THOMSON REUTERS
CHECKPOINT™

S. Davis & Associates, P.A.
Certified Public Accountants & Consultants

THE PPC
GOVERNMENTAL UPDATE

DECEMBER 2019, VOLUME 26, NO. 12

Future Changes to Auditor's Report

In May, the AICPA issued SAS No. 134, *Auditor Reporting and Amendments, Including Amendments Addressing Disclosures in the Audit of Financial Statements*, a suite of auditor reporting standards. This suite of auditor reporting standards is the result of the AICPA's ongoing Auditor's Report project. SAS No. 134 supersedes, replaces, adds, and amends many AU-C sections, including 200, 210, 220, 230, 240, 260, 300, 315, 320, 330, 450, 510, 540, 570, 600, 700, 701, 705, 706, and 910.

Though the changes are not effective and cannot be implemented until December 31, 2020, year ends, the changes are significant and auditors should familiarize themselves with them before then.

Changes to the Standard Auditor's Report

Changes are coming to the standard auditor's report to—

- Require the first section of the auditor's report to have the heading "Opinion" and to include the auditor's opinion on the financial statements, followed directly by the "Basis for Opinion" section (unless a different order is prescribed by law or regulation).
- Require the "Basis for Opinion" section to include an affirmative statement about the auditor's independence and fulfillment of the other ethical responsibilities in accordance with relevant ethical requirements.
- Add an option to communicate key audit matters (KAMs).
- Expand the description of management's responsibilities for the financial statements. It requires a section with the heading "Responsibilities of Management for the Financial Statements" that, in addition to the description of management's responsibilities now included in auditor's reports, also is required to state management's responsibility for assessing the entity's ability to continue as a going concern and whether use of the going concern basis of accounting is appropriate.
- Expand the description of the auditor's responsibilities and key features of an audit. It requires a section with the heading "Auditor's Responsibilities for

In this Issue:

This newsletter is also available online.
Please call (800) 431-9025, or order online:
https://tax.thomsonreuters.com/products/brands/checkpoint/ppc/

THOMSON REUTERS™

the Audit of the Financial Statements" that, in addition to the description of the auditor's responsibilities for the audit now included in auditor's reports, also is required to state that (1) the auditor's objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue a report that includes the auditor's opinion, (2) reasonable assurance is a high level of assurance, but not absolute assurance, and isn't a guarantee that an audit will detect a material misstatement when it exists, (3) the risk of not detecting a material misstatement resulting from fraud is higher than one resulting from error, (4) misstatements can arise from fraud or error and are considered material if they could reasonably be expected to influence the economic decisions users make based on the financial statements, (5) the auditor exercises professional judgment and maintains professional skepticism throughout the audit, and (6) the auditor's responsibilities include concluding on the entity's ability to continue as a going concern.

- Require the section of the auditor's report that describes the auditor's responsibilities to state that the auditor is required to communicate with those charged with governance about the planned scope and timing of the audit, significant audit findings, and certain internal control matters identified.
- Require the auditor's report to include a separate section when the auditor concludes there is substantial doubt about the entity's ability to continue as a going concern.

Report Modifications

Changes are coming to the form and content of the auditor's report for when the auditor's opinion is modified. These changes are to conform to the other changes in the suite of standards. However, the criteria for when modification to the auditor's opinion is required and the type of modification required are unchanged by the revisions. It is now clear that an emphasis-of-matter paragraph, other-matter paragraph, and communication of KAMs doesn't constitute a report modification.

Emphasis-of-Matter and Other-Matter Paragraphs

The relationship between matters included in emphasis-of-matter paragraphs and communicating KAMs in the auditor's report has now been clarified. An emphasis-of-matter paragraph isn't a substitute for describing KAMs in the auditor's report when a description of KAMs is required. The revised guidance also now requires that, when KAMs are included in the auditor's report, the heading of any emphasis-of-matter sections should include the term "Emphasis of Matter." Otherwise, the existing guidance on other-matter paragraphs is essentially unchanged.

Going Concern

SAS No. 134 also revised certain disclosure provisions in the auditor's report when the auditor concludes there is substantial doubt about the entity's ability to continue as a going concern (after considering relevant conditions and events and management's plans). The revisions require the auditor's conclusion about substantial doubt to be expressed in a separate section in the auditor's report, rather than in an emphasis-of-matter paragraph. In addition, the revisions make certain changes to the form and content of the separate section. The revised standard clarifies that if the auditor expresses a qualified or adverse opinion because of inadequate disclosure of going concern uncertainties, the auditor's "Basis for Qualified (Adverse) Opinion" section of the report is required to state either that substantial doubt exists or that substantial doubt has been alleviated, as appropriate, and that the financial statements fail to adequately disclose those matters.

Auditor Communications

In addition, SAS No. 134 requires the auditor to communicate with those charged with governance about (1) significant risks identified by the auditor and (2) circumstances that affect the form and content of the auditor's report.

Effective Date

SAS No. 134 is effective for audits of financial statements for periods ending on or after December 15, 2020, with early adoption not permitted.

Practical Consideration:

SAS No. 134, *Auditor Reporting and Amendments, Including Amendments Addressing Disclosures in the Audit of Financial Statements*, is available at **www.aicpa.org** or in the Advanced and Proposed Documents section of the AICPA Professional Standards on Checkpoint at **checkpoint.riag.com**.

Proposed Guidance for Certain Partnership Arrangements

In June 2019, the GASB issued a proposed statement, *Public-Private and Public-Public Partnerships and Availability Payment Arrangements*, to provide guidance on public-private and public-public partnership arrangements (PPPs) as well as availability payment arrangements (APAs).

Arrangements that allow a government to transfer the obligation for providing certain public services to other entities is becoming increasingly common. The GASB is proposing this guidance because current guidance on service concession arrangements (SCAs) and leases does not address all types of arrangements into which governments enter. The proposal would supersede current SCA guidance and include it in the new standard.

Practical Consideration:

The definition of an SCA and current financial reporting and accounting guidance for SCAs is provided in GASBS No. 60, *Accounting and Financial Reporting for Service Concession Arrangements*, which is available on Checkpoint at **checkpoint.riag.com** if you subscribe to GASB content.

What are PPPs and APAs?

The proposed standard defines PPPs and APAs as follows:

- A *PPP* is an exchange or exchange-like transaction in which a government (the transferor) conveys control of the right to operate or use infrastructure or a nonfinancial asset (the underlying PPP asset) over a specified period of time to a third party (the operator) for the purpose of providing a public service.
- An *APA* is an exchange or exchange-like transaction in which a government compensates a third party (the operator) to design, construct, finance, maintain, or operate infrastructure or a nonfinancial asset over a specified period of time. Compensation is based on the asset's availability for use (such as physical condition, construction milestones, achievement of certain performance measures) versus tolls, fees, or other measures of demand.

These arrangements differ from SCAs in terms of control. In a SCA, the government determines the services the operator provides, to whom the services are provided, and fees that can be charged for the services. In PPPs and APAs, the government doesn't have this level of control. The proposed standard indicates that PPPs that do not meet the definition of a SCA but do meet the definition of a lease should be accounted for under the lease accounting guidance in GASBS No. 87, *Leases*.

Practical Consideration:

The definition of a SCA in the proposed standard is essentially unchanged.

Recognition and Measurement—PPP Transferors

At the commencement of the PPP, the transferor would recognize a receivable for the present value of any payments expected to be received related to the PPP and a corresponding deferred inflow of resources. A transferor would continue to report the underlying PPP asset if the asset exists at the commencement of the PPP term. The transferor would also continue to depreciate or impair, if applicable, the PPP asset during the PPP term unless the operator is required to return the asset in its original condition.

A PPP asset that is purchased or constructed by the operator (or a current asset that is improved) should be accounted for as follows:

- If the PPP meets the definition of a SCA, the transferor would record the PPP asset at acquisition value (with a corresponding deferred inflow of resources) when placed into service and would depreciate or impair the asset as applicable.
- If the PPP does *not* meet the definition of a SCA, the transferor would record a receivable and corresponding deferred inflow of resources for the estimated carrying value of the PPP asset when ownership is transferred from the operator. The receivable would be remeasured if the PPP term is changed and expected to significantly change the estimated carrying value of the underlying PPP asset.

The PPC Governmental Update is published monthly by Thomson Reuters/Tax & Accounting, P.O. Box 115008, Carrollton, Texas 75011-5008, (800) 431-9025.

Tax & Accounting - Checkpoint
P.O. Box 115008
Carrollton, Texas 75011-5008
UNITED STATES OF AMERICA

ADDRESS SERVICE REQUESTED

PRSRT STD
U.S. POSTAGE
PAID
Thomson

Practical Consideration:

The proposed standard defines the term of the PPP and provides guidance on related matters, including options to extend or terminate, fiscal funding or cancellation clauses, and reassessment of the term. Detailed guidance is also provided for the initial and subsequent measurement of any receivables recognized, including guidance on discount rates, amortization of the discount, variable payments, residual value guarantees, and change in the PPP term.

Recognition and Measurement—PPP Operators

At commencement of the PPP, if the transferor owns the underlying PPP asset, the operator would record a liability for the present value of any payments expected to be paid related to the PPP and a corresponding intangible right-to-use asset.

A PPP asset that is purchased or constructed by the operator (or a current asset that is improved) should be accounted for as follows:

- If the PPP meets the definition of a SCA, the operator would record a right-to-use asset at cost and would amortize the asset over the shorter of the PPP term or the useful life of the asset.
- If the PPP does *not* meet the definition of a SCA, the operator would record the asset at cost and would depreciate or impair the asset as applicable. When the asset is placed into service, the operator would record a liability and corresponding deferred outflow of resources for the estimated carrying value of the PPP asset when ownership is transferred to the transferor. The liability would be remeasured if the PPP term is changed and expected to significantly change the estimated carrying value of the underlying PPP asset.

Practical Consideration:

The proposed standard provides detailed guidance on the right-to-use asset, including initial direct costs, amortization, and impairment. The proposal also has guidance on initial and subsequent measurement of any liability recognized, including guidance on discount rates, interest expense, variable payments, residual value guarantees, and change in the PPP term.

Recognition and Measurement—APAs

APAs for the design, construction, or financing of infrastructure or nonfinancial assets where ownership of the asset transfers to the government by the end of the contract would be accounted for as a financed purchase by the government. APAs for operation or maintenance services of infrastructure or nonfinancial assets should be accounted for as an expense or expenditure in the period to which the payment relates.

Disclosure Requirements

The proposed statement includes disclosure requirements related to PPPs for both transferors and operators. Disclosures include a description of the nature of the arrangement as well as information on the underlying PPP asset and any related receivable, liability, deferred inflows of resources, and deferred outflows of resources.

Effective Date and Transition

The proposed statement would be effective for fiscal years beginning after June 15, 2021, with earlier application encouraged.