Everything But Tax Update 2026

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Auditing, Attestation and Accounting Update

Title
FASB Standards
ARSC Update, Comps, and Reviews
QM Standards
Ethics and Independence
Audit Standards Update/Workpaper Documentation
Peer Review

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FASB Accounting Standards Updates

Learning objective

- Identify recently issued FASB Accounting Standards Updates (ASUs) that cover broad issues, other than those related to the "big three" of revenue recognition, financial instruments, and leases.

ASU’s Issued

Year	ASU’s Issued
2025	12
2024	4
2023	6
2022	6
2021	10
2020	11
2019	12
2018	20

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ASU No. 2022-03, Fair Value Measurement *(Topic 820): Fair Value Measurement of Equity Securities Subject to Contractual Sale Restrictions*

- Applies to entities that are required to account for equity securities at fair value and those securities are subject to a contractual sales restriction.
- Do not account for any contractual restriction of an equity security in determining the fair value of the equity security.
- Transition
  - Include in income any increase in fair value due to the exclusion of the discount that had been recognized due to the contractual restriction.

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Required disclosures and effective date

- The fair value of equity securities subject to contractual sales restrictions reflected in the balance sheet
- The nature and remaining duration of the restrictions
- The circumstances that could cause a lapse in the restrictions

Public business entities:

- Fiscal years beginning after December 15, 2023, and interim periods within those years

All other entities:

- Fiscal years beginning after December 15, 2024, and interim periods within those years.

Early adoption is permitted for financial statements that have not been issued or made available for issuance.

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ASU No. 2023-05: *Business Combinations-Joint Venture Formations — (Subtopic 805-60): Recognition and Initial Measurement*

Codifies accounting for the newly formed joint venture for the initial contribution of asset and assumption of liabilities

Current ASC does not provide guidance and specifically excluded joint ventures from Topic 805 and Topic 845

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ASU No. 2023-05: *Business Combinations-Joint Venture Formations — (Subtopic 805-60: Initial Measurement*

- Overarching principle is this is a new entity and acquisition method of accounting will be followed with no acquiring entity (with exceptions)
- Measure identifiable contributed assets and liabilities at fair value, including goodwill, if any
- Equity at formation will be equal to 100% of fair value of identified net assets

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ASU No. 2023-05: *Business Combinations-Joint Venture Formations — (Subtopic 805-60: Disclosures*

The financial statements of the joint venture will disclose relevant information

- Nature and effect of formation
- Date of formation

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ASU No. 2023-05: *Business Combinations-Joint Venture Formations — (Subtopic 805-60: Effective Date*

- Joint venture formations on or after January 1, 2025
- Early adoption permitted
- Retrospective application can be applied for existing joint venture is relevant information is available.

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FASB ASU No. 2023-08, *Intangibles — Goodwill and Other — Crypto Assets — (Subtopic 350-60): Accounting for and Disclosure of Crypto Assets*

Characteristics of a crypto asset

- Meets ASC definition of an intangible asset
- Does not provide enforceable rights
- Created by blockchain or similar technology
- Secured through cryptography
- Fungible
- Not created or issued by the reporting entity or related party

Measurement of Crypto Assets

Measured at fair value on balance sheet date

May be level 1, 2, or 3 inputs

Gain or loss reported on the income statement or statement of activities

Presentation of Crypto Assets

Present on balance sheet separately from other intangible assets

May be current or non-current

Report as cash transaction on Statement of Cash Flows if Crypto is received for the sale of goods or services and immediately converted to cash

Gain or loss is reported or disclosed separately from gains or losses from other intangible assets

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Disclosure of Crypto Assets

Interim and annual disclosures

- Name, cost basis, fair value, and number of units for each significant crypt holding
- May aggregate information for holdings that are not individually significant
- Any contractual sales restrictions for crypto assets and circumstances that could cause the restrictions to lapse

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Disclosure of Crypto Assets (continued)

Annual disclosures

- Aggregate rollforward of crypto holdings (beginning balance, additions, dispositions, and gains and losses)
- Gain or loss on disposals and line item on income statement where reported (if not reported separately)
- Method for determining cost basis

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Effective Date and Transition

All entities for fiscal periods ending after December 15, 2024, and interim periods within that fiscal period

Early adoption permitted

Record a cumulative-effect adjustment to adjust the recorded value of any crypto asset to fair value on the first day of the fiscal year of adoption

ASU No. 2023-09, *Income Taxes (Topic 740): Improvements to Income Tax Disclosures*

- Enhances and adds specific disclosures
- Most changes relate to public business entities
- Eliminates some disclosures

Rate reconciliation — Public entities

Tabular reconciliation with the following categories:

- State and local, net of federal
- Foreign tax effects
- Effect of changes in tax laws, current
- Effect of cross-border tax laws
- Tax credits
- Changes in valuation allowance
- Nontaxable or deductible items
- Changes in unrecognized tax benefits

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Rate reconciliation (continued)

- Certain items must be further disaggregated if the effect of the reconciling items is equal to or greater than 5% of income or loss from continuing operations before income taxes by the applicable statutory income tax rate
- Explanations, if not otherwise evident, of individual reconciling items disclosed (nature, effect, and underlying causes of the reconciling items)
- Judgment used in categorizing reconciling items

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Rate reconciliation — Non-public entities

Qualitative disclosures about the following items that cause a difference between the statutory tax rate and the effective tax rate

- Specific categories of reconciling items
- Individual jurisdictions

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Disclosures — Income taxes paid

- The amount of income taxes paid (net of refunds), disaggregated by federal, state, and foreign taxes
- The amount of income taxes paid (net of refunds) disaggregated by individual jurisdictions in which income taxes is equal to or greater than 5% of total income taxes paid (net of refunds)

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Other disclosures

- Income or loss from continuing operations before income tax expense (or benefit) disaggregated between foreign and domestic
- Income tax expense (or benefit) from continuing operations disaggregated by federal, state, and foreign

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Eliminated disclosures

- Nature and estimate of the range of reasonably possible change in the unrecognized tax benefits balance in the next 12 months or a statement that such an estimate of the range cannot be made
- Cumulative amount of each type of temporary difference when a deferred tax liability is not recognized because of certain exceptions

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Effective date of ASU No. 2023-09

Public business entities

Periods beginning after December 15, 2024

Other than public business entities

Periods beginning after December 15, 2025

Early adoption permitted

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ASU No. 2024-01, *Compensation – Stock Compensation (Topic 718): Scope Application of Profits Interest and Similar Awards*

- Aims to improve clarity and lead to consistent application
- Provides illustrative examples to help practitioners apply scope guidance in determining whether profits interest and similar awards should be accounted for under Topic 718, Compensation – Stock Compensation
- Issued in response to complexities and diversity in practice (even for similar fact patterns) identified by the PCC regarding the accounting of profits interest awards, which are used by entities to align compensation with performance and provide participants with future profits and/or equity appreciation

Effective date of ASU No. 2024-01

For public business entities (PBEs), the amendments are effective for annual periods beginning after December 15, 2024, including interim periods within those annual periods

For all other entities, they are effective for annual periods beginning after December 15, 2025, and interim periods within those annual periods

Early adoption is permitted for both interim and annual financial statements not yet issued or available for issuance

Entities can apply the amendments retrospectively to all prior periods presented or prospectively to awards granted or modified after the first application date

ASU No. 2024-02, Codification Improvements – Amendments to Remove References to the Concepts Statements

- Introduces amendments to the Codification to remove all references to the Concepts Statements, which are nonauthoritative
- Ensures the Codification only reflects authoritative U.S. GAAP
- The update is expected to streamline the application of GAAP by eliminating potential confusion over the role of Concepts Statements in preparing financial statements

Effective date of ASU No. 2024-02

Effective for public entities for fiscal years beginning after December 15, 2024; for private entities, the effective date is after December 15, 2025

Early adoption is permitted for any fiscal year or interim period within

The transition can be applied either prospectively to all new or modified transactions recognized on or after the date of first application or retrospectively to the beginning of the earliest comparative period presented

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2025 FASB ASUs — At a Glance

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ASU 2025-01	Expense Disaggregation Effective Date Clarification
ASU 2025-02	SAB No. 122 — Crypto Assets
ASU 2025-03	Business Combinations & VIE Acquirer
ASU 2025-04	Share-Based Consideration Payable to Customer
ASU 2025-05	Credit Losses — Private Co. Simplification
ASU 2025-06	Internal-Use Software Improvements
ASU 2025-07	Derivatives Scope Refinements
ASU 2025-08	Credit Losses — Purchased Loans
ASU 2025-09	Hedge Accounting Improvements
ASU 2025-10	Government Grants
ASU 2025-11	Interim Reporting Narrow-Scope Fixes
ASU 2025-12	Codification Improvements

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ASU No. 2025-05, Measurement of Credit Losses for Accounts Receivable and Contract Assets

- Introduces a practical expedient for all entities and an accounting policy election for entities other than public business entities related to applying Subtopic 326-20 to current accounts receivable and current contract assets arising from transactions accounted for under Topic 606.
- Stakeholders observed that estimating expected credit losses for current accounts receivable and current contract assets that were collected before the date that the financial statements were available to be issued can require significant effort and documentation and can result in recording expected credit losses for amounts that have been subsequently collected.

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ASU No. 2025-05, Measurement of Credit Losses for Accounts Receivable and Contract Assets (cont.)

- Stakeholders noted that the ability to consider collection activity after the balance sheet date when estimating expected credit losses would provide investors and other financial statement users with decision-useful information while significantly reducing complexity for preparers.
- The amendments in this Update affect entities that apply the practical expedient and accounting policy election (if applicable) when estimating expected credit losses on current accounts receivable and/or current contract assets arising from transactions under Topic 606, including those assets acquired in a transaction accounted for under Topic 805, Business Combinations.

ASU No. 2025-05, Measurement of Credit Losses for Accounts Receivable and Contract Assets (cont.)

- The amendments in this Update provide (1) all entities with a practical expedient and (2) entities other than public business entities with an accounting policy election when estimating expected credit losses for current accounts receivable and current contract assets arising from transactions accounted for under Topic 606, as follows:

1. Practical expedient. In developing reasonable and supportable forecasts as part of estimating expected credit losses, all entities may elect a practical expedient that assumes that current conditions as of the balance sheet date do not change for the remaining life of the asset.

2. Accounting policy election. An entity other than a public business entity that elects the practical expedient is permitted to make an accounting policy election to consider collection activity after the balance sheet date when estimating expected credit losses.

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ASU No. 2025-05, Effective Date

- An entity that elects the practical expedient and the accounting policy election, if applicable, should apply the amendments in this Update prospectively.
- The amendments will be effective for annual reporting periods beginning after December 15, 2025, and interim reporting periods within those annual reporting periods. Early adoption is permitted in both interim and annual reporting periods in which financial statements have not yet been issued or made available for issuance.
- An entity other than a public business entity that elects the practical expedient and, if applicable, the accounting policy election after the effective date would not need to perform a preferability assessment in accordance with paragraph 250-10-45-2.

PCC and FASB Technical Agenda

Purpose and Composition of PCC

- Two primary responsibilities:
  - To determine whether exceptions or modifications to existing non-governmental U.S. GAAP are required to address the needs of users of private company financial statements; and
  - To serve as the primary advisory body to the FASB on the appropriate treatment for private companies for items under active consideration on the FASB's technical agenda
- The PCC has completed this first responsibility and is now generally serving in a consulting and advisory role to the FASB as the FASB progresses on its technical agenda
- Influence of PCC seen in recently issued FASBs on consolidation, etc..

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Composition of PCC

- Between 9–12 members, including a Chairman
- Appointed by FAF Board of Trustees
- Represent broad constituencies:
  - Financial statement users
  - Financial statement preparers
  - Accounting practitioners

Items on Which the PCC is Consulting

- Accounting for and Disclosure of Crypto Assets project;
- Accounting for and Disclosure of Software Costs project;
- Accounting for Investments in Tax Credit Structures Using the Proportional Amortization Method project;
- Accounting for Environmental Credit Programs project;
- Stock-Based Compensation project;
- Profits Interests and Their Interrelationship with Partnership Accounting project;
- FASB’s Agenda consultation;
- Implementation issues related to ASC 606, 842 and 326; and
- Targeted Improvements to Income Tax Disclosures project

FASB Technical Agenda

- 8 active projects as of December 2025:
  - Accounting for Debt Exchanges (Final ASU expected Q1 2026)
  - Accounting for Environmental Credit Programs (Final ASU expected Q1 2026)
  - Accounting for Transfers of Crypto Assets
  - Classification of Certain Digital Assets as Cash Equivalents
  - Codification Improvements (Evergreen)
  - Equity Method of Accounting: Targeted Improvements
  - Initial Measurement of Paid-in-Kind Dividends on Equity-Classified Preferred Stock
  - Statement of Cash Flows: Targeted Improvements
  - Details available at FASB.org

Additional FASB Projects

- 8 Research Projects (e.g., Goodwill, Hedge Accounting, Consolidation
- 3 EITF Projects
- 1 Post Implementation Review (Credit Losses)

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Where are we at with the “Big 3”?

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FASB Post-Implementation Reviews

- FASB has begun Post-Implementation Reviews (PIRs) for the following standards:
  - ASC 606 – *Revenue from Contracts with Customers - Completed*
  - ASC 842 – *Leases – Completed November 20, 2025*
  - ASC 326 – *Credit Losses – Stage 1*
- Purpose of PIR process
  - An evaluation of whether a standard is achieving its objective by providing financial statement users with relevant information in ways that justify the cost of providing it
  - During the PIR process, the FASB solicits and considers diverse stakeholder input and other research to evaluate the standards that are issued and determine whether there are areas of improvements that the FASB should address

Stages of PIR Process

- Stage 1 – Post-issuance date implementation monitoring
  - Actively monitor practice as stakeholders prepare for initial implementation
  - Develop and disseminate implementation guidance and educational material
  - Communicate and perform outreach with stakeholder organizations
- Stage 2 – Post-effective date evaluation of costs and benefits
  - Understand the costs that an entity incurred in applying the standard, as well as the costs that investors and other users incurred in analyzing and interpreting the information that the standard provides
  - Understand the benefits of the standard to investors and other users as well as to entities
  - Monitor the ongoing application of the standard
- Stage 3 – Summary of research and reporting

Objectives of 606 PIR Process

1. Determine if ASC 606 fulfills its stated purpose, specifically evaluating whether it resolves the underlying issues that prompted its development, provides decision-useful information, is operational in practice, and has not resulted in significant unintended consequences

2. Evaluate the implementation and compliance costs, as well as the benefits realized by various stakeholders, including preparers, investors, and regulators

3. Gather feedback to refine the standard-setting process, particularly regarding effective date selection, coordination with other accounting guidance, and considerations for globally converged standards

ASC 606 PIR – Stage 1 Activities 2014

- Status of PIR activities
  - Six meetings of the TRG
  - Variety of standard-setting activity
  - Issuance of ASU No. 2021-03 and ASU No. 2021-09
  - Responses to over 250 technical inquiries
  - Dissemination of technical materials
  - Held webcasts and other communication events

ASC 606 PIR – Stage 2 – 2018-2024

- Public company-focused activities
  - 42 company preparer surveys
  - Outreach to auditors and regulators
  - Accounting system focus
    - Gathering of feedback for advisory meetings
    - Performed analysis of XBRL
    - Stakeholder feedback
  - Investor focus
    - Feedback on cost-benefit analysis
    - Academic research
- Similar feedback will be obtained related to private companies and NFPs following their ASC 606 implementation date
- Stage 3 report issued in 4th quarter of 2024: https://www.fasb.org/news-and-meetings/in-the-news/fasb-issues-post-implementation-review-report-for-its-revenue-recognition-standard-420135

Who were the Stakeholders the FASB used?

The FASB used a multi-faceted approach to gather feedback. The conducted individual interviews and hosted group discussions. They organized advisory group meetings, public roundtables, and stakeholder surveys. They delivered webcasts and participated in conferences. And they solicited and reviewed comment letters in response to exposure drafts

- Investors: Including buy-side and sell-side analysts, accounting analysts, credit rating agency professionals, lenders, and private equity firms
- Preparers: Public and private companies, as well as not-for-profit entities, across a wide spectrum of industries and sizes
- Practitioners: Representatives from audit and consulting firms at the international, national, and regional levels
- Other stakeholders: Academics, state CPA societies, trade organizations, regulators, and other standard setters

Achievements of ASC 606 per the PIR process

Developed a unified, principles-based revenue recognition model that applies broadly across all industries and transactions

Introduced comprehensive disclosure requirements, improving investor insight through enhanced revenue disaggregation and qualitative descriptions

Achieved global convergence by aligning U.S. GAAP with IFRS 15, reducing inconsistencies for multinational organizations

Impact on Stakeholders

Most entities experienced minimal impact on the dollar amount of reported revenues but faced significant efforts to revise internal processes and controls. The FASB believes extensive implementation support was crucial and included TRG meetings, ASUs for clarification, and detailed Q&As

All entities, regardless of the impact on revenue figures, undertook comprehensive reviews of contracts and revenue recognition practices. These reviews and improvements did lead to challenges

Although overall feedback on ASC 606 was positive, stakeholders identified several areas that posed difficulties due to the increased need for professional judgment and adaptation to new principles

Summary of key areas of ASC 606 that still present challenges

1. Licensing of intellectual property: Determining the timing of revenue recognition and whether licenses are distinct
2. Identification of performance obligations: Assessing whether promises in a contract are distinct and separable
3. Standalone selling price determination: Estimating prices when not directly observable
4. Variable consideration constraint: Estimating and constraining revenue based on expected outcomes
5. Sales/usage-based royalties: Recognizing revenue tied to customer sales or usage metrics

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Summary of key areas of ASC 606 that still present challenges

6. Principal vs. agent assessments: Determining control and gross vs. net presentation

7. Consideration payable to a customer: Accounting for payments made to customers or third parties

8. Incremental costs of obtaining a contract: Capitalization and amortization of contract-related costs

9. Short-cycle manufacturing revenue recognition: Recognizing revenue over time for customized, short-cycle products

10. Disclosures: Meeting the expanded requirements effectively and efficiently

Cost/Benefit Analysis

A key goal of the PIR process is to evaluate implementation and compliance costs relative to the benefits accrued from the standard. The FASB completed this step and identified four key benefits that arose as a result of the standard's implementation

1. Investors gained deeper insights into contract structures and revenue recognition policies

2. Investors further benefited from enhanced comparability across entities, industries, and global markets, fostering better investment decisions. In short, the income statement has become more comparable

3. Preparers benefited from improved contract analysis and strengthened internal controls over revenue processes

4. Global convergence of standards simplified reporting for multinational entities and reduced discrepancies between GAAP and IFRS, making statements across localities more comparable

Cost/Benefit Analysis

- Costs
  1. Preparers identified significant implementation costs for system upgrades, staff training, and process changes, especially where industry-specific guidance was eliminated
  2. Investors faced initial learning costs, including model updates and analysis changes, though these were generally one-time costs
  3. Many preparers and practitioners identified ongoing costs related to estimating variable consideration, enhanced disclosures, and maintaining robust controls
- Despite these costs, “overall, stakeholders agreed that the benefits of the revenue standard outweigh its costs, especially from a long-term perspective”

Lessons Learned from the PIR

- The need for realistic effective date planning, factoring in implementation complexity and stakeholder readiness
- Importance of proactively identifying cross-cutting issues, especially those affecting multiple areas of GAAP
- Recognition that early-stage TRGs could enhance guidance clarity and reduce post-issuance amendments
- While global convergence is beneficial, it introduces added time, cost, and complexity that must be weighed carefully

What's next for Revenue Recognition under ASC 606?

- There is no immediate need for standard setting changes – ASC 606 is operational and broadly effective. **"The staff has not identified any matters that warrant immediate standard-setting action on Topic 606"**

- FASB determined that ASC 606 met its core objectives: delivering a robust, consistent, and principles-based revenue recognition framework. The cost-benefit relationship aligned with initial expectations, with long-term benefits justifying the implementation effort

- Going forward, FASB will maintain ongoing support via the Technical Inquiry Service to address emerging questions. The Board will monitor practice developments and consider future agenda items based on evolving needs. Insights from the PIR will be incorporated into the development of future standards and implementation support strategies

Lease Accounting and Credit Losses – The Post Implementation Phase has begun.

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Update on SSARS Engagements

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The ARSC is a senior committee of the AICPA with 7 members designated by Council to issue pronouncements in connection with unaudited financial statements or other unaudited financial information of a nonpublic entity

4 – Major Firm Group (Top 100)

2 – Top 100-400 Firms

1 – Small Practitioners

0 – Big Four firms

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Learning objectives

- Distinguish among the nature and elements of reviews, compilations, and preparation engagements of financial statements.
- Revisit key provisions in SSARS No. 25, *Materiality in a Review of Financial Statements and Adverse Conclusions*.
- Look at the most recently issued SSARS No. 26, *Quality Management for an Engagement Conducted in Accordance with Statements on Standards for Accounting and Review Engagements* and SSARS No. 27, *Applicability of AR-C Section 70 to Financial Statements Prepared as Part of a Consulting Services Engagement.*

What Types of Engagements are Covered Under the SSARS?

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Financial statement engagements under the SSARS

	Preparation	Compilation	Review
Level of assurance	None	None	Limited
Understand internal control	Not required	Not required	Not required
Assess fraud risk	Not required	Not required	Not required
Test to obtain evidence	None	None	Inquiry, analytical procedures, management representation letter.
Could be performed	After 2015	After 1978	After 1978

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Preparation engagement

- Provides no assurance
- Does not require the accountant to understand internal controls
- Does not require tests to obtain evidence
- Does not require a written report

Preparation engagement

- Purpose: To prepare financial statements in accordance with an applicable financial reporting framework.
- Required when an accountant is <u>engaged</u> to prepare financial statements, including a single statement, supplementary information, or pro forma information.

- When does AR-C section 70 apply? https://www.aicpa-cima.com/resources/download/is-ar-c-section-70-applicable-yes-or-no

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Preparation standards

- Nonattest service
- Independence does not have to be considered.
- No report is required.
  - —Opinion is not issued.
  - —Legend noting no assurance is provided on each page of the financial statements.
  - —If no legend is provided on the financial statements, accountant must either issue a disclaimer, perform a compilation in accordance with AR-C Section 80 or withdraw from the engagement.

Performance requirements — preparation

- Agree upon the terms of the engagement with the client
- Obtain an understanding of the financial reporting framework and significant accounting policies
  - —Sufficient to complete the engagement
  - —Gained through inquiry, experience, and consulting relevant guidance
- Prepare the financial statements
  - —Statement of no assurance

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Documentation for preparation engagements

Required

- Engagement letter (signed)
- Financial statements

Recommended

- Client acceptance form
- Disclosure checklist

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Defining a compilation engagement

- Definition
  - —Apply accounting and financial reporting expertise to assist management in the presentation of financial statements
  - —Report on the financial statements without undertaking to obtain or provide any assurance
- Required when an accountant is engaged to perform a compilation
  - —Significant change from previous standards
  - —New preparation engagement

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Compilation — Performance standards

•Standards

—Establish an understanding with the client.

-The engagement letter should be in writing and signed by both parties.

—Have appropriate knowledge and understanding of the entity's financial reporting framework.

—Read the financial statements.

—Obtain additional information if information is incorrect, incomplete, or otherwise satisfactory.

-Bring to management.

-Request additional or revised information.

Documentation for compilation engagements

Purpose

- Compliance with SSARSs & SQCSs
- May vary by client

Required

- Engagement letter (signed)
- Financial statements
- Accountant’s report

Recommended

- Client acceptance form (knowledge and understanding of the client)
- Work program (outlines the engagement)
- Bridging documents (captures difference between client’s records and compiled statements)
- Disclosure checklist
- Other support

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The Objective of a Review

- The objective of a review is to obtain limited assurance **primarily by performing analytical procedures and inquiries,** as a basis for reporting whether the accountant is aware of any material modifications that should be made to the financial statements for them to be in conformity with the applicable financial reporting framework (i.e. U.S. GAAP, cash-basis, tax-basis).
- Accountant accumulates review evidence to obtain a limited level of assurance
- It is an assurance engagement

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Review of Financial Statements

- AR-C section 90 applies to all reviews of historical financial information – excluding:
  - Interim financial information (which is covered by AU-C section 930)
  - Pro-forma financial information (which is covered by AT-C section 310)

Review Performance Procedures

- New SSARS 25 performance requirements:
- The accountant is required to plan and perform the review with professional skepticism, recognizing that circumstances may exist that cause the financial statements to be materially misstated.

Review Performance Procedures

- New SSARS 25 performance requirements:
  - Explicit requirement to determine materiality and apply this materiality in designing the procedures and evaluating the results obtained from those procedures.
    - Also required, in obtaining sufficient appropriate review evidence as a basis for a conclusion on the financial statements as a whole, to design and perform the analytical procedures and inquiries to address **all material items in the financial statements, including disclosures**.

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Review Performance Procedures

- Review procedures are tailored based on the accountant’s:
  - Understanding of the industry
  - Knowledge of the client
  - Awareness of the risk of that the or she may unknowingly fail to modify the accountant’s review report on financial statements that are materially misstated

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Review Performance Procedures

- The accountant performs primarily analytical procedures and inquiries to obtain sufficient appropriate review evidence as the basis for a conclusion on the financial statements as a whole.
- In obtaining sufficient appropriate review evidence as the basis for a conclusion no the financial statements as a whole, the accountant is required to design and perform the analytical procedures and inquiries to address the following
  - <u>All material items in the financial statements, including disclosures</u>
  - Areas in the financial statements where the accountant believes there are increased risks of material misstatements

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Review Performance Procedures

- If the accountant becomes aware of a matter that causes the accountant to believe the financial statements may be materially misstated, *the accountant designs and performs additional procedures, as the accountant considers necessary in the circumstances, to be able to conclude on the financial statements.*

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Review Performance Procedures

- SSARS 25 included new required inquiries about:
  - Material commitments, contractual obligations, or contingencies that have affected or may affect the entity’s financial statements, including disclosures
  - Material nonmonetary transactions or transactions for no consideration in the financial reporting period under consideration

SSARS 25 – Reporting options

- Prior to the issuance of SSARS 25, the accountant was prohibited from modifying the standard report to include a statement that the financial statements are not in accordance with the applicable financial reporting framework (that is, an adverse conclusion).
- ISRE 2400 (Revised) provides for the issuance of an adverse conclusion.

SSARS 25 – New reporting option

- ARSC concluded that it was not in the public interest to prohibit the expression of an adverse conclusion when the accountant is aware that the financial statements are materially and pervasively misstated.
- Although the accountant may withdraw from the engagement, users of the financial statements may not then be made aware of such misstatements.
- Accountant is not precluded from withdrawing.
- SSARS 25 includes and illustrative accountant's review report including an adverse conclusion.

Modified Conclusions in a Review Engagement

- Qualified Conclusion
  - Appropriate when misstatements are ***material, but not pervasive***
  - Modify the conclusion paragraph heading with the word “qualified”
  - Include a separate paragraph describing the reason for the modification, immediately before the conclusion paragraph

- Adverse Conclusion
  - Appropriate when misstatements are ***both material and pervasive***
  - Modify the conclusion paragraph heading with the word “adverse”
  - Include a separate paragraph describing the reason for the modification, immediately before the conclusion paragraph

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Insufficient Review Evidence

This situation is rarely encountered

- Client refusal to respond to inquiries
- Client refusal to sign representation letter
- Insufficient data to perform analytical procedures

Accountant must withdraw from the engagement (AR-C 90.45)

- No "disclaimer" report allowed

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SSARS 25 – New reporting requirements

- If substantial doubt about the entity's ability to continue as a going concern exists, include a separate section headed "Substantial Doubt About the Entity's Ability to Continue as a Going Concern"
  - Replaces required EOM but wording is similar
  - Consistent with SAS 134
  - No new performance requirements

Required documentation

Purpose:

- Compliance with SSARSs/SQCSs
- May vary by client
- Minimizes liability

Required:

- Signed engagement letter
- Communications with management and other accountants
- Reviewed financial statements and accountant's report
- Analytical and inquiry procedures
- Additional procedure performed in response to unexpected findings
- Any significant findings or issues
- Significant unusual matters
- Management representation letter
- Materiality (at least I think)

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New SSARS No. 26, *Quality Management for an Engagement Conducted in Accordance with Statements on Standards for Accounting and Review Services*

- Background

— Part of a suite of other new standards issued by the AICPA to enhance firm systems of quality management.

–New Statements on Quality Management Standards

–New SAS — Quality Management Auditing Standards

— Aligns SSARS with new quality management standards

- Effective date

— Periods beginning on or after December 15, 2025

–Except: AR-C section 90 change related to engagement letters effective immediately

Key provisions of SSARS No. 26 on quality management

- Includes revisions to AR-C Section 60
  - Clarify and emphasize engagement partner's responsibility to determine that members of the engagement team have appropriate competence and capabilities.
  - Add explicit guidance for the engagement partner to determine that sufficient and appropriate resources to perform the engagement are made available to the engagement team.
  - Modify guidance that the system of quality management includes establishing a monitoring and remediation process.
- Includes revisions to AR-C Section 90
  - Removes requirement that engagement letter be obtained prior to beginning the engagement

SSARS No. 27 , Applicability of AR-C Section 70 to Financial Statements Prepared as Part of a Consulting Services Engagement

- Amends AR-C Section 70 to:
  - **Explicitly exclude financial statements prepared as part of a consulting services engagement performed in accordance with CS section 100, *Consulting Services: Definitions and Standards,* in AICPA *Professional Standards* from those engagements in which AR-C section 70 is required to be applied**.
  - Address misunderstanding as to the required application of AR-C section 70. The scope paragraphs of the section are amended to <u>clarify that the accountant is not required to apply the section, but application is not precluded, in whole or in part, when an accountant prepares financials statements or prospective financial information as part of consulting services engagement performed in accordance with CS section 100 in which the preparation of financial statements is not the primary objective of the engagement</u>.
- Effective for preparation of financial statements for periods ending on or after December 15, 2026. Early implementation is permitted.

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AICPA CS Section 100 – Consulting Services

- Definition of Consulting Services:
  - Very broad, encompassing various activities like consultations, advisory, support, etc.
- General Standards:
  - It emphasizes the importance of professional competence, due professional care, planning and supervision, and sufficient relevant data
- Understanding with the Client:
  - Crucial to establish a written or oral understanding with the client regarding the nature, timing, scope, and limitations of the services to be performed.
- Reporting:
  - Emphasizes the need for clear communications of findings to clients

In essence, CS 100 provides a framework for CPAs to deliver consulting services while adhering to ethical and professional standards. (Effective date 1.1.1992)

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Issues to Consider under CS 100 – Consulting Services

- Will your firm use engagement letters?
- How will you disclose framework departures
  - It all starts with the Code – Due professional care under 1.300
- Internal checklists to ensure financial statements are in accordance with the selected Financial Reporting Framework
  - GAAP
  - Income Tax
  - Cash or modified cash
- Will you restrict the use of the financial statements – “Management Use Only”
- **These will not be subjected to peer review (at least not now).**

Practice issues for Engagements Under the SSARS and Some Guidance on Analytical Procedures

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Common practice issues – Going concern

- Accounting principles generally accepted in the United States require management to perform evaluation of going concern and consider need for disclosure
  - Management may not have performed evaluation or provided adequate disclosure
  - CPAs who prepare financial statements need to be aware of accounting standards requirements
- Considerations
  - If disclosures are inadequate, the accountant is required to consider whether the modification of the standard report is adequate to disclose the departure from the applicable financial reporting framework.
  - The accountant is not required to include an emphasis-of-matter paragraph in the accountant's review report if the financial statements appropriately disclose uncertainty about the entity's ability to continue as a going concern.
  - However, the accountant may consider it necessary to draw users' attention to the issue.

Documentation of independence considerations

Two basic risks of independence:

- Risk that the practitioner is not independent (independence in mind); and
- Risk that the practitioner is perceived as not being independent (independence in appearance)

Practitioners should use a conceptual framework which involves:

- Identifying threats to independence
- Evaluating the threat that the AICPA member would not be independent or would be perceived by a reasonable and informed third party as not being independent
- Threats must be eliminated or reduced to an acceptable level to be independent

Documentation of independence considerations

Threats to independence:

- Adverse interest threat;
- Advocacy threat;
- **Familiarity threat**;
- **Management participation threat;**
- Self-interest threat;
- **Self-review threat;** and
- Undue influence threat

Nonattest service rules apply during the period of professional engagement and during the period covered by the financial statements

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Documentation of independence considerations

- Independence Conceptual Framework

Is the nonattest service(s) specifically mentioned in ET Sec. 1.295?

No → Evaluate the nonattest service using the conceptual framework at ET Sec. 1.210.010.

Does the nonattest service(s) specifically impair independence?

Yes → Service may not be performed for attest client.

Are there threats that would need supplemental safeguards to bring them to an acceptable level?

Yes → Evaluate firm safeguards and apply them. Document the safeguards and how they were applied.

→ Firm is independent if management is willing and able to provide a person with suitable skill, knowledge and experience to review and take responsibility for the service. Ensure that this documentation is thorough and that the important engagement letter and rep letter provisions are included.

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Safeguards

Safeguards that could applied by the firm are:

- Firm leadership that stresses the importance of independence
- Policies and procedures that are designed to implement and monitor quality control in attest engagements
- Documented independence policies
- Internal policies and procedures that are designed to monitor compliance
- Use of different partners, partner equivalents, and engagement teams that have separate reporting lines
- Training timely communication of a firm’s policies and procedures, and any changes to them

Review Engagements: Analytical Procedures Are Not Properly Performed

Peer reviewers have noted that accountants are not:

- Properly documenting the development of expectations of recorded amounts or ratios;
- Evaluating whether the expectation is sufficiently precise to provide the accountant with limited assurance that a misstatement will be identified that, either individually or when aggregated with other misstatements, may cause the financial statements to be materially misstated; and
- Properly documenting the comparison of recorded amounts or ratios developed from recorded amounts to expectations developed by the accountant through identifying and using relationships that are reasonably expected to exist, based on the accountant's understanding of the entity and the industry in which the entity operates

New practice aid on analytical procedures in a review engagement

- Section 90 requires the use of analytical procedures in a review engagement

  -Analytical procedures are defined as

  > *"evaluations of financial information through analysis of plausible relationships among both financial and nonfinancial data. Analytical procedures also encompass such investigation, as is necessary, of identified fluctuations or relationships that are inconsistent with other relevant information or that differ from expected values by a significant amount."*

New practice aid on analytical procedures in a review engagement (continued)

- Two important components

— <u>Development of an expectation</u>

–Expectation is a prediction of the recorded accounts or ratios

–Used to compare expected amount or ratio to what is recorded – difference may be a misstatement

— Considering the precision of the expectation

–Closeness to the correct amount (which is not necessarily the recorded amount)

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New practice aid on analytical procedures in a review engagement (continued)

- Four steps to performing an analytical procedure
  1. Form an expectation
  2. Compare accountant's expected value with the recorded value and considers the unexpected difference
  3. Inquire of management regarding the difference if the amount exceeds the acceptable threshold
  4. Evaluate the difference between the expected value and the recorded amount and consider implications for the accountant's review report.

New practice aid on analytical procedures in a review engagement (continued)

Four types of methods to develop an expectation

1. **Trend analysis.** This is the analysis of changes in an account balance over time.
2. **Ratio analysis.** This is the comparison of relationships between financial statement accounts (between two periods or over time), the comparison of an account with nonfinancial data (such as revenue per order or sales per square foot), or the comparison of relationships between entities in an industry (for example, gross-profit comparisons).
3. **Reasonableness testing.** This is the analysis of account balances or changes in account balances within an accounting period that involves the development of an expectation based on financial data or nonfinancial data, or both.
4. **Regression analysis.** Regression analysis is the use of statistical models to quantify the accountant's expectation in dollar terms, with measurable risk and precision. In many cases, the entity has developed analytical procedures or internal models, or both, that it uses to monitor and evaluate its business and performance.

Quality Management

The ASB is a senior committee of the AICPA with 19 members designated by Council to issue auditing, attestation, and quality control standards and practical guidance

5 - Public members and users (CFO, Academia, Government)

5 – Local, Regional, National & Global firms

5 – Individuals representing State Regulators

4 – Big Four firms

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Statements on Quality Management Standards

- Statement on Quality Management Standards (SQMS) 1, *A Firm's System of Quality Management*
- SQMS 2, *Engagement Quality Reviews* (New!)
- SAS No. 146, *Quality Management for Engagements Performed in Accordance with Generally Accepted Auditing Standards*
- Related conforming amendments (SSAE No. 23, SSARS No. 26)

Affects every firm that performs engagements in accordance with SASs, SSAEs or SSARS.

SQMS 1 (supersedes SQCS 8)

SQMS 2 (new)

AU-C 220 (Revised)

Conforming amendments: SSAE No. 23, SSARS No. 26, SQMS 3

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Setting the Stage – Overall Objective of QM Standards

Establish the quality related requirements for firm accounting and auditing practices

Enable the AICPA to communicate objectives and expectations regarding quality

Adherence is:

- Required through adherence to the Code of Professional Conduct
- Evaluated through peer review, firm monitoring and evaluation, and the performance of engagement quality reviews (as applicable)

The stated objective in the new QM standards explains (consistent with QC standards):

- Design, implement, and operate a system of quality management for engagements performed by the firm in its A&A practice that provides the firm with reasonable assurance that:
  - a) The firm and its personnel fulfill their responsibilities in accordance with professional standards and applicable legal and regulatory requirements and conduct engagements in accordance with such standards and requirements, and
  - b) Engagement reports issued by the firm are appropriate in the circumstances.

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Key Changes

1. New risk-based approach focused on quality management tailored to the firm's circumstances
2. Revised components of the system of quality management, including information and communication
3. More robust leadership and governance requirements
4. Enhanced monitoring and remediation process
5. New! Requirements for networks and service providers

The five key changes clarify and improve existing quality management processes

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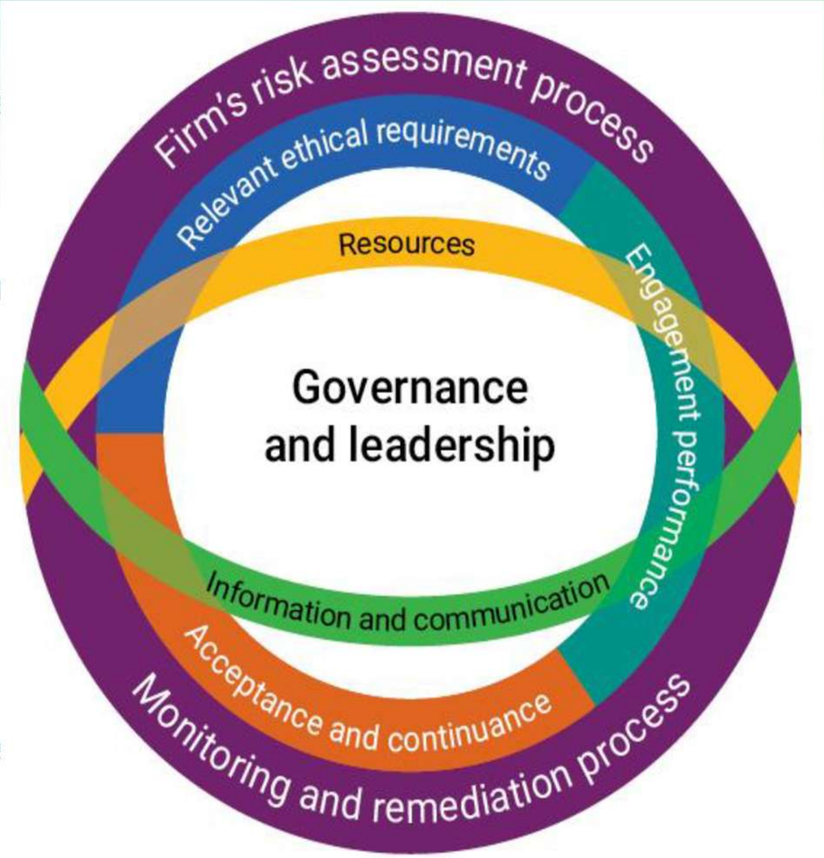
SQMS No. 1: The system and its components

- New focus on quality management, through risk-base
  approach
- Evolved from a linear and soloed system, to a system
  that operated in an iterative and integrated manner
- Proactive approach, with a continual flow of
  remediation and improvement
- Tailored system, scalable to the nature and
  circumstances of the firm and the engagements it pe



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Overview of effective dates

Standard	Full title	Effective date
SQMS No. 1	*A Firm's System of Quality Management*	**December 15, 2025** (system designed and implemented by this date; evaluation of the system required within one year)
SQMS No. 2	*Engagement Quality Reviews*	**December 15, 2025**
SQMS No. 3	*Amendments to QM Sections 10,* A Firm's System of Quality Management, *and 20,* Engagement Quality Reviews	**December 15, 2025**
SAS No. 146	*Quality Management for an Engagement Conducted in Accordance With Generally Accepted Auditing Standards*	**Audits for periods beginning on or after December 15, 2025**
SSAE No. 23	*Amendments to the Attestation Standards for Consistency With the Issuance of AICPA Standards on Quality Management*	**Attestation engagements beginning on or after December 15, 2025**
SSARS No. 26	*Quality Management for an Engagement Conducted in Accordance With Statements on Standards for Accounting and Review Services*	**Engagements beginning on or after December 15, 2025**

General requirements of establishing the firm's system of quality management

- By December 15, 2025, firms should have complied with the requirement of SQMS No. 1 unless the requirement is not relevant, including:
  - The assignment of responsibilities for the firm's system of quality management
  - The identification of quality objectives and related quality risks
  - The design and implementation of appropriate quality responses to identified risks
  - The establishment of a monitoring and remediation process

Implementation is not the end

- Proactive and continual improvement of engagement quality and the system of quality management is critical. The system will respond to changes in risks and adapt.
- Additional requirements of SQMS No. 1 include, but are not limited to:
  - Engagement performance and professional staff responsibilities
  - Monitoring of the system and remediation activities
  - Annual, or periodic, evaluations
  - Engagement quality reviews

Post-December 15, 2025, the question is not whether the firm *has* a system of quality management.

The question is whether the system is operating effectively through engagement performance.

General engagement performance responsibilities

- **Quality is *executed* at the engagement level**
  - Quality objectives and responses are established at the firm level
  - Quality is *realized* when engagement teams apply responses in the context of a specific engagement

- **Professional staff is the first line of defense**
  - First line of defense in identifying and responding to quality issues
  - Quality management happens during the engagement through awareness and action

- **Engagement partners retain overall responsibility**
  - Quality is executed by the engagement team
  - Engagement partners retain responsibility for engagement performance and compliance with professional standards

General professional staff responsibilities

- **Perform procedures in accordance with firm methodology**
  - Includes required steps, templates, tools, and consultation thresholds
- **Document work performed and professional judgment**
  - Documentation remains a foundational responsibility
  - It demonstrates that engagement-level execution aligns with firm-level quality responses
- **Escalate issues timely**
  - Escalation not an admission of error
  - It is a control within the system
  - Know when to pause, consult, and involve the appropriate level of supervision

Wrapping up engagement performance and professional staff responsibilities

Keep in mind:

- Quality is executed at the engagement level
- Firm methodology provides the framework; judgment provides the substance
- Professional staff are the first line of defense
- Clear documentation supports quality and monitoring
- Timely escalation protects engagement outcomes

Defining the terms: monitoring and remediation

Monitoring is an activity designed to

- provide relevant, reliable, and timely information about the design, implementation, and operation of the system of quality management.

Remediation is a process that will

- take appropriate actions to respond to identified deficiencies such that deficiencies are remediated on a timely basis.

Think of monitoring and remediation as the firm's quality feedback loop.
When monitoring identifies issues, remediation is how we correct them, not only on a single engagement, but at the system level.

Monitoring is more than inspection

Ongoing awareness	Targeted procedures	Evaluation
May include • supervision • review • coaching notes • consultations • independence confirmations Day-to-day operation of the firm's methodology	May include • engagement inspections • pre-issuance reviews • post-issuance reviews • thematic reviews • testing of specific responses, like acceptance and continuance steps, independence compliance, or the use of required templates Planned activities designed to evaluate whether responses are operating	Includes • evaluating findings to determine whether deficiencies exist • assessing severity and pervasiveness • identifying root cause(s) Assessment and consideration of why

Roles and accountability

The entire organization plays a critical role in the monitoring process:

- Firm assigns responsibility for monitoring and remediation
- Leadership is accountable for system effectiveness
- Engagement partners retain engagement responsibility
- Professional staff provide primary monitoring inputs

Key point

Monitoring is not something that happens to an engagement team. Monitoring is something the system uses to learn from engagement execution.

What is subject to monitoring activities?

Monitoring activities should be structured to provide information about whether the system is designed appropriately and operating effectively.

Monitoring may examine:

- Engagement performance and compliance with standards
- Application of firm methodology
- Firm-level quality responses
- Recurring issues and trends identified during the year

Monitoring should not be random.
It should connect to the firm's quality risks and responses.

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Example monitoring procedures

- Engagement inspections or file reviews
  - Sample of engagements selected and reviewed against professional standards
  - Sample of engagements selected and reviewed against firm methodology
- Thematic or targeted reviews

Appropriateness of

- Risk assessment documentation
- Use of specialists
- Engagement supervision and review evidence
- Going concern
- Estimates
- How the engagement team documented professional judgment in complex areas

Example monitoring procedures (continued)

- Testing firm-level responses
  - Independence confirmations
  - Training completion
  - Methodology updates
  - Technology access controls
  - Vendor oversight
- Analysis of issues, consultations, and complaints
  - Complaints and allegations
  - Internal consultation trends
  - Recurring review notes
  - Engagement overruns caused by rework
  - Late-stage reporting changes

Monitoring output

Monitoring procedures → Findings → Evaluation

A monitoring activity produces findings.

A finding is an observation.

The firm evaluates and determines whether findings indicate a deficiency in the system of quality management.

Evaluation of findings

The firm accumulates findings from

- the performance of monitoring activities,
- external inspections, and
- other relevant sources.

The firm then exercises **professional judgment** in determining whether findings, **individually or in combination with other findings**, give rise to a deficiency in the system of quality management.

Note that the results of monitoring activities, results of external inspections, and other relevant information may reveal information about the **effectiveness of the monitoring and remediation process itself**.

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Evaluation of findings (continued)

When evaluating, the firm considers **severity** and **pervasiveness**.

Severity asks

- How serious is this?
- Does it create a meaningful risk that engagements are not performed in accordance with professional standards or that reports may be inappropriate?

Pervasiveness asks

- Is this isolated?
- Does it appear across multiple engagements, offices, engagement teams, or service lines?

Results of the evaluation

The evaluation of a finding may result in the firm identifying a **deficiency** in their system of quality management.

A **deficiency** exists when:

- a quality objective required to achieve the objective of the system of quality management is not established;
- a quality risk, or combination of quality risks, is not identified or properly assessed;
- a response, or combination of responses, does not reduce to an acceptably low level the likelihood of a related quality risk occurring because the responses are not properly designed, implemented, or operating effectively; or
- another aspect of the system of quality management is absent, or not properly designed, implemented, or operating effectively, such that a requirement of this section has not been addressed.

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Example deficiencies

A deficiency is rarely defined by one mistake.

Example deficiencies may include:

- Engagement teams **consistently** omit required risk assessment steps in accordance with firm methodology for audits of smaller entities.
- Professional judgment is not documented at a level sufficient to support conclusions in complex or judgmental areas on multiple engagements.
- Evidence of timely supervision and review is inconsistent **across engagements and engagement teams**.
- Acceptance and continuance procedures do not adequately identify engagement-specific risks before work begins.

A deficiency is rarely defined by one mistake.

Evaluating deficiencies — Root cause analysis

A root cause analysis is:

- A structured evaluation of why a deficiency occurred
- Focused on system design and operation
- Forward-looking, with the goal of preventing recurrence
- An essential bridge between identifying deficiencies and designing remediation

A root cause analysis is not:

- Identifying who made the error
- Rewriting the finding in different words
- Fixing a single engagement file
- Assuming “staff training” is always the answer

Example root causes and deficiencies

Example deficiencies may include:

- Staff did not understand expectations or training was insufficient.
- Methodology was unclear, overly complex, or not aligned with actual engagement circumstances.
- Supervision and review were not timely or not documented.
- Engagement budgets or timelines created pressure that undermined quality.
- Resources were inadequate, including staffing capacity, subject matter expertise, or technology tools.

Root cause analysis is not about blame. It is about identifying contributing factors that can be addressed.

Responding to deficiencies

After root cause is identified, the firm designs remedial actions that are responsive to the deficiency. Effective remedial actions are specific and measurable.

Examples of remedial actions may include:

- Updating methodology and templates to clarify requirements
- Targeted training focused on recurring issues
- Strengthening supervision checkpoints, including required review milestones
- Revising acceptance and continuance procedures for certain engagement types
- Adjusting staffing models or engagement scheduling
- Increasing consultation requirements for high-risk areas
- Revising how engagement quality reviews are triggered, when applicable

More about remedial actions

The remediation of a deficiency contains several steps.

First, the firm:

- Will **design** remedial action to address identified deficiencies and be responsive to the results of the root cause analysis; and
- Will **implement** the remedial action.

Then, the individual assigned operational responsibility for the monitoring and remediation process:

- Will **evaluate** that design and whether the implemented action properly corrected the identified deficiency or deficiencies.

Communication

The monitoring and remediation process does not work if the results stay within a small group.

SQMS No. 1 expects communication of monitoring results to those responsible for the system, and appropriate internal communication more broadly.

What might communication look like?

- Results communicated to firm leadership
- Themes shared through training and guidance
- Staff informed of expectations and changes

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Documentation

The firm's documentation of its system of quality management will, at a minimum, include the following:

a. The person(s) with ultimate responsibility
b. The person(s) with operational responsibility
c. The quality objectives included in QM section 10 and any additional objectives identified by the firm
d. The quality risks related to the identified quality objectives
e. Responses to identified quality risks
f. How the quality risks are addressed via quality responses
g. Monitoring and remediation activities, including,
    i. the evaluation of any findings
    ii. the evaluation of any identified deficiencies (and their root causes)
    iii. communications about monitoring and remediation
h. Conclusions reached regarding the firm's system of quality management and the basis for those conclusions

Wrapping up monitoring and remediation

Key takeaways:

- Monitoring is a continuous feedback loop, not a periodic inspection exercise
- Findings evaluated to determine whether system-level deficiencies exist
- Root cause analysis links deficiencies to effective, targeted remediation
- Remedial actions implemented and evaluated for effectiveness
- Monitoring feedback strengthens future engagement performance

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Required broad evaluations

SQMS No. 1 requires firms to step back and answer two related but distinct questions:

1. Is our **system of quality management** designed and operating effectively? (*evaluated at least annually*)
2. Are the **individuals** responsible for the system fulfilling their assigned responsibilities effectively? (*evaluated periodically*)

This is not an inspection, **not a peer review substitute**, and not a formality.

The annual evaluation is the firm's formal conclusion about whether it has reasonable assurance that its quality objectives are being achieved.

Annual evaluation of the firm's system of quality management

Purpose	Timing	Inputs
Intended to determine whether, as a whole, the firm's system of quality management provides reasonable assurance that: • The firm and its personnel comply with professional standards and applicable legal and regulatory requirements, and • Engagement reports issued by the firm are appropriate in the circumstances	The evaluation is required to be performed at least annually. The evaluation date is consistent and intentional (For example, aligned with year-end or the end of the firm's monitoring cycle).	The evaluation is based on information from monitoring and remediation, including: • Results of engagement inspections or file reviews • Broad and targeted monitoring • Identified findings and deficiencies • Root cause analyses • Status and effectiveness of remedial actions • Complaints and allegations • Changes in the firm, such as growth, new services, staffing changes, or new standards

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What is the firm evaluating?

The firm evaluates whether:

- Quality objectives remain appropriate
- Quality risks were identified appropriately
- Responses to quality risks were properly designed
- Responses were implemented and operated as intended
- Monitoring and remediation processes functioned effectively

Evaluation conclusions

Possible conclusions of the firm's evaluation of its system of quality management:

The system provides reasonable assurance

This conclusion is reached when the system of quality management **provides** the firm with reasonable assurance that the objectives of the system of quality management are being achieved.

OR

"Except for"

This conclusion is reached when **except for** matters related to identified deficiencies that **have a severe but not pervasive effect** on the design, implementation, and operation of the system of quality management, the system of quality management **provides** the firm with reasonable assurance that the objectives of the system of quality management are being achieved.

The system does not provide reasonable assurance

This conclusion is reached when the system of quality management **does not provide** the firm with reasonable assurance that the objectives of the system of quality management are being achieved.

Key reminders on the annual evaluation of the system

- The annual evaluation is a formal, documented conclusion about whether the system provides reasonable assurance that quality objectives are being achieved.
- The evaluation is based on information accumulated throughout the year, primarily from monitoring and remediation activities.
- Deficiencies are assessed for severity and pervasiveness to determine the appropriate evaluation conclusion, including the "except for" outcome when applicable.
- The evaluation focuses on the effectiveness of the system as a whole, not on individual engagements.

Periodic evaluation of those responsible for the system

Purpose	Who	What
SQMS No. 1 recognizes that even a well-designed system can fail if responsibilities are not performed effectively. This is about **performance of responsibilities**, not personal performance reviews.	The individual(s) with operational responsibility for the system of quality management If applicable: Individuals responsible for specific components, such as monitoring and remediation, ethics and independence, acceptance and continuance, engagement performance, or resources In small firms, this may be one individual. In larger firms, it may be a group.	The evaluation is based on information from monitoring and remediation, including: • Results of engagement inspections or file reviews • Broad and targeted monitoring • Identified findings and deficiencies • Root cause analyses • Status and effectiveness of remedial actions • Complaints and allegations • Changes in the firm, such as growth, new services, staffing changes, or new standards

Conclusion on responsibility evaluation

Key reminders:

- A positive performance evaluation may be rewarded through compensation, promotion, and other incentives that focus on the individual's commitment to quality and reinforce accountability.
- On the other hand, the firm may take corrective actions to address a negative performance evaluation that may affect the firm's achievement of its quality objectives. Corrective actions may include:
  - Changes to role assignments
  - Adjustments to authority or reporting lines
  - Additional training or support
  - Reallocation of responsibilities

If responsible individuals were unable to perform effectively due to structural or resource constraints, the remediation should address the structure, not the individual

Documentation

The firm's documentation of its system of quality management will, at a minimum, include the following:

a. The person(s) with ultimate responsibility

b. The person(s) with operational responsibility

c. The quality objectives included in QM section 10 and any additional objectives identified by the firm

d. The quality risks related to the identified quality objectives

e. Responses to identified quality risks

f. How the quality risks are addressed via quality responses

g. Monitoring and remediation activities, including,

- i. the evaluation of any findings
- ii. the evaluation of any identified deficiencies (and their root causes)
- iii. communications about monitoring and remediation

h. Conclusions reached regarding the firm's system of quality management and the basis for those conclusions

Interplay between required evaluations

These evaluations are related but distinct:

- The firm's system of quality management may be ineffective, even if individuals worked hard, due to poor design.
- Individuals may fail to fulfill responsibilities even if the system is well designed.
- Often, weaknesses in one evaluation inform remediation in the other.

Together, they ensure accountability at both the system level and the governance level.

Wrapping up annual and periodic evaluations

Key takeaways:

- The annual evaluation is a formal, documented conclusion.
- Severity and pervasiveness drive the evaluation outcome.
- The evaluations are based on monitoring and remediation results.
- Evaluations inform accountability and system improvements.

5 things to remember

1. Quality management is now operational and continuous, not a one-time implementation
2. Engagement performance is where the system succeeds or fails
3. Professional staff execution and timely escalation are controls
4. Monitoring and remediation drive improvement, not compliance
5. Annual evaluation confirms whether the system provides reasonable assurance

Let's Talk Ethics and the AICPA Code of Professional Conduct

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Applicability of the code

- **AICPA and state CPA society**
  - Private, voluntary memberships
  - Codes often the same
  - Many are members of both
- **Joint ethics enforcement program**
  - Jointly investigate potential disciplinary matters and arrange for:
    - presentation of cases before the trial board when evidence of violation of an applicable rule of conduct is found, or
    - matter to be settled by a settlement agreement.
- **Range of possible outcomes**

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Role of Professional Judgment and Critical Thinking

- Not always bright line – you will navigate complex issues and uncertainty
- Apply professional judgment
- Think critically
- Appearance of independence
- Conflict of interest
- Conceptual framework

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Key points of professional judgment

- The importance of an inquiring mind
- Openness to the need for further evaluation or action
- Awareness of the effects of conscious or unconscious bias

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Conceptual Framework Approach

- Two frameworks for members in public practice
- One framework for members in business
- A systematic approach for identifying and evaluating threats
- May not override a rule by coming to a different conclusion using the conceptual framework
- Framework is not optional

Steps to Apply the Approach – Identify Threats to Independence (Step 1)

- Adverse interest
- Advocacy
- Familiarity
- Self-interest
- Self-review
- Undue influence
- Management participation

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Evaluate the Significance and Apply Safeguards (steps 2 & 3)

- Not all threats are the same.
- Determine if a threat is acceptable.
- Consider both qualitative and quantitative factors.
- Conclude and communicate.
- Apply safeguards, if required.

Ethical Conflicts

Applies when a member in public practice or in business encounters

- obstacles to following an appropriate course of action due to internal or external pressures or
- conflicts in applying relevant professional and legal standards.

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Ethical Conflicts – cont.

Consider

- relevant facts and circumstances, including applicable rules, laws, or regulations;
- ethical issues involved; and
- established internal procedures.

Consultation and documentation can be critically important.

Independence Rules for CPAs

Overview of Independence rules

- Independence is the cornerstone of public accounting.
- Understanding independence is important for all members. Includes independence of mind and independence in appearance.
- Definitions are not absolutes. All threats are required to be reduced to an acceptable level.

Definitions

- Attest client — A person or entity with respect to which a member performs an attest engagement.
- Attest engagement — An engagement that requires *independence*, as set forth in the AICPA Statements on Auditing Standards (SASs), Statements on Standards for Accounting and Review Services (SSARSs), and Statements on Standards for Attestation Engagements (SSAEs).

Definitions (Continued)

- Attest engagement team — Those individuals participating in the *attest engagement*, including those who perform concurring and engagement quality reviews. The attest engagement team includes all employees and contractors retained by the *firm* who participate in the *attest engagement*, regardless of their functional classification (for example, audit, tax, or management consulting services).

Which Independence Rules Apply?

- AICPA — All AICPA members and others performing audits under generally accepted auditing standards (GAAS) or other attest services
- State Accountancy Boards — All licensees (including via mobility rules) practicing under a state board's jurisdiction
- SEC and PCAOB
  - Public companies filing reports with the SEC
  - SEC registered broker-dealers, hedge funds, investment advisers

Which Independence Rules Apply? (Continued)

- CFTC — Audits of futures commission merchants comply with independence requirements applicable to non-issuer broker-dealer audits
- GAO — Attest services under government auditing standards
- DOL — Audits of employee benefit plans subject to ERISA

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Which Independence Rules Apply? (Continued)

- FDIC or other banking agencies — Policy statements on independence including internal audit, SOX, and indemnification
- NAIC — Model Audit Rule incorporates several aspects of the SEC's independence requirements
- IESBA – Global code that serves as the foundation for member body codes throughout the world
- EC — Audit and independence rules for European Union

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When Is Independence Required?

- Independence in fact and appearance
  - Period of the professional engagement
  - Period covered by the financial statements
- Financial Interests — Independence required during the *professional engagement.*
- Nonattest services, business, and employment relationships — Independence required during the *professional engagement* and *period covered by financial statements.*

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Conceptual Framework For Independence

- Threats and safeguards approach used for independence for many years.
- Identify threats
  - Are threats significant?
  - If significant, could safeguards reduce or eliminate?
  - Threats must be at “acceptable level” or independence is impaired.
- If a rule applies, do not apply conceptual framework, which is intended to address situations where no rule exists.

Nonattest Services

- Advisory services **(be careful here)**
- Appraisal, valuation, or actuarial services
- Benefit plan administration services
- Bookkeeping, payroll, and other disbursement services
- Business risk consulting services
- Corporate finance consulting services
- Executive or employee recruiting services

Nonattest Services (Continued)

- Forensic accounting services
- Hosting services
- Information systems design, installation, or integration services
- Internal audit services
- Investment advisory or management services
- Tax services

General Requirement 1 — Establish Understanding with Client

Independent CPA responsibilities	The client's responsibilities
Establish and document in writing the understanding with the client regarding: • Objectives of the engagement, • Services to be performed, • Member's responsibilities, • Client's acceptance of responsibilities, and • Any limitations of the engagement.	• Accepting responsibility for the services, • Designating an individual, preferably within senior management, who possesses suitable skill, knowledge, or experience to oversee the service, • Evaluating the adequacy and results of the services performed, and • Making management decisions and assuming all management responsibilities.

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General Requirement 2

- Management responsibilities involve leading and directing an entity.
- Examples:
  - Setting policy or strategic direction
  - Directing or accepting responsibility for actions of employees
  - Authorizing, executing, or consummating transactions
  - Preparing source documents
  - Having custody of an attest client's assets
  - Deciding which recommendation of the member to implement
  - Reporting to those charged with governance on behalf of management

General Requirement 3

- Before perform nonattest services, establish and document understanding with client
- Engagement letter or another type of document
- Failure to document does not affect independence but would be considered a compliance issue

Note: Routine activities are NOT nonattest services and do not require compliance with the General Requirements

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General Impairments of Independence

- Authorizing, executing or consummating a transaction, or otherwise exercising authority on behalf of a client or having the authority to do so;
- Preparing source documents, in electronic or other form;
- Having custody of client assets;
- Supervising client employees in their normal recurring activities;
- Determining which 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, general counsel or its equivalent; and
- Establishing, maintaining, or monitoring internal controls.

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Primary Threats to Independence

- **Self-review threat** – Members reviewing as part of an attest engagement evidence that results from their own, or their firm's, nonattest work such as, preparing source documents used to generate the client's financial statements.
- **Advocacy threat** – Actions promoting an attest client's interests or position.
- **Adverse interest threat** – Actions or interests between the member and the client that are in opposition, such as, commencing, or the expressed intention to commence, litigation by either the client or the member against the other.
- **Familiarity threat** – Members having a close or longstanding relationship with an attest client or knowing individuals or entities (including by reputation) who performed nonattest services for the client.
- **Undue influence threat** - Attempts by an attest client's management or other interested parties to coerce the member or exercise excessive influence over the member.
- **Financial self-interest threat** - Potential benefit to a member from a financial interest in, or from some other financial relationship with, an attest client.
- **Management participation threat** - Taking on the role of client management or otherwise performing management functions on behalf of an attest client.

Recent Interpretations

AICPA — New and Revised

- New “Determining Fees for an Attest Engagement” interpretation (ET sec. 1.230.030)
- New “Fee Dependency” interpretation (ET sec. 1.230.040)
- Revised “Conceptual Framework for Independence” interpretation (ET 1.210.010) – Includes a *self-interest threat* (member could benefit, financially or otherwise from an interest or relationship with an attest client or persons associated with the attest client.
- Revised “Client Affiliates” interpretation (ET sec. 1.224.010)
- Unpaid fees – No more “bright line” test of one year or more. 12/31/2022

Updates related to fees

- New “Determining Fees for an Attest Engagement” interpretation (ET sec. 1.230.030)
- New “Fee Dependency” interpretation (ET sec. 1.230.040)
- Revised “Conceptual Framework for Independence” interpretation (ET sec. 1.210.010)
- Revised “Client Affiliâtes” interpretation (ET sec. 1.224.010)

Determining fees for an attest engagement

Key points in the interpretation include:

- The fees to be charged to an attest client, whether for attest or other services, is a business decision
- The determination takes into account the facts and circumstances relevant to that specific engagement
- The provision of other services to an attest client is not an appropriate consideration in determining the attest engagement fee in most circumstances
- The covered member responsible for setting the fee may consider the cost savings achieved as a result of experience derived from providing the other service

The "Fee Dependency" interpretation

Key points in this new interpretation include the following:

- The dependence on and concern about the potential loss of fees from attest and other services from that client affect the level of the self-interest threat and create an undue influence threat to a covered member's independence.

- The total fees of the firm should include fees from attest and nonattest services.

- A covered member might use financial information available from the previous financial year to estimate the proportion of total fees.

- A covered member is not required to include fees from attest and nonattest services of other network firms within the firm's network.

- When the attest client is a financial statement attest client, the covered member should include fees from entities described under item (a) of the definition of *affiliate*.

The “Fee Dependency” interpretation (continued)

Moreover, the interpretation stipulates that one of the following safeguards should be applied to reduce threats to an acceptable level when total fees from an attest client represent or are likely to represent a large proportion of the total fees received by the firm for five consecutive years:

a. Prior to the attest report being issued for the fifth year, an appropriate reviewer who is not a member of the firm issuing the report reviews the fifth year’s attest work.

b. After the attest report on the fifth year has been issued, and before the attest report is issued on the sixth year’s attest engagement, an appropriate reviewer who is not a member of the firm issuing the report reviews the fifth year’s attest work.

AICPA — New Under “Professional Qualifications or Competencies”

Any member who knowingly solicits or discloses Uniform CPA Examination questions or answers without the AICPA’s written authorization has violated the “Acts Discreditable Rule.”

A member will also be considered in violation of the “Acts Discreditable Rule” if the member engages in false, misleading, or deceptive acts related to professional qualifications or competencies, including

- soliciting or knowingly disclosing questions or answers of any continuing professional education (CPE) course examination
- falsifying or misrepresenting attendance at a CPE course, and
- tampering with the administration of or examination grading for any CPE course or credential.

The Professional CPA Creed (how many knew we had one?)

As a professional CPA, I willingly accept my responsibility (1) to serve the public interest; (2) to maintain and broaden public confidence by performing all my responsibilities with integrity; (3) to maintain my objectivity and be free of conflicts of interest, and to discharge all my responsibilities with due care.

Other Guidance, Tools and Aids

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Online Code of Professional Conduct

- Online platform
  - Basic and advanced search capability
  - Pop ups
  - Bookmarks
  - Record notes
  - Hyperlinks
- Revision History
- https://www.aicpa-cima.com/topic/ethics/code-of-professional-conduct

Non-authoritative Tools and Aids

- **Toolkit: Conceptual Framework for Members in Business and Public**
  - Understanding and flowcharts
  - Examples and worksheet
- **FAQs**
  - Frequently asked and general industry questions
- **Ethics Case Study and Questions**
- **Ethics decision tree for members in business and industry**
- **Ethically Speaking podcasts**
- **Call me BMSS 256.964.9826 or e-mail at mbrand@bmss.com**

Audit Standards Update and Workpaper Documentation

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Recently Issued/Effective Statements on Auditing Standards

- Identify the fundamental aspects of the recently issued new SAS No. 149, *Special Considerations – Audits of Group Financial Statements (Including the Work of Component Auditors and Audits of Referred-to Auditors).*
- **ASB is currently reviewing comment letters received on the proposed SAS *External Confirmations* and on *The Auditor's Responsibilities to Fraud in an Audit of Financial Statements.***
- **There are two related attestation standards exposure drafts currently open for public comment (Deadline: June 30, 2026), that together will constitute a comprehensive revision of the attestation standards:**

1. **Proposed SSAE – *Common Concepts, Examination Engagements, Review Engagements, and Engagements to Report on Sustainability Information***
2. ***Proposed SSAE – Amendments to SSAE Nos. 18-169 and 21.***

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SAS No. 149, *Special Considerations — Audits of Group Financial Statements (Including the Work of Component Auditors and Audits of Referred-to Auditors)*

- Background
  - —The ASB's intent is to converge with IAASB, specifically, International Standard on Auditing (ISA) 600, because
  - –the issues that led the IAASB to update its group audit standard are equally present and important in the United States and
  - –it is not feasible for firms that perform engagements following IAASB and ASB standards to comply with fundamentally different standards for group audits.

SAS No. 149 (continued)

- Fundamental aspects of the new standard
  - —Defining group financial statements as including financial information of more than one entity or business unit through a consolidation process
  - —Identifying various ways in which consolidation may occur
  - —Providing guidance on whether and how the SAS applies to entities with branches and divisions, shared service centers, and noncontrolled entities
  - —Clarifying that all AU-C sections need to be applied in a group audit and establishing stronger links to the other AU-C sections
  - —Introducing a risk-based approach to planning and performing a group audit

SAS No. 149 Engagement Partner Responsibilities

- Managing and achieving quality on the group audit engagement
- Reviewing overall audit strategy and audit plan
- Being sufficiently and appropriately involved with the work of the component auditors to determining whether significant judgments made, and the conclusions reached, are appropriate given the nature and circumstances of the group engagement
- Determining whether sufficient appropriate audit evidence can reasonably be obtained, including through involving component auditors to provide a basis for forming an opinion on the financial statements

SAS No. 149 Component Auditor Communications

- Identification of the financial information on which the component auditor has been requested to perform audit procedure
- Whether the component auditor has performed the work requested by the group auditor
- Whether the component auditor has complied with the relevant ethical requirements
- Instances of noncompliance with laws or regulations
- Any corrected or uncorrected misstatements of the component financial information
- Any indicators of possible management bias

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SAS No. 149 Component Auditor Communications (cont.)

- Description of deficiencies in the system of internal control identified
- Any fraud or suspected fraud
- Other significant matters that the component auditor has or expects to communicate to component management or those charged with governance
- Overall findings and conclusions

SAS No. 149 Evaluation of Audit Evidence

- Group auditor evaluates whether sufficient appropriate evidence has been obtained from the audit procedures by
  - -determining whether, and the extent to which, it is necessary to review additional component auditor audit documentation
    - -Nature, timing, and extent of work performed
    - -Competence and capabilities
    - -Direction, supervision, and review of work performed

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Auditor's Report: Referencing the Referred to Auditor

- The new SAS retains the option for the group engagement partner to make reference to the referred-to auditor's report in the group audit report.
- The group engagement partner should take responsibility for ensuring the referred-to auditor is aware of relevant ethical requirements.
- Make reference only when the group engagement partner has determined that the referred-to auditor has performed an audit of the financial statements of the component in accordance with GAAS or PCAOB auditing standards.
- The referred-to auditor's report cannot be restricted as to use.
- The group engagement partner should read the component's financial statements and the referred-to auditor's report

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SAS No. 149 Effective Date

- Group audits for financial statements for periods ending on or after December 15, 2026

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What are Working Papers?

The Importance of Audit Working Papers

- Records
  - What auditor did
  - What auditor found
  - How auditor responded or concluded
- Enables communication among auditors
- Required by professional standards

AU-C Section 230 Requirements

- Provide a clear understanding of
  - Nature, timing, and extent of audit procedures;
  - Results;
  - Evidence obtained and its source; and
  - Conclusions reached.
- Who performed and who reviewed the work, and when
- The reconciliation of accounting records to the financials

Why the Focus on Documentation?

- It’s all we have to ‘evidence’ your work
- It supports your conclusions on a specific risk/assertion/account balance/disclosure etc..
- It supports your opinion or report and the overall audit objectives (obtain reasonable assurance and issue the appropriate report) were met
- It provides evidence that you complied, in all material respects, with GAAS
- It’s a common peer review finding, or a common peer review ‘excuse’

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Why the focus on documentation? (…cont’d)

- Critical to practice monitoring – both internal and external
- Can be hard to distinguish what you “know” (in your head) versus what you’ve actually documented. (I thought I documented that!)
- Face it, some are better at documenting than others – practicing helps, supervising and reviewing helps, review notes help, inspections (internal and external) help, OTJ training helps.
- No documentation? No credit….

What is it?

- The auditor’s record of

- Procedures performed - what I did
- Evidence obtained (including disconfirming evidence) – what I saw
- Conclusions reached – what I thought

What is it? (…cont’d)

- Includes:

- Planning docs, checklists, memos, analyses, detailed tests, sample calculations, analytical procedures, tests of details, excerpts, images, scanned source documents, confirmations, representation letters, correspondence, 3rd party reports, system generated data, videos, tic marks, initials, dates, firm QC documents etc. etc. etc.

- Excludes:

- What you didn’t document
- What is not readily determinable by a knowledgeable third party
- What cannot be inferred from the totality of the documentation
- Oral explanation when the requirements of AU-C 230 have not been met

Straight out of the standard

.08 The auditor should prepare audit documentation that is sufficient to enable an experienced auditor, having no previous connection with the audit, to understand(Ref:par..A4–.A7and.A19–.A20)

- a. the nature, timing, and extent of the audit procedures performed to comply with GAAS and applicable legal and regulatory requirements;(Ref:par..A8–.A9)
- b. the results of the audit procedures performed, and the audit evidence obtained; and
- c. significant findings or issues arising during the audit, the conclusions reached thereon, and significant professional judgments made in reaching those conclusions.(Ref:par..A10–.A13)

Straight out of the standard (…cont’d)

.09 In documenting the nature, timing, and extent of audit procedures performed, the auditor should record

- a. the identifying characteristics of the specific items or matters tested;(Ref:par..A14)
- b. who performed the audit work and the date such work was completed; and
- c. who reviewed the audit work performed and the date and extent of such review.

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What is required?

- Experienced auditor with no connection to the audit should understand:

- The nature, timing and extent of procedures performed
- Results and evidence obtained
- Significant findings, issues and professional judgments

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Nature, timing and extent

- Identifying characteristics of the items tested

- Can the test be reperformed if necessary?

- Who performed and the date of performance
- Who reviewed and the date/extent of review

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Results and conclusions

- Were the results in line with expectations?
- Were anomalies investigated?
- Does another course of action need to be taken?
- Is more testing required?
- Are there deficiencies that should be considered?
- Has materiality been considered?
- Has the materiality benchmark used also been considered?
  - Did you use assets as your benchmark, but then have material

Significant findings, issues and judgments

- Determining what is significant will require an objective analysis
- To what extent is professional judgment required
- Document relevant discussions – what, who and when
- Inconsistencies

- Disconfirming evidence should be documented and how resolved
- Team differences should be documented
- All documentation should be timely – evidence must be obtained, documented with conclusions and reviewed prior to dating/issuing financial statements.

Documentation requirements – lock down

- File lock down within 60 days (GAAS) following the report release date

- Audit evidence should NOT be performed or introduced into the wps during the 60-day time performed

- Largely administrative tasks only

- After 60 days NO DELETIONS

Documentation errors

- Planning brainstorm, RMM and fraud (peer review indicates that more than 10% of firms are not complying, just going through the motions).
- Understanding the entity and internal control
- RMM at financial statement and relevant assertion level
- Significant risks
- Linkage to and responses to risks (connecting judgements about risk with procedures)
- Results/conclusions/level of effort/RMM are not in synch
- Professional skepticism not demonstrated
- Disconfirming evidence thrown out and not addressed
- Source documents not evaluated for completeness or accuracy

Documentation errors (…cont'd)

- Controls are not tested, but CR is less than the maximum (some control testing is really testing of processes, not controls).
- Significant risk identified but design and implementation of controls not evaluated
- Sample sizes have no basis
- Cannot recreate the work based on the evidence documentation
- No linkage to brainstorm, especially fraud
- No test of details when significant risk identified
- No expectations and basis for those expectations for substantive analytics
- Precision/persuasiveness of the expectation not aligned with risk assessment.

Connection to risk assessment

Lower RMM	←-----------------→	higher RMM
Less documentation	←-----------------→	more documentation
Less review	←-----------------→	more review
Less persuasive	←-----------------→	more persuasive
Less precise	←-----------------→	more precise
Fewer items (less coverage)	←-----------------→	more items(more coverage)
Less reliable	←-----------------→	more reliable

Is your risk assessment, evidence and documentation aligned?

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Other Guidance (partial listing only)

- Engagement Letter (AU-C sec. 210)
- Quality control conclusions (AU-C sec. 220)
- Auditor’s consideration of fraud and communication with the entity about any discovered fraud (AU-C sec. 240)
- Identified or suspected noncompliance with laws (AU-C sec. 250)
- Required communications with those charged with governance (AU-C sec. 260)
- Communications related to control weaknesses (AU-C sec 265)
- Overall audit strategy (AU-C sec. 300)

Engagements that Require Working Papers

Service	Applicable Standard
Preparation of Financial Statements	Statements on Standards for Accounting and Review Services (SSARS)
Compilation of Financial Statements	Statements on Standards for Accounting and Review Services (SSARS)
Review of Financial Statements	Statements on Standards for Accounting and Review Services (SSARS)
Attestation Engagements	Statements on Standards for Attestation Engagements (SSAE)
Valuation Services	Statement on Standards for Valuation Services (SSVS)

How “good” is the Evidence – Sufficient (enough) and Appropriate (relevant and reliable)

- Source / type – is 3rd party evidence really more reliable?
- Determining the impact of management bias considering
- The ability of the entity to influence the external information source
- Management’s selection of information from an external source known to be favorably biased toward corroborating management’s assertions or information
- Quantity (this cant overcome a lack of appropriateness)
- Corroborate or contradict
- Precision / susceptibility to bias
- Level of detail - disaggregation

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How “good” is the Evidence – Sufficient (enough) and Appropriate (relevant and reliable) (continued)

- Accuracy / authenticity
- Complete
- Recent
- Previous experience
- Is the evidence persuasive? HOW persuasive is it? Minimal… to … compelling.
- How good does it need to be? What is your RMM?
- MUST REMAIN SKEPTICAL – WHAT DOES THAT MEAN TO YOU?

Nature of Working Papers

- Working papers should be adaptable to needs of engagement.
- Documentation refers to anything enabling the auditor to render an opinion.

-Work programs and checklists

-Confirmations

-Contracts

-BOD minutes

-Memos

-Correspondence (including e-mail)

AICPA Focus Areas and Peer Review Issues Identified

- Top issue identified – **Risk assessment**
- **Documentation** – 25% of engagements subject to review were materially nonconforming due to failure to comply with documentation standards
- **Single Audits** – Remain a significant focus area

Peer Review

Common Areas of Noncompliance — Reviews

Engagement & Reporting

The firm did not do the following:

- Have all the required elements within the engagement letter
- Cover all the periods or the correct periods presented in the financial statements in the accountant's report
- Document expectations or the comparison of expectations to recorded amounts for analytical procedures

Common Areas of Noncompliance — Reviews (continued)

Rep Letters & Materiality

The firm did not do the following:

- Obtain appropriate management representation letters, including:
  - Omitted representations required by the applicable professional standards
  - Inappropriate date
  - Inappropriate financial statement periods
- Update reports in conformity with the applicable professional standards
- Document materiality in accordance with current professional standards

Common Areas of Noncompliance — Compilations

Reports & Engagement Letters

The firm did not do the following:

- Prepare reports in accordance with professional standards
- Obtain appropriate engagement letters, including:
  - Omitted elements required by SSARSs
  - Omitted wording indicating the lack of independence
  - Omitted wording identifying nonattest services provided
  - Not obtaining required signatures

Common Areas of Noncompliance — Preparations

Engagement Letters & Disclosures

The firm did not do the following:

- Obtain an engagement letter for the period covered or include all language required by the applicable professional standards
- Include a statement that indicates that at a minimum, no assurance is provided on the financial statements
- Disclose departures from the financial reporting framework, including the omission of the statement of cash flows

Common Areas of Noncompliance — Documentation

Documentation Requirements

Documentation requirements include:

- Nature, timing, and extent of procedures performed
- Results and evidence obtained
- Significant findings, issues, and professional judgments

- Applies to any procedure that provides audit evidence necessary to support the opinion

Common Areas of Noncompliance — Auditing Standards

Planning & Documentation

The firm did not do the following:

- Appropriately document planning procedures, including:
  - Risk assessment (and linkage of risks to procedures performed)
  - Planning analytics
  - Understanding of IT environment
  - Internal control testing
  - Consideration of going concern

Common Areas of Noncompliance — Auditing Standards (continued)

Risk Assessment

Improperly supporting and documenting the assessed level of risk:

- Setting control risk less than high without proper testing
- Performing risk assessment at audit level rather than at the relevant assertion level
- No documentation of fraud risk regarding inquiries with those charged with governance and response to management override of controls
- No documentation of sources for conclusions on design and implementation of controls, including key controls and walkthroughs
- Did not appropriately identify or address management override and revenue recognition due to fraud

Common Areas of Noncompliance — Auditing Standards (continued)

Rep Letters & Engagement

The firm did not do the following:

- Obtain appropriate management representation letters, including:
  - Update the letter to include all representations required by applicable professional standards
  - Date the letter appropriately
  - Include appropriate financial statement periods

Common Areas of Noncompliance — Auditing Standards (continued)

Policies, Standards & Governance

The firm did not adhere to established policies and procedures:

- Incorrect or insufficient use of third-party practice aids
- Insufficient review of audit documentation
- Lack of compliance with policies related to CPE

The firm also did not do the following:

- Communicate and/or document required communications with those charged with governance
- Properly adopt newer standards regarding revenue recognition and leasing

Common Areas of Noncompliance — Code of Professional Conduct

Independence & Nonattest Services

The firm did not do the following:

- Establish and document in writing the understanding with the client with regard to nonattest services provided
- Address management's responsibilities to oversee and evaluate the results of the services performed
- Identify significant threats to independence, along with the safeguards applied

Common Areas of Noncompliance — Accounting and Reporting

Disclosures & Classification

The firm did not do the following:

- Disclose the date through which subsequent events were evaluated
- Correctly classify long-term debt on the cash flow statement
- Include required disclosures (such as, revenue recognition matters related to ASC 606)

Common Areas of Noncompliance — Accounting and Reporting (continued)

Fair Value & NFP Reporting

- Perform sufficient procedures or sufficiently document the procedures to obtain assurance of the fair value measurements
- Properly classify unrealized gains or losses on investments
- Follow the financial reporting model for not-for-profit financial statements in accordance with requirements of ASU No. 2016-14

Refer to Examples of Matters in Peer Reviews

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Center for Plain English Accounting (CPEA)

Membership Includes:

- Timely written responses to technical inquiries
- Monthly A&A reports — in plain English
- 24 hours of CPE via webcast
- Alerts summarizing new accounting guidance
- Library of over 400 past reports

Common Peer Review MFCs

Matters for Further Consideration

Common MFCs

AICPA Annual Listing

The firm did not do the following:

- Listing prepared annually by AICPA staff based on peer reviews accepted over a 15-month period
- Examples of Matters in Peer Reviews | Resources | AICPA & CIMA
- Most recent report includes engagements performed with balance sheet dates between 03/01/23–6/30/24
- New listing will be updated by end of February 2026
- While list is updated every year, many findings are repeats

CPEA Analysis of Peer Review MFCs — AU-C Related

Top AU-C sections cited in peer review matters for further consideration:

21%	13%	7%	6%
Risk Assessment **AU-C 315**	**Risk Assessment** **AU-C 330**	**Documentation** **AU-C 230**	**Governance** **AU-C 260**
↑ Trending higher	↑ Trending higher		

Source: AICPA CPEA Peer Review Analysis

Example MFC — AU-C 315: Risk Assessment (SAS 145)

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Firm adopted SAS 145 but overlooked assessing RMM the same as inherent risk when control risk is assessed as high. As a result, several instances were noted where RMM was assessed higher than inherent risk.

Key Takeaway: When control risk is assessed at maximum, RMM = inherent risk. Firms must ensure risk assessment tools reflect this SAS 145 requirement.

Example MFC — AU-C 315: Control Risk Documentation

The firm erroneously documented that they were going to test controls, and they did not actually test the controls. On the risk assessment they showed the control risk at less than maximum which was in error since they did not test controls. In all cases they performed enough work to support a high risk of material misstatement.

Key Takeaway: If controls are NOT tested, control risk must be set at maximum. Documentation must match actual procedures performed.

To set control risk < maximum

Requires testing operating effectiveness

Example MFC — AU-C 315: Significant Risk Linkage

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Documentation surrounding risk assessment and responses did not provide a clear linkage between assessed risk and procedures performed. The firm documented several areas as significant risks, but there was no specific response to those risks. The intent was to document significant audit areas, not significant risks. The documentation linkage did not deviate enough to be nonconforming with risk assessment standards.

Key Takeaway: Every significant risk must have a documented, specific response. Audit areas ≠ significant risks under SAS 145.

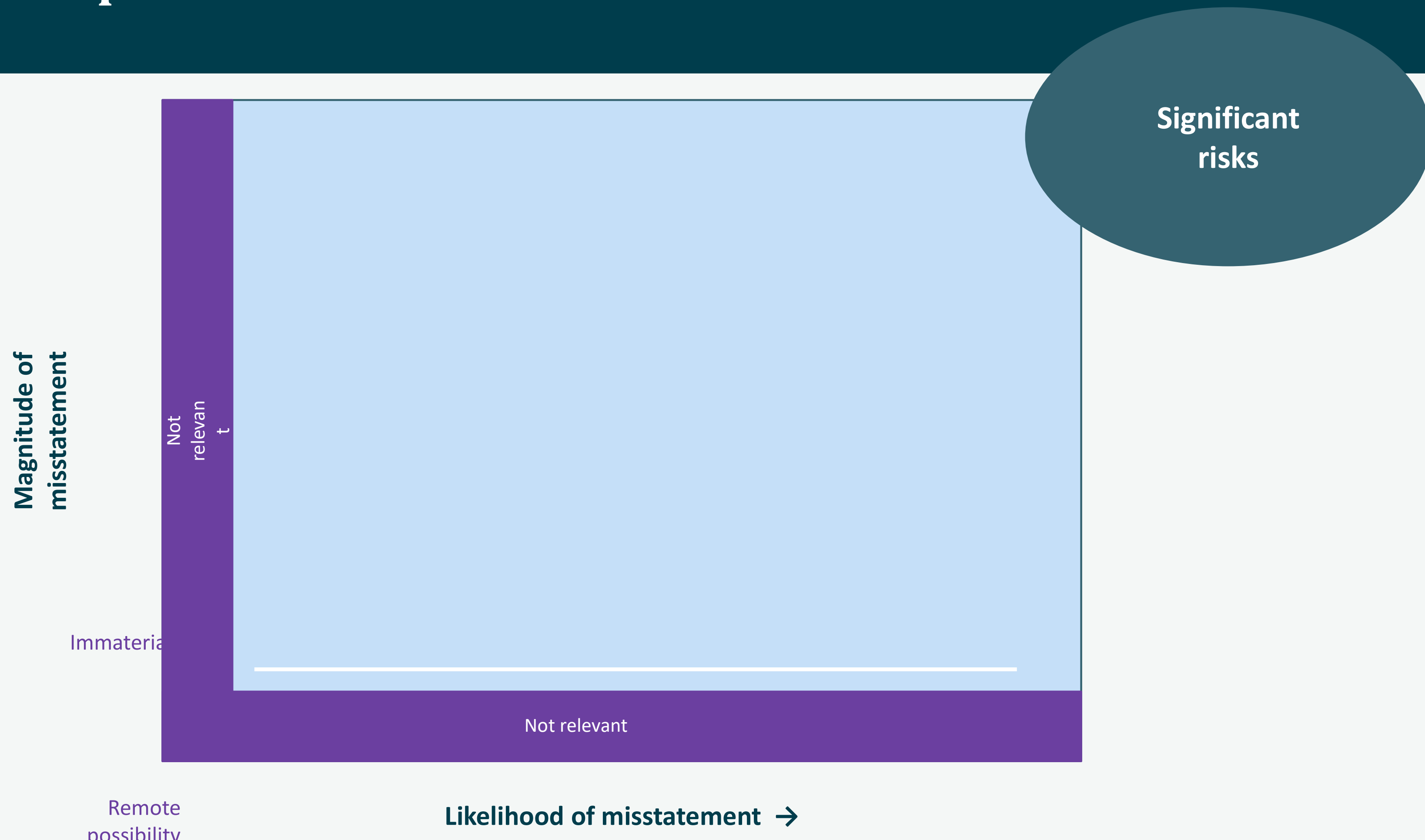
Example MFC — AU-C 315: Inherent Risk Assessment (Nonconforming)

Nonconforming engagement

Risk assessment procedures were not sufficient to ensure compliance with professional standards. Audit areas were noted where significant risks were identified and inherent risk was assessed as low or medium. Expansion of scope was not necessary as firm had similar documentation on other engagements. This engagement is considered nonconforming as a result of this matter.

⚠ Nonconforming: Significant risks require inherent risk assessed near the upper end of the spectrum. Low/medium IR is inconsistent with a significant risk designation.

The Spectrum of Inherent Risk



Adapted from the SAS 145 Introduction Presentation at Engage 2023

Significant Risk — Definition (SAS No. 145)

New Concept Under SAS 145

An identified risk of material misstatement for which the assessment of inherent risk is close to the upper end of the spectrum of inherent risk due to the degree to which inherent risk factors affect the combination of the likelihood of a misstatement occurring and the magnitude of the potential misstatement should that misstatement occur,

— OR —

That is to be treated as a significant risk in accordance with the requirements of other AU-C sections.

Obtained from the SAS 145 Presentation at the 2023 AICPA EBP Conference

Example MFC — AU-C 315: Government Audit (Nonconforming)

Nonconforming engagement

For one government audit engagement, the risk assessment included risks related to specific assertions for debt, proprietary fund revenues, capital assets, expenditures and capital assets. The controls related to the significant risks were not identified and therefore not evaluated for design and implementation. The engagement was considered nonconforming relating to the risk assessment standard.

⚠ Nonconforming: Controls related to significant risks must be identified and evaluated for design and implementation — not just mentioned.

Identified Controls (Relevant to the Audit) — SAS 145

- Evaluating design and determining implementation (D&I) required in following areas within Control Activities component:
  - Significant risks (such as revenue)
  - Controls over journal entries and other adjustments as required by AU-C section 240
  - Controls for which there is a plan to test operating effectiveness (planned control reliance or substantive procedures alone not sufficient)
  - Other controls, based on professional judgment

- Include general IT controls that address risks arising from the use of IT

The phrase "identified controls" replaces "relevant controls" and "controls relevant to the audit."

Some methodologies refer to "key" controls.

Obtained from the SAS 145 Deeper Dive Presentation at Engage 2023

Auditor's Responsibilities for Internal Control

1	Gaining an Understanding of Internal Control	• All significant audit areas (i.e., SCOTABDs)
2	Procedures Over Design and Implementation (D&I)	• Identified controls only • Formally known as relevant controls • Must be more than inquiry
3	Testing Operating Effectiveness	• Areas where control risk (CR) has been assessed below maximum • Reliance on controls planned

Common MFCs — General Audit Issues

Audit Standards

The firm did not do the following:

- Failure to properly adopt new standards regarding revenue recognition and/or the new lease standard
- Failure to include audit documentation that contains sufficient complete evidence to support the firm's opinion on the financial statements
- Failure to document required communication with the predecessor auditor
- Failure to document testing of subsequent events through the date of the auditor's report

Example MFC — AU-C 210: Predecessor Auditor Communication

In one ERISA audit, the firm did not sufficiently document its communications with the predecessor auditor.

Key Takeaway: Predecessor inquiries must be documented regardless of whether they are oral or written (AU-C 210.A33).

Predecessor Inquiries — AU-C 210

Required Before Engagement Acceptance

Requirements:

- Required to be made before engagement acceptance (AU-C 210.11–12)
- Auditor may propose on an engagement before inquiries have been authorized by management
  - If this is the case, auditor can advise management that proposal is not final until inquiries have been performed and results evaluated (AU-C 210.A29)
- Communication with predecessor can be written or oral (AU-C 210.A33)

Common MFCs — Reporting/Disclosure

Financial Statement Disclosures

The firm did not:

- Include required disclosures concerning:
  - Long-term debt for the next five years
  - Composition of current/deferred income taxes
  - Inventory at lower of cost or net realizable value
  - Revenue recognition for FASB ASC 606
- Failure to appropriately implement ASU 2016-14
- Failure to disclose the date through which subsequent events were evaluated

Example MFC — ASC 606 / ASC 842: Missing Disclosures

Footnotes to the financial statements were missing several required disclosures under the new revenue recognition standards including disclosures about revenue recognized at a point in time versus over time and opening balances for contract assets and liabilities for all revenue sources. The lease footnote was also missing disclosure about the weighted average remaining lease term, weighted average discount rate and the policy on separating lease components.

Key Takeaway: Verify ASC 606 and ASC 842 disclosure checklists are complete on every engagement, including point-in-time vs. over-time revenue disaggregation and lease term/rate disclosures.

Example MFC — ASC 842: Lease Standard Not Implemented

The new lease standard had not been implemented in the financial statements of the compilation without disclosures engagement reviewed in peer review. It was determined that the amounts of right of use assets and related liabilities would be material to the balance sheet.

Key Takeaway: Even compilation without disclosures engagements must implement ASC 842 when ROU assets and lease liabilities are material.

Common MFCs — Subsequent Events Disclosures

FASB ASC 855-10-45 and 50 | ASC 450-20-50-9

Disclose BOTH of the following:

- The date through which subsequent events have been evaluated
- Whether that date is either of the following:

The date the financial statements were issued

OR

The date the financial statements were available to be issued

Nonrecognized subsequent events that could be misleading must also disclose: the nature of the event, estimate of financial effect (or statement that estimate cannot be made), and consideration of pro forma statements.

Example MFC — ASC 855: Subsequent Event Date Discrepancy

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The report date did not agree to the subsequent event date in the disclosures, and neither of those dates agreed with the date the rep letter was signed, or the "as of" date included in the rep letter. The days were each off by only a few days.

Key Takeaway: Report date, subsequent event disclosure date, rep letter date, and rep letter "as of" date must ALL agree. Even a few days off creates a finding.

Common MFCs — Compilation Engagements (AR-C 80)

SSARS / AR-C 80

The firm did not:

- Update report in accordance with current SSARS
- Mention that substantially all disclosures were omitted
- Disclose special purpose framework
- Appropriately date the report
- Include verbiage related to supplemental schedules (and degree of responsibility the accountant is taking)
- Note lack of independence in engagement letter

Example MFC — AR-C 80: Compilation Report Period & Basis Error

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The Accountant's Compilation Report references the month ended and twelve months ended 12/31/23 and the statements are for the quarter and twelve months ended 12/31/23. Additionally, the financial statements are on the income tax basis but are referred to as being on the modified cash basis in the last two paragraphs of the report.

Key Takeaway: The compilation report must accurately reflect the periods covered AND the basis of accounting used — inconsistencies create MFCs.

Common MFCs — Review Engagements (AR-C 90)

SSARS / AR-C 90

The firm did not:

- Review Reports:
  - Failure to cover all of the periods or the correct periods presented in the financial statements in the accountant's report
- Failure to document materiality
- Insufficient/no analytical procedures performed
- Failure to document expectations

Example MFC — AR-C 90: Analytical Procedures

The accountant's analytical procedures did not include comparing recorded amounts or ratios to expectations developed by the accountant.

Key Takeaway: Review-level analytical procedures must compare recorded amounts to independently developed expectations — not just to prior year actuals.

Common MFCs — Agreed-Upon Procedures (AUP) Engagements

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SSAE 19 / AT-C 215

The firm did not:

- Include required language in AUP reports in accordance with professional standards, including:
  - Failure to include the word "independent" in the title
  - A statement that the sufficiency of the procedures is solely the responsibility of the specified parties and a disclaimer of responsibility for the sufficiency of those procedures
- Failure to obtain management representation letter
- Failure to provide appropriate documentation concerning agreed upon procedures
- Failure to obtain an engagement letter

Example MFC — SSAE 19: AUP Report Template Not Updated

The independent accountant's report on applying agreed-upon procedures was not in accordance with professional standards. Specifically, the firm did not use an updated report template from its practice guides in accordance with SSAE 19.

Key Takeaway: Practice guide templates must be updated to comply with SSAE 19. Using outdated report templates is a common, easily avoidable MFC.

Nonconforming Engagements

Engagement Reviews — Scenarios & Conformity Standards

Nonconforming Engagements

What is a nonconforming engagement? An engagement identified as not performed or reported on in accordance with the requirements of applicable professional standards in all material respects.

What is the impact on the Peer Review report rating?

Engagement Reviews	System Reviews
Report rating based on the number of nonconforming engagements in the review.	Report rating based on pervasiveness and evidence of a deficiency in the Quality Management system as a whole.

Conformity: Compilation Engagements — Conclusions Checklist

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VI. CONCLUSIONS (General Compilation Engagement Checklist)

Based on the work performed, did anything come to your attention that caused you to believe:

- The firm did not perform the engagement in all material respects in accordance with Statements on Standards for Accounting and Review Services. [ET sec. 1.310.001]
- The compilation report was not appropriate in the circumstances.
- The financial statements were not fairly presented in accordance with GAAP (or when applicable, a special purpose framework) in all material respects and the compilation report was not appropriately modified. [ET sec. 1.320.001]

Compilations: Scenario 1

Compilation Scenario 1

Engagement Type: Compilation omitting substantially all disclosures

Reporting Framework: GAAP

Reporting Period(s): Years ended December 31, 2025 and December 31, 2024

Matters:

- The engagement letter does not indicate that the compiled financial statements will omit disclosures.
- The compilation report refers to the year ended December 31, 2025, rather than the years ended December 31, 2025 and 2024.

Is the engagement nonconforming?

Compilations: Scenario 2

Compilation Scenario 2

Engagement Type: Compilation omitting substantially all disclosures

Reporting Framework: GAAP

Reporting Period(s): Years ended December 31, 2025 and December 31, 2024

Matters:

- The engagement letter does not exist, nor does another form of agreement with management regarding engagement terms.
- The compilation report does not include a separate paragraph discussing a known departure from GAAP.

Is the engagement nonconforming?

Compilations: Scenario 3

Compilation Scenario 3

Engagement Type: Compilation omitting substantially all disclosures

Reporting Framework: Tax basis

Reporting Period(s): Years ended December 31, 2025 and December 31, 2024

Matters:

- The significant elements of the compilation report are correct, including the paragraph which states, "The financial statements are prepared in accordance with the tax basis of accounting, which is a basis of accounting other than accounting principles generally accepted in the United States of America." However, the report also contains the following incorrect phrase: "Management has elected to omit substantially all the disclosures required by accounting principles generally accepted in the United States of America."
- The related financial statements with the report are appropriately labeled as "tax basis".

Is the engagement nonconforming?

Compilations: Scenario 4

Compilation Scenario 4

Engagement Type: Compilation omitting substantially all disclosures

Reporting Framework: Tax basis

Reporting Period(s): Years ended December 31, 2025 and December 31, 2024

Matters:

- The compilation report contains the following incorrect phrase: "Management has elected to omit substantially all the disclosures required by accounting principles generally accepted in the United States of America."
- The compilation report is missing the phrase: "and for determining that the tax basis of accounting is an acceptable financial reporting framework."
- The compilation report is missing the phrase: "The financial statements are prepared in accordance with the tax basis of accounting, which is a basis of accounting other than accounting principles generally accepted in the United States of America."

Is the engagement nonconforming?

Conformity: Review Engagements — Conclusions Checklist

V. CONCLUSIONS

Based on the work performed, did anything come to your attention that caused you to believe:

- The firm did not perform the engagement in all material respects in accordance with SSARSs? [ET sec. 1.310.001]
- The review report was not appropriate in the circumstances?
- The financial statements were not fairly presented in accordance with GAAP (or, when applicable, a special purpose framework) in all material respects and the review report was not appropriately modified? [ET sec. 1.320.001]
- The documentation on this engagement does not evidence compliance with professional standards?

Reviews: Scenario 5

Review Scenario 5

Engagement Type: Review

Reporting Period(s): Year ended December 31, 2025

Matters:

- Though some evidence of analytics existed, materiality was not documented.

Is the engagement nonconforming?

Reviews: Scenario 6

Review Scenario 6

Engagement Type: Review

Reporting Period(s): Year ended December 31, 2025

Materiality: $165,000

Matters:

- Though some evidence of analytical procedures existed, the documentation did not demonstrate how materiality was considered in designing or evaluating those procedures.
- Analytical procedures lacked documentation of expectations.

Is the engagement nonconforming?

Reviews: Scenario 7

Review Scenario 7

Engagement Type: Review

Reporting Period(s): Year ended December 31, 2025

Materiality: $165,000

Matters:

- Revenue Analytics: The entity subject to review had three revenue streams.
  - The firm disaggregated revenue and performed analytics specifically tailored to 2 of 3 revenue streams as well as reviewing overall total revenue in a more general analytic.
  - The third revenue stream (though material) represented only 3% of total revenue, had not varied significantly from the prior year, and the firm documented inquiries regarding the nature and expectations of the revenue.

Is the engagement nonconforming?

Conformity: Audit Engagements — Conclusions Checklist

b. The auditor failed to perform planning, including documentation and an appropriate risk assessment, in accordance with current professional standards. Consider the adequacy of the collective work performed in the following areas:

- Identified risk of material misstatement at the financial statement level
- Identified risk of material misstatement at the relevant assertion level for material classes of transactions, account balances and disclosures
- Planned audit procedures responsive to the risk assessment
- Risk assessment procedures, beyond inquiry, performed to evaluate the design and confirm implementation of key controls (manual and IT) relevant to the audit

g. The auditor's opinion is not supported by sufficient and appropriate documented audit evidence. For example, if significant oral explanations were required from the firm to support its conclusions for significant areas, answer this question yes.

Audits: Scenario 8 — NFP Risk Assessment / Inherent Risk

Audit Scenario 8

Engagement Type: Audit (not-for-profit entity)

Reporting Period(s): Year ended June 30, 2025

Background:

The firm documented significant risks related to the NFP's contribution revenue and net assets as its donor base historically gives late in the year and directs support to specific programs.

Matter:

The firm's assertion level assessment did not elevate inherent risk (IR) for the assertions likely related to these significant risks. However, the firm's audit programs and procedures demonstrated appropriately tailored and expanded procedures to address elevated IR in the following areas:

- Contribution revenue – cutoff and classification
- Net assets – classification

Is the engagement nonconforming?

Audits: Scenario 9 — D&I Controls & ITGC Documentation

Audit Scenario 9

Engagement Type: Audit (not-for-profit entity)

Reporting Period(s): Year ended June 30, 2025

Background:

Assume the fact pattern and existing matter from Scenario 8, while considering the additional matter below.

Matter:

Though the firm identified significant risks and properly addressed them via substantive audit procedures, the following issues also occurred:

- The firm did not document consideration of the design and implementation for internal controls over contribution revenue cutoff or classification.
- The firm did not document consideration of the design and implementation for Information Technology General Controls (ITGCs).

Is the engagement nonconforming?

Audits: Scenario 10 — ASC 606 Disclosure Omission

Audit Scenario 10

Engagement Type: Audit

Reporting Period(s): Year ended June 30, 2025

Matters:

- Though the company properly adopted and implemented ASC 606, Revenue from Contracts With Customers, the company failed to include appropriate disclosures related to the implementation. The only omitted disclosure was related to the opening balance of contract assets and liabilities.

Is the engagement nonconforming?

Audits: Scenario 11 — Going Concern Omission

Audit Scenario 11

Engagement Type: Audit

Reporting Period(s): Year ended June 30, 2025

Matters:

- Though the audit indicated the client was clearly in economic distress (debt covenant violations, cash flow issues, probable material lawsuit loss), the firm did not add an Emphasis of Matter paragraph to their report for going concern, nor did they include a going concern footnote.

Is the engagement nonconforming?

To Recap… Key Takeaways

Top Reasons for Nonconformity and/or Non-Pass Reports:

1. Risk assessment
2. Control documentation
3. Significant accounting standard changes (revenue recognition, leases, etc.)
4. Reporting departures

Remember! Nonconformity with professional standards impacts engagement and system reviews differently. The report rating for engagement reviews is based solely on the engagements reviewed, while the report rating for system reviews is based on the reviewed firm's system of Quality Management.

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Questions?

Contact your BMSS engagement team for guidance on peer review readiness and nonconforming engagement prevention.

Thank You!

Any questions, just e-mail me at mbrand@bmss.com

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