 20XX.] based on [Identify criteria—for example, the ABC criteria set forth in Note 1.].

[Signature]

[Date]

* * *

Exhibit 2-3

Illustrative Examination Report (Examination of Assertion about the Subject Matter)

INDEPENDENT ACCOUNTANT'S REPORT

We have examined management's assertion that [Identify the assertion—for example, the accompanying schedule of investment returns of XYZ Company for the year ended December 31, 20XX is presented in accordance with ABC criteria set forth in Note 1.]. XYZ Company's management is responsible for the assertion. Our responsibility is to express an opinion on the assertion based on our examination.

Our examination was conducted in accordance with attestation standards established by the American Institute of Certified Public Accountants and, accordingly, included examining, on a test basis, evidence

supporting management's assertion and performing such other procedures as we considered necessary in the circumstances. We believe that our examination provides a reasonable basis for our opinion.

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

In our opinion, management's assertion referred to above is fairly stated, in all material respects, based on [Identify established or stated criteria—for example, the ABC criteria set forth in Note 1.] .

[Signature]

[Date]

* * *

The report should be dated as of the completion of the examination procedures. The notion of completion of the examination procedures is not defined in the attestation standards. However, SAS No. 103, *Audit Documentation*, which defines the report date for audits of financial statements, might be helpful in determining the report date for examination reports. SAS No. 103 says the report date is no earlier than "the date on which the auditor has obtained sufficient appropriate audit evidence to support the opinion." Under the SAS, obtaining sufficient evidence includes completion of workpaper review, preparation of the financial statements, including disclosures, and management's acknowledgement of its responsibility for the financial statements.

The report may include additional commentary or information. This information might include, for example, inherent limitations of the data so that it is not misinterpreted; emphasis of certain aspects of the data, such as the interpretations made in applying the criteria; or uncertainties, such as pending legislation that might affect the assertions in the future. However, the additional information should not overshadow or contradict the message in the rest of the report. For example, it should not suggest that, despite an unqualified report, the practitioner is unsure of whether the presentation is fairly stated.

The following is an illustration of a paragraph that provides additional information.

Our examination is not intended to provide any assurance as to the monthly investment summaries distributed by XYZ Fund issued during 20X1 or the interim reports already issued in 20X2.

The example reports in the appendixes to AT 101 (in Exhibits 2-2 and 2-3 show the emphasis paragraph preceding the opinion paragraph. It is believed that it would be acceptable for any emphasis paragraph to follow the opinion paragraph. Some accountants prefer this approach so that information not affecting the opinion comes after the opinion paragraph.

Consistency. If the report covers multiple dates or periods during which criteria changed (for example, a report on comparative information), the practitioner should determine whether the criteria are clearly stated or described for each of the dates or periods, and whether the changes have been adequately disclosed. If the criteria used for the current report differ from those used in the past and the prior subject matter is not presented, the practitioner should consider whether the changes in criteria are likely to be significant to users of the report. If so, the practitioner should determine whether the criteria are clearly stated or described and the fact that the criteria have changed is disclosed.

Scope Limitations. If the scope of the examination is significantly restricted by the client or circumstances, the practitioner's report should indicate a scope limitation. The limitation should be described in the report. In addition, the practitioner's opinion should be qualified or disclaimed, depending on the size and pervasiveness of the data that could not be adequately tested.

A scope limitation also results if the client is the responsible party and refuses to provide a written assertion. In that case, AT 101.73 states that the scope limitation may require the practitioner to qualify the opinion, disclaim an opinion, or withdraw from the engagement. It may also result if the client is not the responsible party.

The following is an example of a report qualified for a scope limitation:

INDEPENDENT ACCOUNTANT'S REPORT

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.

Except as noted below, our examination was conducted in accordance with attestation standards established by the American Institute of Certified Public Accountants and, accordingly, included examining, on a test basis, evidence supporting [Identify the subject matter—for example, XYZ Company's schedule of investment returns.] and performing such other procedures as we considered necessary in the circumstances. We believe that our examination provides a reasonable basis for our opinion.

We were unable to [Identify scope limitation—for example, satisfy ourselves about the amount of income from the Asian funds, which accounted for 23% of the reported income.].

In our opinion, except for the effects of any adjustments that might have been necessary if we had been able to [Describe scope limitation—for example, examine evidence related to the Asian funds], the schedule referred to above presents, in all material respects, [identify the subject matter—for example, the investment returns of XYZ Company for the year ended December 31, 20XX.] based on [identify criteria—for example the ABC criteria set forth in Note 1.].

[Signature]

[Date]

A disclaimer of opinion due to the significance of the scope limitation reads as follows:

INDEPENDENT ACCOUNTANT'S REPORT

We were engaged to examine 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.

[Scope paragraph should be omitted.]

[Include paragraph to describe scope restrictions.]

Since management [Describe scope restrictions.], the scope of our work was not sufficient to enable us to express and, therefore, we do not express, an opinion on whether the schedule referred to above presents, in all material respects, [identify the subject matter—for example, the investment returns of XYZ Company for the year ended December 31, 20XX.] based on [Identify criteria—for example, the ABC criteria set forth in Note 1.].

[Signature]

[Date]

Misstatements. When conditions exist that, individually or in the aggregate, result in one or more material deviations from the criteria, SSAE No. 10 requires practitioners to report directly on the subject matter. Thus, when practitioners believe the assertion is misstated in any way (including problems with measurement, form, content, underlying assumptions, or disclosure), practitioners should report directly on the subject matter, not on the assertion.

The practitioner's report should describe the matter and the opinion should be modified. The opinion should be either qualified or adverse, depending on the materiality of the misstatement. The following is an example of a report qualified for a material misstatement:

INDEPENDENT ACCOUNTANT'S REPORT

We have examined 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 American Institute of Certified Public Accountants and, accordingly, included examining, on a test basis, evidence supporting [Identify the subject matter, for example, XYZ Company's schedule of investment returns.] and performing such other procedures as we considered necessary in the circumstances. We believe that our examination provides a reasonable basis for our opinion.

Our examination disclosed the following [Describe condition(s) that, individually or in the aggregate, resulted in a material misstatement or deviation from the criteria.]

In our opinion, except for the material misstatement [or deviation from the criteria] described in the third paragraph, the schedule referred to above, presents, in all material respects, [Identify the subject matter—for example, the investment returns of XYZ Company for the year ended December 31, 20XX.] based on [Identify criteria—for example, the ABC criteria set forth in Note 1.] .

[Signature]

[Date]

An adverse report might read as follows:

INDEPENDENT ACCOUNTANT'S REPORT

We have examined 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 American Institute of Certified Public Accountants and, accordingly, included examining, on a test basis, evidence supporting [Identify the subject matter, for example, XYZ Company's schedule of investment returns.] and performing such other procedures as we considered necessary in the circumstances. We believe that our examination provides a reasonable basis for our opinion.

Our examination disclosed the following [Describe condition(s) that, individually or in the aggregate, resulted in a material misstatement or deviation from the criteria.]

In our opinion, because of the effects of the matter [or deviation from the criteria] described in the third paragraph, the schedule referred to above does not present, in all material respects, [Identify the subject matter—for example, the investment returns of XYZ Company for the year ended December 31, 20XX.] based on [Identify criteria—for example, the ABC criteria set forth in Note 1.] .

[Signature]

[Date]

Report Restrictions. The report is required to carry a use restriction in three circumstances:

- When the criteria used to evaluate the subject matter are determined by the accountant 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.
- When the criteria used to evaluate the subject matter are available only to the specified parties.
- When a written assertion is not provided by the responsible party.

However, the accountant is not precluded from restricting the use of any report.

The attestation standards suggest that the practitioner consider informing the client that restricted-use reports are not intended for distribution to nonspecified parties, regardless of whether they are included in a document containing a separate general-use report. It goes on to note that the practitioner is not responsible for controlling a client's distribution of restricted-use reports. It also notes that a restricted-use report filed with a regulatory agency may be required by law or regulation to be made available to the public as a matter of public record. A restricted-use report should alert readers to the restriction on the use of the report by indicating that the report is not intended to be and should not be used by anyone other than the specified parties.

Including a restricted-use report in a document that includes a general-use report does not affect the intended use of either report. However, if two such reports are combined into a single report, it should be restricted to the specified parties.

A restricted-use report should present a separate paragraph at the end of the report containing the following:

- A statement indicating that the report is intended solely for the information and use of the specified parties.
- An identification of the specified parties to whom use is restricted.
- A statement that the report is not intended to be and should not be used by anyone other than the specified parties.

When the report is restricted because of a failure to obtain a written assertion, that reason should be stated in the *introductory* paragraph of the report. If the restriction is caused by something else, the reason is not described in the report.

The following is an example of a use-restriction paragraph:

This report is intended solely for the information and use of [the specified parties] and is not intended to be and should not be used by anyone other than these specified parties.

The following report illustrates a restriction because the criteria, while suitable, are available only to specified parties.

INDEPENDENT ACCOUNTANT'S REPORT

We have examined 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 American Institute of Certified Public Accountants and, accordingly, included examining, on a test basis, evidence supporting [Identify the subject matter, for example, XYZ Company's schedule of investment returns.] and performing such other procedures as we considered necessary in the circumstances. We believe that our examination provides a reasonable basis for our opinion.

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

In our opinion, the schedule referred to above, presents, in all material respects, [Identify the subject matter—for example, the investment returns of XYZ Company for the year ended December 31, 20XX.] based on the ABC criteria referred to in Note 1.

This report is intended solely for the information and use of XYZ Company and [identify other specified parties] and is not intended to be and should not be used by anyone other than these specified parties.

[Signature]

[Date]

The following is an example of a report restricted because the responsible party refused to provide a written assertion. The reason for the restriction is stated in the first paragraph.

INDEPENDENT ACCOUNTANT'S REPORT

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. XYZ management did not provide us a written assertion about their schedule of investment returns for the year ended December 31, 20XX. Our responsibility is to express an opinion based on our examination.

Our examination was conducted in accordance with attestation standards established by the American Institute of Certified Public Accountants and, accordingly, included examining, on a test basis, evidence supporting [Identify the subject matter—for example, XYZ Company's schedule of investment returns.] and performing such other procedures as we considered necessary in the circumstances. We believe that our examination provides a reasonable basis for our opinion.

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

In our opinion, the schedule referred to above presents, in all material respects, [Identify the subject matter—for example, the investment returns of XYZ Company for the year ended December 31, 20XX.] based on [Identify criteria—for example, the ABC criteria set forth in Note 1.].

This report is intended solely for the information and use of [identify specified party] and is not intended to be and should not be used by anyone other than the specified party.

[Signature]

[Date]

Including a Description of Tests of Controls or Other Procedures in an Examination Report. An interpretation at AT 9101.70 notes that a practitioner may include in an examination report a description of tests of controls or other procedures performed and their results. For example, users might want such details related to tests of controls over non-financial reporting matters similar to the description of tests of controls provided in a Type 2 service auditor report. It warns, however, that such a description could overshadow the practitioner's overall opinion or may cause report users to misunderstand the opinion. So, before including a description of tests, the practitioner might consider whether:

- Parties have requested this information and if they have an appropriate business need or reasonable basis for requesting it (for example, the specified parties need the information to assess their own controls that encompass or are dependent on the controls the practitioner is testing).
- The parties have an understanding of the nature and subject matter of the engagement and experience in using the information.
- The description is likely to cause report users to misunderstand the practitioner's opinion.
- The practitioner's tests of controls or other procedures performed directly relate to the subject matter of the engagement.

It notes that the addition of a description of tests of controls or other procedures performed and their results may increase the need to restrict the use of the report to specified parties.

SELF-STUDY QUIZ

Determine the best answer for each question below. Then check your answers against the correct answers in the following section.

28. Bill Broderick, CPA, has been engaged by Gibson Watch Factory to perform an examination engagement. In performing that engagement, Bill has determined that he will hire a specialist to assist him with the valuation of precious jewels and other parts used in the manufacture of the company's high-end watches. When working with a specialist in this engagement, Bill should do **all but which** of the following?
- a. Obtain an understanding of the methods or assumptions to be used by the specialist to see that they are consistent with the practitioner's purposes.
 - b. Determine that the specialist's findings support the subject matter.
 - c. Consider whether the findings are unreasonable on the surface.
 - d. Refer to the specialist in the attestation report.
29. While obtaining representation letters is recommended, such letters are not required by AT 101. If the practitioners decide to obtain one, which of the following matters would **not** ordinarily be found in a representation letter from the responsible party in an examination engagement?
- a. We are responsible for the [subject matter] and for our assertion that is presented in conformity with [criteria].
 - b. As of [date of subject matter], the [subject matter] is presented in conformity with [criteria].
 - c. The financial statements referred to above are fairly presented in conformity with U.S. generally accepted accounting principles.
 - d. We have disclosed to you all information of which we are aware that may contradict the [subject matter], and we have disclosed to you all communications from regulatory agencies affecting [subject matter].
30. Sometimes, the practitioner may be requested by the client to read a document that will contain the practitioner's report. In that case, which of the following statements best describes the practitioner's responsibilities?
- a. The practitioner should read the other information not covered by the practitioner's report and consider whether it, or the manner of its presentation, is materially inconsistent with the information appearing in the practitioner's report.
 - b. If the practitioner believes the other information is inconsistent with the information appearing in his or her report, he or she should revise the report to agree with the other information.
 - c. If the practitioner determines the other information results in a material inconsistency and recommends that it be revised, but the responsible party refuses to revise it, the practitioner should withdraw from the engagement.
 - d. The practitioner is responsible only for the information in his or her report; the practitioner has no responsibility for other information contained in a document containing that report.

31. The attestation standards provide guidance on how a practitioner should report on an examination engagement. Which of the following best describes this guidance?
- a. The practitioner must report his or her conclusions about the subject matter directly.
 - b. The standards provide guidance to assist the practitioner with the decision on whether to report on the subject matter or on the responsible party's assertion about the subject matter.
 - c. When the practitioner is modifying the report because of material misstatements, he or she must report directly on the subject matter.
 - d. If the practitioner examines the assertion, he or she must opine on the assertion rather than on the subject matter.
32. The examination of Whole Foods was complete. The practitioners concluded that the subject matter was materially misstated because of deviations from the criteria. The manager on the engagement asked Danny Davis, a senior auditor, to prepare a draft of the examination report. When the manager saw the draft, he expressed extreme displeasure with Danny's work. Which of the following statements did Danny include in the draft that caused the manager's displeasure?
- a. A statement that the assertion is the responsibility of the management of Whole Foods, Inc.
 - b. A statement that the accountant's responsibility is to express an opinion on the assertion based on his or her examination.
 - c. A statement that the accountant believes the examination provides a reasonable basis for his or her opinion.
 - d. An opinion that, except for the deviation from the criteria described in the report, management's assertion about the subject matter is fairly presented in accordance with the criteria.
33. Which of the following best describes the practitioner's responsibilities when he or she has determined that the examination report should be restricted as to use?
- a. The practitioner's restricted-use report should present a separate paragraph at the end of the report containing, among other things, a statement indicating that the report is intended solely for the information and use of the specified parties.
 - b. The practitioner must inform the client that restricted-use reports are not intended for distribution to nonspecified parties, regardless of whether they are included in a document containing a separate general-use report.
 - c. The practitioner is responsible for controlling a client's distribution of restricted-use reports.
 - d. The practitioner cannot include a restricted-use report in a document that includes a general-use report without affecting the intended use of the latter.

SELF-STUDY ANSWERS

This section provides the correct answers to the self-study quiz. If you answered a question incorrectly, reread the appropriate material. **(References are in parentheses.)**

28. Bill Broderick, CPA, has been engaged by Gibson Watch Factory to perform an examination engagement. In performing that engagement, Bill has determined that he will hire a specialist to assist him with the valuation of precious jewels and other parts used in the manufacture of the company's high-end watches. When working with a specialist in this engagement, Bill should do **all but which** of the following? **(Page 202)**
- a. Obtain an understanding of the methods or assumptions to be used by the specialist to see that they are consistent with the practitioner's purposes. [This answer is incorrect. The practitioner who decides to use a specialist in an examination engagement should look to the guidance in SAS No. 73, *Using the Work of a Specialist*. According to that SAS, this is one of the things the practitioner should do.]
 - b. Determine that the specialist's findings support the subject matter. [This answer is incorrect. The practitioner who decides to use a specialist in an examination engagement should look to the guidance in SAS No. 73, *Using the Work of a Specialist*. According to that SAS, this is one of the things the practitioner should do.]
 - c. Consider whether the findings are unreasonable on the surface. [This answer is incorrect. The practitioner who decides to use a specialist in an examination engagement should look to the guidance in SAS No. 73, *Using the Work of a Specialist*. According to that SAS, this is one of the things the practitioner should do.]
 - d. **Refer to the specialist in the attestation report. [This answer is correct. According to the guidance in SAS No. 73, the practitioner would not refer to the specialist in the attestation report.]**
29. While obtaining representation letters is recommended, such letters are not required by AT 101. If the practitioners decide to obtain one, which of the following matters would **not** ordinarily be found in a representation letter from the responsible party in an examination engagement? **(Page 202)**
- a. We are responsible for the [subject matter] and for our assertion that is presented in conformity with [criteria]. [This answer is incorrect. This is the statement of the responsible party's acknowledgment of responsibility for the subject matter and related assertion. Accordingly, such a statement would ordinarily be included in the representation letter.]
 - b. As of [date of subject matter], the [subject matter] is presented in conformity with [criteria]. [This answer is incorrect. This statement is the responsible party's assertion about the subject matter based on the criteria. Accordingly, such a statement would ordinarily be included in the representation letter.]
 - c. **The financial statements referred to above are fairly presented in conformity with U.S. generally accepted accounting principles. [This answer is correct. This statement refers to management's assertion about the conformity of the financial statements with GAAP, which is implied in an audit of financial statements. Accordingly, such a statement would not be included in a representation letter for an examination engagement under the attest standards.]**
 - d. We have disclosed to you all information of which we are aware that may contradict the [subject matter], and we have disclosed to you all communications from regulatory agencies affecting [subject matter]. [This answer is incorrect. This statement is the responsible party's disclosure that it has disclosed to the practitioner all known matters contradicting the assertion and any communication from regulatory agencies affecting the subject matter or the assertion. Accordingly, such a statement would ordinarily be included in the representation letter.]

30. Sometimes, the practitioner may be requested by the client to read a document that will contain the practitioner's report. In that case, which of the following statements best describes the practitioner's responsibilities? **(Page 204)**
- a. **The practitioner should read the other information not covered by the practitioner's report and consider whether it, or the manner of its presentation, is materially inconsistent with the information appearing in the practitioner's report. [This answer is correct. This might happen when a client includes the practitioner's report in an annual report of a charitable organization and then distributes it to the public.]**
 - b. If the practitioner believes the other information is inconsistent with the information appearing in his or her report, he or she should revise the report to agree with the other information. [This answer is incorrect. Although the practitioner should consider whether the report requires revision, it might be the other information and not the report that needs to be revised. If the practitioner concludes that the report does not require revision, that best practices indicate he or she should request the client to revise the other information.]
 - c. If the practitioner determines the other information results in a material inconsistency and recommends that it be revised, but the responsible party refuses to revise it, the practitioner should withdraw from the engagement. [This answer is incorrect. Although this is one option available to the practitioner, he or she had others. First, the practitioner could revise his or her report to include an explanatory paragraph describing the material inconsistency. Second, the practitioner could withhold the use of his or her report in the document. Finally, the practitioner could withdraw from the engagement.]
 - d. The practitioner is responsible only for the information in his or her report; the practitioner has no responsibility for other information contained in a document containing that report. [This answer is incorrect. At a minimum, best practices indicate that the practitioner should read the other information not covered by the practitioner's report and consider whether it, or the manner of its presentation, is materially inconsistent with the information appearing in the practitioner's report.]
31. The attestation standards provide guidance on how a practitioner should report on an examination engagement. Which of the following best describes this guidance? **(Page 205)**
- a. The practitioner must report his or her conclusions about the subject matter directly. [This answer is incorrect. The practitioner may either report his conclusions on the subject matter or on the responsible party's assertion about the subject matter. For instance, the reports on prospective and pro forma financial statements have always been on the subject matter. Reports on internal control traditionally have been on either.]
 - b. The standards provide guidance to assist the practitioner with the decision on whether to report on the subject matter or on the responsible party's assertion about the subject matter. [This answer is incorrect. The attest standards provide no guidance on this matter. However, best practices indicate that users generally prefer a report directly on the subject matter because it is clearer and more direct.]
 - c. **When the practitioner is modifying the report because of material misstatements, he or she must report directly on the subject matter. [This answer is correct. According to attestation reports, if there are material misstatements, the practitioner's report must be on the subject matter, not the assertion.]**
 - d. If the practitioner examines the assertion, he or she must opine on the assertion rather than on the subject matter. [This answer is incorrect. In this case, the practitioner may report either on the assertion or on the subject matter. This means that, while the introductory paragraph may refer to the assertion, the opinion paragraph may refer directly to the subject matter. Best practices indicate that the attest standards did not intend to preclude, alternatively, examining the subject matter and reporting on the assertion. Best practices also indicate that the alternative is not mentioned in the standard because users are less likely to want it.]

32. The examination of Whole Foods was complete. The practitioners concluded that the subject matter was materially misstated because of deviations from the criteria. The manager on the engagement asked Danny Davis, a senior auditor, to prepare a draft of the examination report. When the manager saw the draft, he expressed extreme displeasure with Danny's work. Which of the following statements did Danny include in the draft that caused the manager's displeasure? **(Page 208)**
- a. A statement that the assertion is the responsibility of the management of Whole Foods, Inc. [This answer is incorrect. This statement would be included in an examination report in which the practitioner is engaged to examine and report on the responsible party's assertion about the subject matter.]
 - b. A statement that the accountant's responsibility is to express an opinion on the assertion based on his or her examination. [This answer is incorrect. This statement would be included in an examination report in which the practitioner is engaged to examine and report on the responsible party's assertion about the subject matter.]
 - c. A statement that the accountant believes the examination provides a reasonable basis for his or her opinion. [This answer is incorrect. This statement would be included in an examination report.]
 - d. **An opinion that, except for the deviation from the criteria described in the report, management's assertion about the subject matter is fairly presented in accordance with the criteria. [This answer is correct. When conditions exist that, individually or in the aggregate, result in one or more material deviations from the criteria, practitioners are required to report on subject matter (rather than on the assertion). Thus, when practitioners believe the subject matter is misstated in any way (including problems with measurement, form, content, underlying assumptions, or disclosure), they should issue a report directly on the subject matter and not on the assertion.]**
33. Which of the following best describes the practitioner's responsibilities when he or she has determined that the examination report should be restricted as to use? **(Page 210)**
- a. **The practitioner's restricted-use report should present a separate paragraph at the end of the report containing, among other things, a statement indicating that the report is intended solely for the information and use of the specified parties. [This answer is correct. In addition, the paragraph should include an identification of the specified parties to whom use is restricted and a statement that the report is not intended to be and should not be used by anyone other than the specified parties.]**
 - b. The practitioner must inform the client that restricted-use reports are not intended for distribution to nonspecified parties, regardless of whether they are included in a document containing a separate general-use report. [This answer is incorrect. The attestation standards suggest that the practitioner make this communication to the client, although it does not require it.]
 - c. The practitioner is responsible for controlling a client's distribution of restricted-use reports. [This answer is incorrect. The practitioner can only suggest to clients that they should not distribute restricted-use reports to others; they cannot control what the client does with the reports. For that reason, the standards require the language on restricted use to inform potential users of the risks of relying on such a report.]
 - d. The practitioner cannot include a restricted-use report in a document that includes a general-use report without affecting the intended use of the latter. [This answer is incorrect. Including a restricted-use report with a general use report does not affect the intended use of either report. However, if two such reports are combined into a single report, it should be restricted to the specified parties.]

EXAMINATION FOR CPE CREDIT**Lesson 2 (NTETG102)**

Determine the best answer for each question below. Then mark your answer choice on the Examination for CPE Credit Answer Sheet located in the back of this workbook or by logging onto the Online Grading System.

19. Which of the following best describes the practitioner's responsibility for performing tests of controls in an attestation engagement?
- a. Like the auditing standards, the attestation standards require the practitioner to test controls and apply walk-through procedures to confirm the understanding of the controls.
 - b. Even if the practitioner believes the subject matter is subject to effective controls and decides to test them, the practitioner cannot use the results as a basis for reducing the level of detection procedures applied to the assertion.
 - c. If the controls are effective, and it is more efficient to test controls and reduce the detection tests than merely to apply more extensive detection tests, the practitioner should consider testing the controls.
 - d. The practitioner is prohibited from testing the controls.
20. Steve has been engaged to perform an attest engagement for ColorSwirl, Inc. What is the most effective test that Steve can perform when examining the subject matter?
- a. Independent confirmation from a third party.
 - b. Analytical procedures performed on significant account balances.
 - c. Observation of year-end inventory procedures.
 - d. Inspection of assets.
21. Which of the following commonly used methods of selecting representative samples involves first determining a sampling interval (by dividing the population by the number of items to be sampled) and then selecting every nth item?
- a. Random selection.
 - b. Systematic sampling.
 - c. Haphazard selection.
 - d. Do not select this answer choice.
22. Sampling risk is the risk that the practitioner may reach a different conclusion if the procedures are applied to a sample than if they are applied to all items in a population. Which of the following best describes the practitioner's response when sampling risk is unacceptable?
- a. The practitioner should recognize that the sampling approach provides a sufficiently precise estimate to record the projected misstatement.
 - b. The practitioner should propose that the subject matter be adjusted based on the projected misstatement.
 - c. The practitioner should try and isolate the cause and nature of the misstatements in the sample and identify any additional misstatements in the population that may have occurred from the same cause.
 - d. The practitioner should downsize the sample when the nature and cause of the misstatements in the sample cannot be isolated.

23. A practitioner must do which of the following when performing an engagement on nonnumeric subject matter?
- a. Obtain sufficient evidence to provide a reasonable basis for the conclusion that is expressed in the information.
 - b. Must state in the report that the information is intended solely for the information and use of the specified parties under the following circumstances.
 - c. Determine if the subject matter is fairly stated, in all material respects, based on the criteria.
 - d. Do not select this answer choice.
24. Which of the following statements best describes the practitioner's responsibility to obtain a representation letter in an examination engagement?
- a. AT 101 requires the practitioner to obtain a representation letter from the responsible party.
 - b. AT 101 does not require the practitioner to obtain a representation letter and obtaining one is not recommended.
 - c. When the client is not the responsible party, it is not necessary for the practitioner to consider obtaining a representation letter from the client.
 - d. AT 101 requires the practitioner to consider obtaining a representation letter from the responsible party.
25. Which of the following best describes the practitioner's responsibility for subsequent events in an examination engagement?
- a. AT 101 states that the practitioner has the responsibility to detect events occurring after the date of the subject matter (or assertion) that might affect it.
 - b. The practitioner is required to ask the responsible party (and the client, if it is not the responsible party) about whether it is aware of any events that occurred between the date of the subject matter or assertion and the date of the practitioner's report that contradict the subject matter or assertion.
 - c. If the practitioner decides to obtain a representation letter from the client, it is not necessary for the practitioner to include a representation about subsequent events in the representation letter.
 - d. It is not necessary for practitioners to consider the effect of subsequent events that provide information about conditions that existed at the date of the subject matter or assertion on his or her determination of whether the subject matter conforms to the criteria.
26. Lila Brown, partner in charge of Regency Construction, asks Brenda Myers, CPA, to draft an examination report on management's assertions about the number of construction jobs completed in 20X2. Which of the following statements would Brenda **not** include in that report?
- a. A title that includes the word "independent."
 - b. An identification of the responsible party.
 - c. A statement that the procedures performed are sufficient for the specified users' purpose.
 - d. A statement that the subject matter is the responsibility of the responsible party.

27. SAS No. 103, *Audit Documentation*, defines the report date for audits of financial statements and is useful in determining the report date for examination reports; however, the attestation standards do not define completion of examination procedures. Accordingly, the SAS report date is the date on which the auditor has obtained sufficient appropriate audit evidence to support the opinion. Thus, the practitioner's examination report should be dated as of the completion of the examination procedures. Which of the following does **not** constitute completion of sufficient audit evidence according to SAS No. 103?
- Preparation of the financial statements.
 - Completion of workpaper review.
 - Communication of control related matters to management.
 - Management's acknowledgement of its responsibility for the financial statements.
28. Which of the following best describes the effect of a scope limitation on the practitioner's examination report?
- The practitioner's report should state that there is a scope limitation, but should provide no further description of the limitation.
 - The practitioner's opinion should be qualified or disclaimed, depending on the size and pervasiveness of the data that could not be adequately tested.
 - There is no scope limitation if the client is the responsible party and refuses to provide a written assertion.
 - A practitioner cannot disclaim an opinion because of a scope limitation.
29. CPA Melanie has issued the following report after finishing her attestation engagements. Identify what type of report Melanie issued.

INDEPENDENT ACCOUNTANT'S REPORT

We have examined 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 American Institute of Certified Public Accountants and, accordingly, included examining, on a test basis, evidence supporting [Identify the subject matter, for example, XYZ Company's schedule of investment returns.] and performing such other procedures as we considered necessary in the circumstances. We believe that our examination provides a reasonable basis for our opinion.

Our examination disclosed the following [Describe condition(s) that, individually or in the aggregate, resulted in a material misstatement or deviation from the criteria.]

In our opinion, because of the effects of the matter [or deviation from the criteria] described in the third paragraph, the schedule referred to above does not present, in all material respects, [Identify the subject matter—for example, the investment returns of XYZ Company for the year ended December 31, 20XX.] based on [Identify criteria—for example, the ABC criteria set forth in Note 1.] .

[Signature]

[Date]

- Report qualified for a material misstatement.
- Adverse report.

- c. Disclaimer of opinion due to the significance of the scope limitation.
 - d. Report qualified for a scope limitation.
30. In certain situations, the attestation standards require the practitioner to restrict the use of the practitioner's attestation report. Which of the following best describes a restricted-use report?
- a. Including a restricted-use report in a document that includes a general-use report affects the intended use of either report.
 - b. If a restricted-use report and a general-use report are included in the same report, it should be restricted to the specified parties.
 - c. All restricted-use reports should describe the reason for the restriction.
 - d. A restricted-use report should not identify the specified parties by name.

Lesson 3: Review Engagements under the Attestation Standards

INTRODUCTION

A review engagement provides a moderate level of assurance on the subject matter. That is, it provides a basis for the practitioner to report that he or she is not aware of any material modifications that need to be made for either (a) the assertion about the subject matter to be fairly stated, in all material respects, based on the criteria or (b) the subject matter to be in conformity with the criteria, in all material respects. In this regard, a review is similar to a review performed under SSARS No. 19 (AR 90), *Compilation and Review of Financial Statements*.

However, SSARS No. 1 does not apply to a review performed under the attestation standards. Instead, the statements on standards for attestation engagements (the attestation standards) do. Therefore, this lesson describes the factors to assess when determining whether to perform a review engagement under the attestation standards. If so, it describes the review procedures to be performed. It also discusses other matters that might affect a review engagement, including the practitioner's responsibilities when other information is included in a document that contains the practitioner's report. Finally, this lesson describes which specific workpapers are ordinarily included in a review engagement, as well as the required elements of a practitioner's review report.

Learning Objectives:

Completion of this lesson will enable you to:

- Assess factors to determine whether to perform a review engagement; identify the procedures to perform in a review engagement; and describe the effect of subsequent events.
- Describe each element in the practitioner's review report.
- Identify required workpapers and determine procedures to perform when wrapping up the engagement, including when part of the work is performed by other practitioners.

REVIEW ENGAGEMENTS

A review engagement provides a moderate level of assurance on the subject matter. That is, it provides a basis for the practitioner to report that he or she is not aware of any material modifications that need to be made for either (a) the assertion about the subject matter to be fairly stated, in all material respects, based on the criteria or (b) the subject matter to be in conformity with the criteria, in all material respects. In this regard, a review is similar to a review performed under SSARS No. 19 (AR 90), *Compilation and Review of Financial Statements*.

Should You Do a Review?

Although AT 101 allows reviews in all situations that examinations can be done, performing reviews is discouraged in most cases. In each attestation section other than AT 101, the Auditing Standards Board has prohibited reviews. [The only exceptions to this are in AT 401, *Pro Forma Financial Information*, and AT 701, *Management's Discussion and Analysis*. But in the former, the review service is permitted only when the underlying historical financial statements are reviewed, and the review and examination procedures applied to the pro forma adjustments are basically the same. In the latter, the review report is restricted to specified users.] Best practices indicate the Board chose to prohibit reviews in most attestation engagements for one or more of the following reasons:

- Inability to define a level of procedures that provides a moderate level of assurance and differs significantly from the procedures that would be performed in an examination.
- Fear that the review report would be misunderstood by users.
- Lack of a market demand for such services.

Accordingly, with the exception of reviewing elements of a financial statement, best practices indicate that a review service should generally be avoided under the attestation standards. But, if it is to be provided, the practitioner

should make sure that the users are able to understand the practitioner's report and the level of responsibility the practitioner assumes.

It is inappropriate to perform a review when the subject matter or criteria are too subjective to perform an examination. Reducing the level of service does not solve the problem presented by the third general standard. The rules are the same for a review and an examination.

Review Procedures

As in an examination engagement, the practitioner should consider attestation risk and materiality in a review engagement. Materiality is the same for reviews and examinations since materiality is based on the subject matter, not on the level of service. The practitioner considers attestation risk in the same manner as for examinations, although he or she can accept more risk in a review. That is attestation risk in an examination must be reduced to a low level, whereas in a review, it must be reduced to a moderate level.

Internal Control. It is recommended that the practitioner in a review engagement have a general understanding of the system that develops the data. Thus, the discussion about internal control at the beginning of lesson 2 is generally applicable to reviews. However, since the practitioner's procedures are more limited in a review, the minimum understanding needed to design the procedures would be correspondingly lower.

It is unusual to test the controls in a review. Because the detection procedures are generally limited to inquiry and analytical procedures, testing controls does not provide a meaningful reduction of those procedures. Accordingly, there is generally little benefit in testing controls. However, the attestation standards do allow tests of controls in review engagements. The practitioner might consider applying them if they make the engagement more efficient by allowing the practitioner to apply the inquiry and analytical procedures to more aggregated data (for example, looking at data for whole divisions rather than on a departmental basis).

Level of Procedures. Generally, procedures in a review engagement consist of inquiries and analytical procedures. It is generally unnecessary in a review to obtain independent confirmations or apply inspection or observation procedures. However, those procedures are not prohibited, and might be efficient in certain circumstances.

Analytical procedures should be applied to identify and provide a basis for inquiry about the relationships and individual items that appear to be unusual and may indicate a material misstatement. Analytical procedures should include the following:

- Developing expectations by identifying and using plausible relationships that are reasonably expected to exist based on the practitioner's understanding of the entity and the industry in which the entity operates.
- Comparing recorded amounts, or ratios developed from recorded amounts, to expectations developed by the practitioner.

Inquiries of members of management with responsibility for the subject matter generally consist of the following:

- Whether the subject matter has been prepared in conformity with the criteria.
- The client's application and interpretation of the criteria.
- Unusual or complex situations that may have an effect on the subject matter.
- Significant transactions/activity occurring or recognized near the end of the reporting period.
- The status of any uncorrected adjustments to the data identified during the previous period.
- Matters as to which questions arose in the course of applying these procedures.
- Events subsequent to the date of the subject matter that would have a material effect on the presentation.

- Their knowledge of fraud or suspected fraud affecting the entity involving management or others where the fraud could have a material effect on the subject matter (e.g., communications received from employees, former employees, or others.)
- Significant journal entries and other adjustments to the data.
- Communications from regulatory agencies.

Also, inquiries should be made concerning actions taken by management or the board of directors that might affect the subject matter.

Other procedures generally consist of the following:

- Reading the subject matter to consider whether it appears to conform to the criteria.
- Obtaining reports of other practitioners, if any, who have been engaged to examine or review the subject matter for significant portions of the entity, its subsidiaries, or other investees.

If the practitioner believes that the inquiry and analytical procedures do not provide the level of assurance needed to give a review report, he or she should apply more effective procedures, such as those involving search and verification. If the inquiries and analytical procedures indicate the possibility of material misstatements, the practitioner might have to resort to the more effective types of tests to resolve the uncertainty or propose adjustment of the subject matter.

The practitioner's procedures should be appropriate for the period covered by the subject matter. Subject matter will be "as of. . ." or "for the year (two years, quarter, or month) ended. . . ." The period covered may significantly affect the procedures necessary to test the subject matter.

Representation Letters. Representation letters are not required by AT 101, but obtaining them anyway is recommended. AT 101 requires only that a practitioner consider obtaining a representation letter from the responsible party. Examples of matters that might appear in such a representation letter include the following:

- A statement acknowledging responsibility for the subject matter and, when applicable, the assertion.
- A statement acknowledging responsibility for selecting the criteria, when applicable.
- A statement acknowledging responsibility for determining that such criteria are appropriate for their purposes, when the client is the responsible party.
- The assertion about the subject matter based on the criteria selected.
- A statement that they have disclosed to the practitioner all known matters contradicting the assertion and any communication from regulatory agencies affecting the subject matter or the assertion.
- Availability of all records relevant to the subject matter.
- A statement that they have disclosed 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).
- Other matters as the practitioner deems appropriate.

The representation letter should be dated as of the date of the practitioner's report. The letter should be addressed to the practitioner and signed by members of management whom the practitioner believes are responsible for and knowledgeable, directly or through others in the organization, about matters covered by the representation. Normally the CEO should sign it. It should also be signed by the highest ranking officer under whose responsibility the subject matter falls. For example, if the subject matter is financial, the CFO should also sign the letter.

When the client is not the responsible party, the practitioner should also consider obtaining a representation letter from the client. Examples of matters that might appear in such a letter include the following:

- A statement that the client has disclosed 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).
- A statement acknowledging the client's responsibility for selecting the criteria and for determining that such criteria are appropriate for their purposes.
- Other matters as the practitioner deems appropriate.

If the responsible party or the client refuses to furnish all written representations that the practitioner deems necessary, the practitioner should consider the effects of such a refusal on his or her ability to issue a conclusion about the subject matter. If the practitioner believes that the representation letter is necessary to obtain sufficient evidence to issue a report, the responsible party's or the client's refusal to furnish such evidence in the form of written representations constitutes a scope limitation. In that case, the practitioner should withdraw from the review engagement.

The practitioner may need specialized expertise in the engagement, and may decide to rely on the work of an expert. When the practitioner uses the work of a specialist, the attestation standards require that he or she have sufficient knowledge of the subject matter to:

- Communicate to the specialist the objectives of the work and
- Evaluate the specialist's work to determine if the objectives were achieved.

Subsequent Events

The practitioner has no responsibility to detect events occurring after the date of the subject matter (or assertion) that might affect it. However, he or she should ask the responsible party (and the client, if it is not the responsible party) about whether it is aware of any events that occurred between the date of the subject matter or assertion and the date of the practitioner's report that would have a material effect on the subject matter or assertion. If the practitioner obtains a representation letter, this representation would ordinarily be included in it.

If the practitioner identifies subsequent events,

- Those that provide information about conditions that existed at the date of the subject matter or assertion, should be considered in determining whether the subject matter conforms to the criteria.
- Those that provide information only about conditions that arose after the date of the subject matter or assertion should be disclosed if necessary to keep the subject matter or assertion from being misleading.

If the practitioner becomes aware of events after the date of his or her report that might have affected the report had he or she known about them, the practitioner may wish to consider the guidance in AU 561, *Subsequent Discovery of Facts Existing at the Date of the Auditor's Report*.

Other Information in a Document Containing the Practitioner's Report

If a client includes in the practitioner's report (a) an annual report to holders of securities or beneficial interests, annual reports of organizations for charitable or philanthropic purposes distributed to the public, and annual reports filed with regulatory authorities under the Securities Exchange Act of 1934 or (b) other documents to which the practitioner, at the client's request, devotes attention:

- The practitioner should read the other information not covered by the practitioner's report or by the report of another practitioner and consider whether it, or the manner of its presentation, is materially inconsistent with the information appearing in the practitioner's report.

- If the practitioner believes that the other information is inconsistent with the information appearing in his or her report, he or she should consider whether the report requires revision. If the practitioner concludes that the report does not require revision, he or she should request the client to revise the other information. If the other information is not revised to eliminate the material inconsistency, the practitioner should consider other actions, such as revising his or her report to include an explanatory paragraph describing the material inconsistency, withholding the use of his or her report in the document, or withdrawing from the engagement.
- If the practitioner becomes aware of information in the document that he or she believes is a material misstatement of fact that is not a material inconsistency, he or she should discuss the matter with the client. If the practitioner concludes that a material misstatement exists, the practitioner should propose that the client consult with some other party whose advice may be useful, such as the entity's legal counsel. If, after discussing the matter, the practitioner concludes that a material misstatement of fact remains, the action taken will depend on his or her judgment in the circumstances. The practitioner should consider steps such as notifying the client's management and audit committee in writing of his or her views concerning the information and consulting his or her legal counsel about further action appropriate in the circumstances.

Workpaper Documentation

AT 101 requires workpapers in review engagements. The quantity, type, and content of workpapers may vary from engagement to engagement.

Best practices indicate that the practitioner's review workpapers will, at a minimum, ordinarily include the following:

- Engagement letter.
- Planning form documenting the practitioner's knowledge of the client and consideration of attestation risk.
- Documentation of the inquiries and analytical procedures performed.
- Support for data in the presentation.
- Discussion of unusual matters encountered (including the justification for any departure from a presumptively mandatory requirement and a description of how the practitioner achieved its objectives).
- Representation letter.
- Copies of reports from other accountants, if any, who have examined or reviewed a component of the assertion.
- Documentation that the workpapers were reviewed.
- Reasons for a step-down in level of service from an examination, if any.

Review Reports

The practitioner can report on the subject matter or on the assertion about the subject matter. This distinction is discussed in lesson 2.

The practitioner's report on a review should include the following:

- a. A title that includes the word "independent."
- b. An identification of the subject matter and the responsible party. (When reporting on the assertion, the report should identify the assertion and the responsible party. When the assertion does not accompany the report, the first paragraph of the report should also contain a statement of the assertion.)

- c. A statement that the subject matter (or, if reporting on the assertion, the assertion) is the responsibility of the responsible party.
- d. A statement that the review was made in accordance with attestation standards established by the AICPA.
- e. A statement that the review is substantially less in scope than an examination, the objective of which is the expression of opinion on the subject matter (or, if reporting on the assertion, the assertion), and accordingly, no such opinion is expressed.
- f. A statement about whether the accountant is aware of any material modifications that should be made to the subject matter for it to be based on, or in conformity with, in all material respects, the criteria, other than those modifications, if any, indicated in his or her report. [If reporting on an assertion, a statement about whether the practitioner is aware of any material modifications that should be made to the assertion for it to be presented (or fairly stated) in all material respects based on (or in conformity with) the criteria, other than those modifications, if any, indicated in his or her report.]
- g. A statement restricting the use of the report to specified parties under the following circumstances:
 - The work was adequately planned and supervised. Sufficient evidence was obtained to provide a reasonable basis for the conclusion expressed in the practitioner's report. When the criteria used to evaluate the subject matter are determined by the accountant 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.
 - When the criteria used to evaluate the subject matter are available only to the specified parties.
 - When a written assertion is not provided by the responsible party and the responsible party is not the client. The introductory paragraph should include a statement to this effect as well.
- h. The manual or printed signature of the accountant's firm.
- i. The date of the review report.

Illustrative Review Report on Subject Matter. The following is an example of a review report that expresses a conclusion on the subject matter, rather than on the assertion about the subject matter:

INDEPENDENT ACCOUNTANT'S REPORT

We have reviewed 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 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 [Identify the subject matter—for example, XYZ Company's schedule of investment returns.]. Accordingly, we do not express such an opinion.

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

Based on our review, nothing came to our attention that caused us to believe that the [Identify the subject matter—for example, schedule of investment returns of XYZ Company for the year ended December 31, 20XX.] was not prepared, in all material respects, in conformity with [Identify the criteria—for example, the ABC criteria set forth in Note 1.].

[Signature]

[Date]

The following is an example review report on an assertion:

INDEPENDENT ACCOUNTANT'S REPORT

We have reviewed management's assertion that [Identify the assertion—for example, the accompanying schedule of investment returns of XYZ Company for the year ended December 31, 20XX is presented in accordance with the ABC criteria set forth in Note 1.]. XYZ Company's management is responsible for the assertion.

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 assertion. Accordingly, we do not express such an opinion.

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

Based on our review, nothing came to our attention that caused us to believe that management's assertion referred to above is not fairly stated, in all material respects, based on [Identify the criteria—for example, the ABC criteria set forth in Note 1.].

[Signature]

[Date]

The report should be dated as of the completion of the review procedures.

The report may include additional commentary or information. Although this is not explicit in AT 101, it is implied in the report examples in Appendix B to the standard. This additional information might include, for example, inherent limitations of the data so that it is not misinterpreted; emphasis of certain aspects of the data, such as the interpretations made in applying the criteria; or uncertainties, such as pending legislation that might affect the assertions in the future. However, the additional information should not overshadow or contradict the message in the rest of the report. For example, it should not suggest that, despite an unqualified report, the practitioner doubts whether the presentation is fairly stated.

Such informational text should precede the opinion paragraph. The following is an illustration of a paragraph that provides additional information.

Our review is not intended to provide any assurance as to the monthly investment summaries distributed by XYZ Fund issued during 20X1 or the interim reports already issued in 20X2.

Consistency. If the report covers multiple dates or periods during which criteria changed (for example, a report on comparative information), the practitioner should determine whether the criteria are clearly stated or described for each of the dates or periods, and whether the changes have been adequately disclosed. If the criteria used for the current report differ from those used in the past and the prior subject matter is not presented, the practitioner should consider whether the changes in criteria are likely to be significant to users of the report. If so, the practitioner should determine whether the criteria are clearly stated or described and the fact that the criteria have changed is disclosed.

Modified Review Report. When the report is modified because of a material misstatement (that is, a deviation from the criteria), the report should express a conclusion on the subject matter, rather than on the assertion about the subject matter. Accordingly, in that circumstance, the accountant does not have a choice of reporting forms, but must use the direct report. AT 101 indicates that this is a more effective form of communication for modified reports.

Restrictions on the scope of a review engagement, including failure to obtain a written assertion when the responsible party is the client, is an inadequate basis for issuing a review report. Accordingly, the accountant should withdraw from a review engagement when there is a material scope limitation.

Report Restrictions. The report is required to carry a use restriction in three circumstances:

- When the criteria used to evaluate the subject matter are determined by the accountant 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.
- When the criteria used to evaluate the subject matter are available only to the specified parties.
- When a written assertion is not provided by the responsible party and the responsible party is not the client.

However, the accountant is not precluded from restricting the use of any report.

The attestation standards suggest that the practitioner consider informing the client that restricted-use reports are not intended for distribution to nonspecified parties, regardless of whether they are included in a document containing a separate general-use report. It goes on to note that the practitioner is not responsible for controlling a client's distribution of restricted-use reports. It also notes that a restricted-use report filed with a regulatory agency may be required by law or regulation to be made available to the public as a matter of public record. A restricted-use report should alert readers to the restriction on the use of the report by indicating that the report is not intended to be and should not be used by anyone other than the specified parties.

Including a restricted-use report in a document that includes a general-use report does not affect the intended use of either report. However, if two such reports are combined into a single report, it should be restricted to the specified parties.

A restricted-use report should present a separate paragraph at the end of the report containing the following:

- A statement indicating that the report is intended solely for the information and use of the specified parties.
- An identification of the specified parties to whom use is restricted.
- A statement that the report is not intended to be and should not be used by anyone other than the specified parties.

The following is an example of a use-restriction paragraph:

This report is intended solely for the information and use of [the specified parties] and is not intended to be and should not be used by anyone other than these specified parties.

When the report is restricted because of a failure to obtain a written assertion, that reason should be stated in the *introductory* paragraph of the report. If the restriction is caused by something else, the reason is not described in the report.

The following is an example of a report restricted because the criteria, while suitable, are available only to specified parties.

INDEPENDENT ACCOUNTANT'S REPORT

We have reviewed management's assertion that [Identify the assertion—for example, the accompanying schedule of investment returns of XYZ Company for the year ended December 31, 20XX is presented in accordance with the ABC criteria referred to in Note 1.]. XYZ Company's management is responsible for the assertion.

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 assertion. Accordingly, we do not express such an opinion.

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

Based on our review, nothing came to our attention that caused us to believe that management's assertion referred to above is not fairly stated, in all material respects, based on [Identify the criteria—for example, the ABC criteria referred to in Note 1.].

This report is intended solely for the information and use of XYZ Company and [Identify other specified parties.] and is not intended to be and should not be used by anyone other than these specified parties.

[Signature]

[Date]

SELF-STUDY QUIZ

Determine the best answer for each question below. Then check your answers against the correct answers in the following section.

34. Cecily Owens, CPA, is considering whether to agree to her client's request to perform a review of subject matter. Which of the following guidelines is correct?
- a. All of the attestation standards allow the performance of a review engagement.
 - b. AT 401, *Pro Forma Financial Information*, permits a review service only when the underlying historical financial statements are reviewed.
 - c. If the subject matter or criteria are too subjective to perform an examination, the practitioner should consider performing a review.
35. Joann Brown is performing a review engagement, but she is unsure about her responsibility for subsequent events in the engagement. After consulting her firm's technical manual, Joann discovers that **all but which** of the following are correct?
- a. The practitioner has no responsibility to detect events occurring after the date of the subject matter (or assertion) that might affect it.
 - b. If the practitioner identifies subsequent events that provide information about conditions that existed at the date of the subject matter, the practitioner should consider them in determining whether the subject matter conforms to the criteria.
 - c. Subsequent events refer to events that arise after the date of the practitioner's report.
36. Ethan Bales Furniture decides to include a document in the practitioner's review report to which the practitioner has devoted his or her attention. **All but which** of the following statements about the practitioner's responsibilities for the other information not covered by the practitioner's report is correct?
- a. If the practitioner believes that the other information is inconsistent with the information appearing in his or her report, he or she should consider whether the report requires revision.
 - b. If the practitioner becomes aware of information in the document that he or she believes is a material misstatement of fact that is not a material inconsistency, he or she should withdraw from the engagement.
 - c. The practitioner should read the other information not covered by the practitioner's report and consider whether it, or the manner of its presentation, is materially inconsistent with the information appearing in the practitioner's report.
 - d. If the practitioner concludes that the report does not require revision, he or she should request the client to revise the other information. If the other information is not revised to eliminate the material inconsistency, the practitioner should consider other actions.
37. Which of the following statements would be found in a review report but **not** in an examination report?
- a. An identification of the subject matter and the responsible party.
 - b. A statement that the review is substantially less in scope than an examination, the objective of which is the expression of opinion on the subject matter and, accordingly, no such opinion is expressed.
 - c. A statement that the subject matter is the responsibility of the responsible party.
 - d. The manual or printed signature of the accountant's firm.

38. Which of the following best describes a use restriction in a review report?

- a. If the responsible party is not the client, a use restriction is not necessary if the responsible party does not provide a written assertion.
- b. When the report is restricted because of a failure to obtain a written assertion, that reason should not be described in the report.
- c. If the report restriction is due to something other than a failure to provide a written assertion, the reason should be described in the report.
- d. The practitioner is not precluded from restricting the use of any report.

SELF-STUDY ANSWERS

This section provides the correct answers to the self-study quiz. If you answered a question incorrectly, reread the appropriate material. **(References are in parentheses.)**

34. Cecily Owens, CPA, is considering whether to agree to her client's request to perform a review of subject matter. Which of the following guidelines is correct? **(Page 223)**
- a. All of the attestation standards allow the performance of a review engagement. [This answer is incorrect. With a few exceptions, virtually every attestation section other than AT 101 prohibits reviews.]
 - b. **AT 401, *Pro Forma Financial Information*, permits a review service only when the underlying historical financial statements are reviewed. [This answer is correct. This is one of the few attestation standards that permits a review engagement. The other is AT 701, *Management's Discussion and Analysis*, which permits a review engagement as long as the review report is restricted to specified users.]**
 - c. If the subject matter or criteria are too subjective to perform an examination, the practitioner should consider performing a review. [This answer is incorrect. Reducing the level of service does not solve the problem in this situation according to the third general standard. Performing a review under these circumstances is inappropriate, as the rules are the same for a review and an examination.]
35. Joann Brown is performing a review engagement, but she is unsure about her responsibility for subsequent events in the engagement. After consulting her firm's technical manual, Joann discovers that **all but which** of the following are correct? **(Page 226)**
- a. The practitioner has no responsibility to detect events occurring after the date of the subject matter (or assertion) that might affect it. [This answer is incorrect. Although the practitioner has no responsibility for subsequent events in a review engagement, he or she should ask the responsible party about whether it is aware of any events that occurred between the date of the subject matter or assertion and the date of the practitioner's report that would have a material effect on the subject matter or assertion.]
 - b. If the practitioner identifies subsequent events that provide information about conditions that existed at the date of the subject matter, the practitioner should consider them in determining whether the subject matter conforms to the criteria. [This answer is incorrect. The practitioner who identifies these types of subsequent events should consider them when evaluating the results of his or her review procedures.]
 - c. **Subsequent events refer to events that arise after the date of the practitioner's report. [This answer is correct. Subsequent events are events occurring after the date of the subject matter or assertion that affect it. Events that occur after the date of the practitioner's report are not subsequent events. However, if the practitioner becomes aware of events occurring after the date of his or her report that might have affected the report had he or she known about them, the practitioner may wish to consider the guidance in AU 561, *Subsequent Discovery of Facts Existing at the Date of the Auditor's Report*.]**
36. Ethan Bales Furniture decides to include a document in the practitioner's review report to which the practitioner has devoted his or her attention. **All but which** of the following statements about the practitioner's responsibilities for the other information not covered by the practitioner's report is correct? **(Page 226)**
- a. If the practitioner believes that the other information is inconsistent with the information appearing in his or her report, he or she should consider whether the report requires revision. [This answer is incorrect. If the information is inconsistent with the report, the practitioner should consider whether report revision is necessary.]
 - b. **If the practitioner becomes aware of information in the document that he or she believes is a material misstatement of fact that is not a material inconsistency, he or she should withdraw from the engagement. [This answer is correct. When the practitioner discovers what he or she believes to**

be a material misstatement of fact, the practitioner should first discuss the matter with the client. If the practitioner concludes that a material misstatement exists, the practitioner should propose that the client consult with some other party whose advice may be useful, such as the entity's legal counsel. If, after discussing the matter, the practitioner concludes that a material misstatement of fact remains, the action taken will depend on his or her judgment in the circumstances. The practitioner should consider steps such as notifying the client's management and audit committee in writing of his or her views concerning the information and consulting his or her legal counsel about further action appropriate in the circumstances.]

- c. The practitioner should read the other information not covered by the practitioner's report and consider whether it, or the manner of its presentation, is materially inconsistent with the information appearing in the practitioner's report. [This answer is incorrect. This is the crux of the practitioner's responsibility for other information not covered by his or her report.]
 - d. If the practitioner concludes that the report does not require revision, he or she should request the client to revise the other information. If the other information is not revised to eliminate the material inconsistency, the practitioner should consider other actions. [This answer is incorrect. In this situation, the practitioner should consider revising his or her report to include an explanatory paragraph describing the material inconsistency, withholding the use of his or her report in the document, or withdrawing from the engagement.]
37. Which of the following statements would be found in a review report but **not** in an examination report? **(Page 227)**
- a. An identification of the subject matter and the responsible party. [This answer is incorrect. This statement would be found in both types of reports.]
 - b. A statement that the review is substantially less in scope than an examination, the objective of which is the expression of opinion on the subject matter and, accordingly, no such opinion is expressed. [This answer is correct. This statement pertains only in a review engagement. Accordingly, it would be found only in a review report. An examination report would contain the practitioner's opinion on whether the subject matter is based on, or in conformity with, the criteria in all material respects based on the criteria.]**
 - c. A statement that the subject matter is the responsibility of the responsible party. [This answer is incorrect. This statement would be found in both types of reports.]
 - d. The manual or printed signature of the accountant's firm. [This answer is incorrect. This statement would be found in both types of reports.]
38. Which of the following best describes a use restriction in a review report? **(Page 227)**
- a. If the responsible party is not the client, a use restriction is not necessary if the responsible party does not provide a written assertion. [This answer is incorrect. If the responsible party is not the client, the practitioner should restrict the use of the report for the responsible party's failure to provide a written assertion.]
 - b. When the report is restricted because of a failure to obtain a written assertion, that reason should not be described in the report. [This answer is incorrect. The reason for the restriction should be described in the introductory paragraph of the report.]
 - c. If the report restriction is due to something other than a failure to provide a written assertion, the reason should be described in the report. [This answer is incorrect. The reason for a restriction should not be included in the report unless it is because of the failure to obtain a written assertion.]
 - d. The practitioner is not precluded from restricting the use of any report. [This answer is correct. The attest standards do not preclude a practitioner from restricting the use of any report for any reason.]**

ENGAGEMENT WRAP-UP, SUPERVISION, AND ADMINISTRATION

SQCS No. 7, "A Firm's System of Quality Control," indicates at QC 10.60–.61 that a firm should establish policies and procedures that address supervision and review responsibilities. The review responsibility policies and procedures should be determined on the basis that qualified engagement team members review the work performed by other team members on a timely basis. The review may include consideration of factors such as the following:

- The work has been performed in accordance with professional standards and any applicable regulatory and legal requirements.
- Significant findings and issues have been considered.
- Appropriate consultations have taken place and the resulting conclusions have been documented and implemented.
- The nature, timing, and extent of work performed is sufficient and appropriate.
- The work performed supports the conclusions reached and is appropriately documented.
- The evidence obtained is sufficient and appropriate to support the practitioner's report.
- The objectives of the engagement procedures have been achieved.

Workpaper Review

In both examination and review engagements, there are generally two levels of workpaper review: the detailed review done on the staff assistants' work and the overall supervisory review done by the partner or manager on the engagement.

The detailed review focuses on the workpapers. It is usually, but not always, done before fieldwork is completed. This review is generally geared towards making sure that:

- Each workpaper is complete and properly prepared.
- Items tested agree to those presented in the subject matter.
- The work program has been completed.
- Misstatements have been properly identified and analyzed.

SSAE No. 10, as amended, requires firms to indicate in the workpapers who performed and reviewed the work. Most firms require the person performing the detailed review to initial each workpaper and schedule that is reviewed.

The supervisory review generally focuses on the summary schedules and conclusions drawn. It is usually conducted after the bulk of fieldwork has been done. This review is the final check on whether the work supports the overall conclusions and the subject matter presented.

It is common for firms to require formal wrap-up procedures to ensure that all necessary technical and administrative matters have been resolved. In addition, SSAE No. 10, as amended, states that workpapers should indicate who reviewed the work. Most firms use some form of checklist to serve as a reminder of those important engagement completion matters and to document completion of the review of the workpapers. A checklist that the practitioner can use to document the wrap-up portion of the engagement would require:

- The staff in charge of fieldwork to sign off when appropriate reviews of the workpapers and report have been completed.

- The partner to indicate that the engagement was adequate and the significant matters were appropriately handled.
- If required by firm policy, an independent reviewer to indicate satisfaction with the engagement.

Other Practitioners

The practitioner whose report is based, in part, on the work of other practitioners who have examined or reviewed subsidiary components of the subject matter can look to SAS No. 1 (AU 543), *Part of Audit Performed by Other Independent Auditors*, for guidance. The SAS suggests inquiries that should be made to obtain assurance about the other practitioner's independence, competence, reputation, and understanding about the use of his or her report.

The practitioner should decide whether to refer to the other practitioner in the attestation report. The SAS suggests that the practitioner could decide not to refer to the work of the other practitioner if:

- the other practitioner was a related firm or otherwise retained by the practitioner and performed the work under the practitioner's guidance,
- the practitioner takes the steps necessary to obtain satisfaction as to the procedures applied by the other practitioner and the reasonableness of the subject matter the other practitioner reported on, or
- the subject matter reported on by the other practitioner is immaterial to the consolidated subject matter.

If the practitioner decides to refer to the work of the other practitioner, the report should indicate the extent of the other practitioner's responsibility. Generally, the introductory, scope, and opinion paragraphs of the standard report are revised to reflect the other practitioner's participation.

The introductory paragraph quantifies the other practitioner's participation. A passage similar to the following might be added to the end of the introductory paragraph of an examination report (similar language should be added to a review report):

We did not examine the [Identify subject matter, for example—Investment Performance of B Company.] which constitutes [Quantify other practitioner's participation, for example—19% of the consolidated total.]. That statement was examined by other accountants whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for [Identify subject matter examined by other practitioner, for example—B Company.], is based solely on the report of the other accountants.

The last sentence of the standard scope paragraph also should be revised, as follows:

We believe that our examination and the report of the other accountants provide a reasonable basis for our opinion.

The opinion paragraph also refers to the other practitioners as follows:

In our opinion, based on our examination and the report of the other accountants, the [Identify subject matter, for example—Statement of Investment Performance Statistics.] is presented. . .

Other Communications

Unlike the auditing literature, AT 101 does not require specific communications other than the issuance of the attestation report. So, for example, the practitioner is not required to communicate significant deficiencies in internal control, errors, fraud, or other illegal acts discovered during the engagement.

Nonetheless, the practitioner should consider reporting these matters to the client as would be done in an audit. This communication may be helpful to the client. It also might limit the practitioner's risk of lawsuits in the event that such matters eventually cause a loss to the client.

Changing the Level of Service

The practitioner who was initially engaged to do an examination might be asked to change the engagement to a review. Attestation standards do not address this issue other than to state (in AT 101.32) that it is not appropriate to change the engagement from an examination to a review if the practitioner has determined that an examination cannot be performed because the criteria are not subject to reasonably consistent evaluation. The practitioner cannot solve a problem of unsuitable criteria by providing a lower level of service.

SSARS No. 19 provides guidance in regard to changes in the level of service for financial statement engagements that can be adapted for attestation engagements. Based on that guidance, if the examination engagement has begun, best practices indicate that the practitioner should consider the following issues before agreeing to the review:

- The reason given for the client's request, particularly the implications of a restriction on the scope of the examination.
- The additional effort required to complete the examination.
- The estimated additional cost to complete the examination.

A change in circumstances affecting the entity's requirement for an examination or a misunderstanding concerning the nature of the services would ordinarily be considered a reasonable basis for the request.

In considering the implications of a restriction on scope, the practitioner should evaluate the possibility that the information affected by the scope restriction may be incorrect, incomplete, or otherwise misleading. If the examination is substantially complete or if the cost to complete it is relatively insignificant, the practitioner should consider the propriety of the request to change the nature of the engagement.

If the practitioner agrees to modify the nature of the engagement, the resulting review report should make no reference to the original engagement, to the change, or to any examination procedures applied.

A client request to change the engagement to an agreed-upon procedures engagement does not generally present a problem to the practitioner. That is because, in an agreed-upon procedure engagement, the users specify the procedures to be performed and are responsible for the sufficiency of the procedures.

Withdrawal

Best practices indicate that the practitioner should consider withdrawing from an examination or review engagement if:

- The practitioner has substantive doubts about the integrity of the client.
- The client refuses the practitioner's request to provide a signed representation letter.
- The practitioner determines that he or she does not have, or cannot obtain, the required knowledge in the subject matter.
- The practitioner determines that he or she is not independent.
- The practitioner encounters a scope restriction that cannot be resolved. (Withdrawal is required in review engagements.)
- The practitioner has significant reservations about the subject matter or the engagement in a review.

Statement on Quality Control Standards (SQCS) No. 7, *A Firm's System of Quality Control*, indicates that a firm should establish policies and procedures on withdrawal from an engagement or from both an engagement and the client relationship. Documentation should include significant issues, consultations, conclusions, and the basis for the conclusions.

SELF-STUDY QUIZ

Determine the best answer for each question below. Then check your answers against the correct answers in the following section.

39. There are typically two reviews performed on each review engagement: a detailed review and a supervisory review. Which of the following statements about the supervisory review is **not** correct?
- a. The supervisory review is the final check on whether the work supports the overall conclusions and the subject matter presented.
 - b. The supervisory review focuses on the adequate completion of the workpapers.
 - c. The supervisory review generally focuses on the summary schedules and conclusions drawn.
 - d. The supervisory review is usually conducted after the bulk of fieldwork has been done.
40. When a client makes a request to change from an examination engagement to a review engagement, which of the following best describes the practitioner's alternatives?
- a. The practitioner cannot solve a problem of unsuitable criteria in an examination engagement by providing a lower level of service.
 - b. Even if the examination is substantially complete, the practitioner need not be concerned about the propriety of the request to change the nature of the engagement.
 - c. If the practitioner agrees to modify the nature of the engagement, the resulting review report should refer to the original engagement, to the change, and to any examination procedures applied.
 - d. A change in circumstances affecting the entity's requirement for an examination or a misunderstanding concerning the nature of the services would ordinarily not be considered a reasonable basis for the request.

SELF-STUDY ANSWERS

This section provides the correct answers to the self-study quiz. If you answered a question incorrectly, reread the appropriate material. **(References are in parentheses.)**

39. There are typically two reviews performed on each review engagement: a detailed review and a supervisory review. Which of the following statements about the supervisory review is **not** correct? **(Page 237)**
- a. The supervisory review is the final check on whether the work supports the overall conclusions and the subject matter presented. [This answer is incorrect. This is one of the purposes of the supervisory review.]
 - b. The supervisory review focuses on the adequate completion of the workpapers. [This answer is correct. The detailed review focuses on the workpapers and ensuring they were properly prepared, not the supervisory review.]**
 - c. The supervisory review generally focuses on the summary schedules and conclusions drawn. [This answer is incorrect. This is one of the purposes of the supervisory review.]
 - d. The supervisory review is usually conducted after the bulk of fieldwork has been done. [This answer is incorrect. This is the typical timing for a supervisory review.]
40. When a client makes a request to change from an examination engagement to a review engagement, which of the following best describes the practitioner's alternatives? **(Page 239)**
- a. The practitioner cannot solve a problem of unsuitable criteria in an examination engagement by providing a lower level of service. [This answer is correct. Although the attestation standards do not address this issue in detail, they do state in AT 101.32 that it is not appropriate to change the engagement from an examination to a review if the practitioner has determined that an examination cannot be performed because the criteria are not subject to reasonably consistent evaluation.]**
 - b. Even if the examination is substantially complete, the practitioner need not be concerned about the propriety of the request to change the nature of the engagement. [This answer is incorrect. Whenever the practitioner is asked to change the nature of the engagement, particularly if the engagement is substantially complete, the practitioner should consider the propriety of the request to change the nature of the engagement.]
 - c. If the practitioner agrees to modify the nature of the engagement, the resulting review report should refer to the original engagement, to the change, and to any examination procedures applied. [This answer is incorrect. The review report should not include a reference to any of these matters. In other words, a user should not be aware from reading the review report that there has been a change in service.]
 - d. A change in circumstances affecting the entity's requirement for an examination or a misunderstanding concerning the nature of the services would ordinarily not be considered a reasonable basis for the request. [This answer is incorrect. For instance, if a client believed its lender required an examination report, and discovered during the engagement that a review would satisfy its purposes, the practitioner could consider the client's request reasonable.]

EXAMINATION FOR CPE CREDIT**Lesson 3 (NTEG102)**

Determine the best answer for each question below. Then mark your answer choice on the Examination for CPE Credit Answer Sheet located in the back of this workbook or by logging onto the Online Grading System.

31. Which of the following best describes the characteristics of a review engagement under the attestation standards?
- a. A review engagement provides a high level of assurance on the subject matter.
 - b. A review engagement provides a basis for the practitioner to report that he or she is not aware of any material adjustments that need to be made for either (a) the subject matter to be in conformity with the criteria, in all material respects or (b) the assertion regarding the subject matter to be fairly stated, in all material respects, based on the criteria.
 - c. AT 101 prohibits reviews in all but a few situations in which examinations can be performed.
 - d. Performing reviews in most cases is encouraged since they are less time consuming than an examination.
32. Which of the following procedures generally are **not** performed in a review engagement?
- a. Reading the subject matter to consider whether it appears to conform to the criteria.
 - b. Analytical procedures.
 - c. Inquiries of client personnel.
 - d. Confirmations.
33. **All but which** of the following statements about the practitioner's responsibilities for a representation letter in a review engagement is correct?
- a. The representation letter should be dated as of the date of the practitioner's report.
 - b. The representation letter should be signed by members of management whom the practitioner believes are responsible for and knowledgeable, directly or through others in the organization, about matters covered by the representation.
 - c. When the client is not the responsible party, the practitioner should also consider obtaining a representation letter from the client.
 - d. AT 101 requires that practitioners obtain a representation letter from the responsible party in review engagements.

34. After the practitioner issued her report, she discovered that the responsible party had entered into a material contract with a major supplier before the engagement. Which of the following best describes the possible effect of this event on the practitioner's report?
- a. If the event might have affected the report had he or she known about them, the practitioner may wish to consider the guidance in AU 561, *Subsequent Discovery of Facts Existing at the Date of the Auditor's Report*.
 - b. The practitioner has no responsibility for this event since it occurred after the date of her report.
 - c. Because this subsequent event provides information about conditions that existed at the date of the subject matter, the practitioner should consider it when determining whether the subject matter conforms to the criteria.
 - d. Because this subsequent event provides information about conditions that arose after the date of the subject matter, the practitioner should disclose it only if necessary to keep the subject matter from being misleading.
35. Although it is not explicit in AT 101, a review report may include additional commentary or information. Such additional information might **all but which** of the following?
- a. Information about uncertainties, such as pending legislation that might affect the assertions in the future.
 - b. Inherent limitations of the data so that it is not misinterpreted.
 - c. Description of a limitation on the scope of the engagement.
 - d. Emphasis of certain aspects of the data, such as the interpretations made in applying the criteria.
36. The practitioner's review report should address consistency in certain situations. Which of the following is **not** included the practitioner's responsibility for consistency in a review report?
- a. The practitioner should decide if the criteria are clearly stated or described for each of the periods or dates if the report includes multiple periods or dates where criteria changed.
 - b. The practitioner should decide if the changes have been sufficiently disclosed if the report is on comparative information.
 - c. The practitioner should consider if the changes in criteria could be significant to users of the report; if so, they should be disclosed if the criteria used for the current report differ from those used in the past and the prior subject matter is not presented.
 - d. The practitioner should withdraw from the engagement if the practitioner believes changes in the criteria from one period to the next could be significant to users and if prior subject matter is not presented.
37. SSAE No.10, as amended, requires which of the following?
- a. Requires firms to consider current and prospective client integrity.
 - b. Requires firms to note in the workpapers who performed and reviewed the work.
 - c. Requires that the practitioner document the justification for any departure from a presumptively mandatory requirement and a description of how the practitioner achieved its objectives.
 - d. Requires that the subject matter be capable of reasonably consistent estimation or measurement using the criteria.

38. The practitioner whose report is based, in part, on the work of other practitioners who have examined or reviewed subsidiary components of the subject matter can look to SAS No. 1, *Part of Audit Performed by Other Independent Auditors*, for guidance. **All but which** of the following describes the guidance in that SAS?
- a. The practitioner should make inquiries to obtain assurance about the other practitioner's independence, competence, reputation, and understanding about the use of his or her report.
 - b. The practitioner must refer to the other practitioner in the attestation report.
 - c. The practitioner should not refer to the work of the other practitioner if the subject matter is immaterial.
 - d. If the practitioner decides to refer to the work of the other practitioner, the report should indicate the extent of the other practitioner's responsibility.
39. Unlike the auditing literature, AT 101 requires which of the following?
- a. Communication of significant deficiencies in fraud.
 - b. The issuance of specific information regarding internal control.
 - c. The issuance of an illustrative review report.
 - d. The issuance of the attestation report.
40. Thomas Thumbs, a practitioner, encounters a scope limitation during a review engagement with his client. The limitation is not resolved. What must Mr. Thumbs do?
- a. Must withdraw from the engagement.
 - b. Consider withdrawing from the engagement.
 - c. Proceed cautiously.
 - d. Contact his attorney.

GLOSSARY

Attestation engagement: One in which a practitioner issues a specific type of report on subject matter that is the responsibility of another party.

Agreed-upon procedures engagement: One in which a practitioner is engaged by a client to perform specific procedures and report findings. The practitioner does not perform an audit or provide an opinion relating to the subject matter or assertion about the subject matter. Rather the practitioner performs only those procedures that have been agreed to and reports findings.

Assertion: Any declaration or set of related declarations about whether the subject matter is based on or in conformity with the criteria selected.

AT 101, Attestation Standards: The umbrella standard that governs all types of attestation engagements, of which there are three: examinations, reviews, and agreed-upon procedures engagements.

AT 201, Agreed-upon Procedures Engagements: The specific guidance on performing agreed-upon procedures engagements.

Attestation interpretations: Recommendations on applying the SSAEs in specific circumstances.

Attestation standards: Consist of the 11 general, field work, and reporting standards and Statements on Standards for Attestation Engagements (SSAEs) issued by the AICPA's Auditing Standards Board (ASB).

Competence: Adequate technical training and proficiency in the attest function and adequate knowledge of the subject matter.

Control risk: The risk that a material misstatement that did occur would not be prevented or detected by the client.

Criteria: The subject matter must have an objective parameter by which it is measured—this basis is called the criteria.

Detection risk: The risk that a material misstatement that eludes the client will also elude the practitioner.

Engagement review: This is for firms that are not required to undergo a system review and do not qualify for a report review. It is for firms that perform SSARS compilations of financial statements that do not omit substantially all disclosures required by GAAP, SSARS reviews, or services under SSAEs.

Examination: Highest level of attestation engagement. Analogous to an audit of historical financial statements.

Financial statement: Something that looks like a financial statement, but is not a tax return.

Inherent risk: The susceptibility of the subject matter to material misstatement.

Materiality: The magnitude of omissions or misstatements—individually or when aggregated with others—that would influence a reasonable person.

Presumptively mandatory requirements: Those that a practitioner is expected to comply with if the circumstances apply to the requirement. If the requirement uses the words *should consider* for a procedure, the consideration of the procedure is presumptively required.

Responsible party: Someone, other than the practitioner, who takes responsibility for the subject matter. Generally, this is the management of the entity whose subject matter is being measured. Generally the responsible party is a group, rather than an individual. It can be the client, but need not be.

Report date: No earlier than “the date on which the auditor has obtained sufficient appropriate audit evidence to support the opinion”. This is per SS No. 103.

Review: Provides limited assurance. Requires the practitioner to reduce the risk of undetected material misstatement to a moderate level and primarily involves inquires and analytical procedures. The review report provides negative assurance.

Risk assessment standards: Eight statements on auditing standards (SAS Nos. 104–111) related to the auditor's risk assessment process.

Risk of material misstatement: Combination of inherent and control risks.

Sampling risk: The risk that the practitioner may reach a different conclusion if the procedures are applied to a sample than if they are applied to all items in a population.

Special engagement: Consist primarily of nonaudit engagements addressed in the auditing standards.

Specified party: Third parties such as banks, regulatory agencies, prospective investors, and prospective purchasers who may ask for enhanced credibility of client provided information. In many cases, the client is also a specified party.

Subject matter: What the engagement is made about. What the practitioner applies procedures to.

Unconditional requirements: Those that a practitioner must follow in all cases if the circumstances apply to the requirement. These requirements use the words *must* or *is required*.

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TESTING INSTRUCTIONS FOR EXAMINATION FOR CPE CREDIT

Companion to PPC's Guide to Nontraditional Engagements—Course 1—An Introduction to Nontraditional Engagements and Agreed-upon Procedures Engagements (NTETG101)

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Please indicate your answer by filling in the appropriate circle as shown: Fill in like this ● not like this ○ ⊗ ⊙.

a	b	c	d	a	b	c	d	a	b	c	d	a	b	c	d
1. ○	○	○	○	11. ○	○	○	○	21. ○	○	○	○	31. ○	○	○	○
2. ○	○	○	○	12. ○	○	○	○	22. ○	○	○	○	32. ○	○	○	○
3. ○	○	○	○	13. ○	○	○	○	23. ○	○	○	○	33. ○	○	○	○
4. ○	○	○	○	14. ○	○	○	○	24. ○	○	○	○	34. ○	○	○	○
5. ○	○	○	○	15. ○	○	○	○	25. ○	○	○	○	35. ○	○	○	○
6. ○	○	○	○	16. ○	○	○	○	26. ○	○	○	○	36. ○	○	○	○
7. ○	○	○	○	17. ○	○	○	○	27. ○	○	○	○	37. ○	○	○	○
8. ○	○	○	○	18. ○	○	○	○	28. ○	○	○	○	38. ○	○	○	○
9. ○	○	○	○	19. ○	○	○	○	29. ○	○	○	○	39. ○	○	○	○
10. ○	○	○	○	20. ○	○	○	○	30. ○	○	○	○	40. ○	○	○	○

You may complete the exam online by logging onto our online grading system at **cl.thomsonreuters.com**, or you may fax completed Examination for CPE Credit Answer Sheet and Course Evaluation to Thomson Reuters at (817) 252-4021, along with your credit card information.

Expiration Date: December 31, 2011

Self-study Course Evaluation

Please Print Legibly—Thank you for your feedback!

Course Title: Companion to PPC's Guide to Nontraditional Engagements—Course 2 Course Acronym: NTETG102
—Performing Examination and Review Engagements under the Attestation Standards

Your Name (optional): _____ Date: _____

Email: _____

Please indicate your answers by filling in the appropriate circle as shown:

Fill in like this ☒ not like this ☐ ☐ ☒.

Satisfaction Level:	Low (1) . . . to . . . High (10)									
	1	2	3	4	5	6	7	8	9	10
1. Rate the appropriateness of the materials for your experience level:	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
2. How would you rate the examination related to the course material?	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
3. Does the examination consist of clear and unambiguous questions and statements?	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
4. Were the stated learning objectives met?	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
5. Were the course materials accurate and useful?	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
6. Were the course materials relevant and did they contribute to the achievement of the learning objectives?	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
7. Was the time allotted to the learning activity appropriate?	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
8. If applicable, was the technological equipment appropriate?	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
9. If applicable, were handout or advance preparation materials and prerequisites satisfactory?	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
10. If applicable, how well did the audio/visuals contribute to the program?	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>

Please provide any constructive criticism you may have about the course materials, such as particularly difficult parts, hard to understand areas, unclear instructions, appropriateness of subjects, educational value, and ways to make it more fun. Please be as specific as you can.

(Please print legibly):

Additional Comments:

- What did you find **most** helpful? _____
- What did you find **least** helpful? _____
- What other courses or subject areas would you like for us to offer? _____
- Do you work in a Corporate (C), Professional Accounting (PA), Legal (L), or Government (G) setting? _____
- How many employees are in your company? _____
- May we contact you for survey purposes (Y/N)? If yes, please fill out contact info at the top of the page. **Yes/No** ☐ ☐

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