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New SSARS Issued

In February 2020, the AICPA issued Statement on Standards for Accounting and Review Services (SSARS) No. 25, *Materiality in a Review of Financial Statements and Adverse Conclusions*. SSARS 25 is effective for engagements performed for periods ending on or after December 15, 2021, with early implementation permitted.

SSARS 25 amends guidance in AR-C 60, *General Principles for Performing Engagements in Accordance With Statements on Standards for Accounting and Review Services*, AR-C 70, *Preparation of Financial Statements*, AR-C 80, *Compilation Engagements*, and AR-C 90, *Review of Financial Statements*. It also converges AR-C 90 with International Standards on Review Engagements (ISRE) 2400, *Engagements to Review Historical Financial Statements* (Revised), and addresses certain differences with auditing standards.

Following is a summary of the significant amendments resulting from SSARS 25:

Materiality

There is now an explicit requirement for the accountant to determine materiality for the financial statements as a whole and apply materiality when designing procedures and evaluating results. Accountants must design and perform analytical procedures and inquiries to address all material items in the financial statements, including disclosures, in order to obtain sufficient appropriate evidence to form a conclusion on the reviewed financial statements. Materiality should be revised if information becomes known during the review engagement that would have caused the amount of materiality to be different initially.

Current guidance for review engagements requires accountants to determine materiality in order to conclude and report that they aren't aware of any material modifications to be made to the financial statements to be in accordance with the applicable financial reporting framework. Thus, there is currently an implicit requirement for accountants to determine materiality in a review engagement.

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The explicit requirement will mean that accountants must not only determine materiality in a review engagement, they must also document their materiality determination.

Adverse Review Conclusion

If financial statements are determined to be materially and pervasively misstated, accountants can now express an adverse conclusion. Under prior guidance, accountants weren't permitted to modify the standard review report to state that the financial statements weren't in accordance with the applicable financial reporting framework and could only withdraw from the engagement. This change conforms the SSARS to ISRE 2400, which permits issuing adverse conclusions.

When the conclusion is modified, the conclusion paragraph in the accountant's review report should have the heading "Adverse Conclusion," followed by a separate "Basis for Adverse Conclusion" paragraph that provides a description of the matter. An example of the conclusion paragraph is, "Based on our review, due to the significance of the matter(s) described in the Basis for Adverse Conclusion paragraph, the financial statements are not in accordance with the applicable financial reporting framework." The basis for conclusion paragraph should describe and quantify the financial effects of the misstatement on the financial statements or disclosures, if known, or should state that management hasn't determined the amounts. It should also explain how narrative disclosures are misstated, or the nature of omitted information where required information isn't disclosed.

Independence

The review report is now required to include a statement that the accountant is required to be independent of the entity being reviewed and to meet other ethical responsibilities and comply with ethical requirements. This requirement is consistent with the statement that is required in audit reports under SAS 134.

Practical Consideration:

SSARS 25 is available on the AICPA's website at **www.aicpa.org** and on Checkpoint at **checkpoint.riag.com**.

New Standard for AUP Engagements

Statement on Standards for Attestation Engagement (SSAE) No. 19, *Agreed-upon Procedures Engagements*, was issued on December 5, 2019. It is effective for agreed-upon procedure (AUP) reports dated on or after July 15, 2021, and early implementation is permitted.

AUP engagements are a type of attestation engagement. Specific procedures are performed on the subject matter, which can be financial or nonfinancial information, based on the needs of the engaging party. The accountant performs various procedures based on the subject matter and reports the procedures performed and the findings. The accountant doesn't perform an examination or review and doesn't provide an opinion or conclusion.

SSAE 19 supersedes SSAE 18 AT-C 215, *Agreed-upon Procedures Engagements*, and amends sections of AT-C 105. Its intent is to provide greater flexibility in performing these types of engagements in the following ways:

- Removing the requirement that accountants obtain an assertion from the responsible party about whether the subject matter is measured or evaluated in accordance with suitable criteria, or to disclose in the accountants' AUP report that an assertion hasn't been obtained. This requirement was previously in AT-C 105 for AUP reports, as it is for examination and review reports.
- Permitting accountants to issue a general-use AUP report. Previously, AT-C 215 required the AUP report to be restricted to the use of specified parties that accepted responsibility for the sufficiency of the procedures performed. There is language in the report that advises that the procedures performed may not be appropriate for their purposes, and accountants can still restrict the use of the report if they think that is more appropriate.
- Eliminating the prior requirement that the intended users of the AUP report (specified parties) take responsibility for determining the procedures to be performed and their sufficiency as part of the terms of the engagement with the accountants.
- Allowing procedures to be developed by the accountant, engaging party, intended users of the report, or any of these together, and to be developed over the course of the engagement without requiring an updated engagement letter or acknowledgment from the other parties. But prior to the report

issuance, the engaging party is required to agree to the procedures and acknowledge that they are appropriate to meet the engagement's intended purpose. This agreement can be documented in the engagement letter, representation letter, or other written communication. If this agreement and acknowledgment aren't provided in writing, however, the accountant should withdraw from the engagement.

Practical Consideration:

The SSAE 19 is available on the AICPA's website at **www.aicpa.org** and on Checkpoint at **checkpoint.riag.com**.

Coronavirus is Increasing Audit Risks

The Coronavirus (COVID-19) outbreak has rightly become the focus of massive public attention in recent weeks, and financial markets around the world have reacted accordingly.

As a result, auditors should be mindful of heightened audit risks this year.

- **Valuation of Financial Assets**. With financial markets reacting to concerns over the spread of the virus, the measurement of financial assets will be a risk. The duration of the disruption is still unknown, but auditors and management may want to consider the potential for impairment. Financial assets reported at fair value on the balance sheet may also result in realized and unrealized losses. Management and auditors will also have to exercise judgment around critical estimates and cash flow projections used in the fair value measurement of non-quoted financial instruments.
- **Hedging**. Hedge accounting may be disrupted by higher-than-anticipated levels of volatility, resulting in higher levels of hedge ineffectiveness to recognize in earnings. Clients may also rethink the likelihood of the occurrence of a hedged forecasted transaction, with potential immediate consequences on earnings as well. Finally, management may be re-thinking their hedging strategies.
- **Valuation of Inventory**. Supply chains are disrupted, and production levels may be affected. If your client has reduced or idle production capacity, their overhead costs may not be allocated to inventory as they usually are. In addition, inventory that can't be turned over because of travel restrictions may have to be evaluated for impairment. Finally, changes in prices and reduction in the level of demand will also have to be taken into consideration.
- **Credit and Liquidity Risks**. Your clients' customers, as well as your clients themselves, may find themselves in financial difficulty, resulting in additional credit risks, higher than usual bad debt, and potentially even impairments and write-offs. Cash flows from operations may also be affected.
- **Measurement and Funded Status of Pension and Other Post-retirement Plans**. Both the expected return on plan assets and the funded status of the plans may have to be revisited in light of the volatility in financial markets.
- **Valuation Allowance on Deferred Tax Assets**. If estimates of earnings of foreign subsidiaries change, management may have to reconsider some of their tax strategies or may not be able to realize all deferred tax assets. This is another area that auditors should consider carefully when assessing critical estimates.
- **Valuation of Goodwill on Subsidiaries in Affected Areas of the Globe**. Subsidiaries in areas heavily affected by the Coronavirus may see their revenues or net income affected by the outbreak. This may trigger a goodwill impairment test. The reassessment of key accounting estimates and projections may result in an immediate goodwill impairment. Goodwill may also have to be tested more than once this year if management considers that evolving circumstances result in more than one triggering event over the next year. This is equally true for other intangible assets.
- **Subsequent Events**. The situation around the spread of the Coronavirus is evolving daily, sometimes even hourly. Auditors should ensure that their clients include the appropriate subsequent event disclosures in their annual and interim financial statements.
- **Disclosures**. Events that significantly affect customers' business and operations may require disclosures, both in the financial statements and outside of the financial statements, in various SEC filings and other parts of the 10-K or 10-Q (business, risk factors, management's discussion and analysis, etc.). The SEC has already signaled that it will be looking for disclosures about the impact of the Coronavirus.
- **Critical Audit Matters and Communication to Audit Committees**. A number of critical accounting estimates and assumptions may be affected by the Coronavirus outbreak, and they may rise to the level of critical audit matters that may now have to be communicated in public companies' auditor's reports.

By engaging with your client and their audit committee about these audit risks and the client's preparedness for such a crisis as it develops, auditors can demonstrate their value as trusted business advisors.

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We Want Your Financial Statements!

We have begun work on the 2020 edition of the Trends portion of *PPC's Guide to Preparing Financial Statements (PFS)* and are on the look-out for new illustrative financial statements. We ask that the financial statements include note disclosures and *not* be for governmental units.

To comply with AICPA or state ethics requirements, you may need to obtain permission from your client before submitting financial statements for consideration. We will carefully edit any financial statements to obscure the name and location of the organization and other identifying information. If your submission is selected for inclusion in the 2020 edition of *PFS*, **you will receive a free copy of that edition of PFS** and ***PPC's Guide to GAAP*** when they are available in the fall.

Financial statements may be submitted by attaching the files to an email and sending to **Checkpoint.PPC.PFS@thomsonreuters.com**.