

What You Need to Know:

# AUDIT CLARITY STANDARDS



Office of the  
**Utah State Auditor**

# Very Brief History

- Clarity Project started around 2004; first complete redraft/recodification since 1972
- Make standards easier to read, understand, and implement
- Harmonize with International Standards on Auditing (ISAs); framework-neutral language
- Effective for calendar year 2012 audits; early adoption not permitted



# What Will Be

- AU = extant
- AU-C = clarified; temporary codification of clarified SASs
  - Clarified SASs will replace extant SASs in 2014



# SASs 122-127

- SAS 122: Statements on Auditing Standards: Clarification and Recodification
- SAS 123: Omnibus Statement on Auditing Standards – 2011
- SAS 124: Financial Statements Prepared in Accordance with a Financial Reporting Framework Generally Accepted in Another Country



# SASs 122-127

- SAS 125: Alert That Restricts the Use of the Auditor's Written Communication
- SAS 126: The Auditor's Consideration of the Entity's Ability to Continue as a Going Concern
- SAS 127: *[new-ish]* Omnibus Statement on Auditing Standards – 2013; amends AU-Cs 600 & 800
- SAS ????: *[to be issued as a separate SAS in late 2013 or early 2014 and codified as AU-C 610]* The Auditor's Consideration of the Internal Audit Function in an Audit of Financial Statements (AU 322)



# AU-Cs With Few or No Changes

- 220-Quality Control
- 230-Audit Documentation
- 240-Consider Fraud
- 260-Comm with Governance
- 300-Planning
- 315-Understanding the Entity
- 450-Evaluate Misstatements
- 500-Audit Evidence
- 520-Analytical Procedures
- 530-Audit Sampling
- 540-Auditing Estimates
- 570-Going Concern
- 580-Written Representations

- 585-Omitted Procedures
- 610 Internal Audit (coming)
- 705-Modifications to Opinion
- 720-Other Information
- 725-Suppl Information
- 730-Required Suppl Info
- 806-Reports on Compliance
- 910-Repts of Another Country
- 915-Rept Appl of Acctg Princ
- 920-Underwriters
- 925-SEC Filings
- 930-Interim Fin Info
- 935-Compliance Audits



# Significant Changes

- Renumbering/reorganization of sections
- Organization and formatting
- New terminology
- Traditional 10 generally accepted auditing standards lose authoritative status
- Wording and format of auditor's reports
- **\*\*Standards for Group Audits\*\*** (AU-C 600)



# Formatting of AU-Cs

- Introduction
- Objective
- Definitions
- Requirements (unconditional = “must” while presumptively mandatory = “should”)
- Application and Other Explanatory Material (integral, but separate from Requirements)



# Implementation

What is the first thing you did to implement?

Who have you involved in the process?

What have been the most helpful resources?

What changes have you discussed with clients?

Any implementation issues you've noted?

Have you visited [www.aicpa.org](http://www.aicpa.org)?



# AICPA's Learning & Implement Guide

1. Designate an expert
2. Familiarize yourself with standards
3. Take a deeper look into the substantive changes and evaluate impact
4. Apply to firm's audit methodology
5. Facilitate training for staff and partners



# AICPA Learning & Implement Guide

6. Determine impact for each audit engagement and prepare for potential client concerns
7. Update engagement letters, auditor's reports, and mgmt rep letters for new language
8. Communicate with clients
9. \* Keep up with clarified standards



# AU-Cs 700, 705, 706: Reporting

Extant AU Section		AU Section Superseded	New AU-C Section		Type of Change
410	Adherence to Generally Accepted Accounting Principles	All	700	Forming an Opinion and Reporting on Financial Statements	Substantive
431	Adequacy of Disclosure in Financial Statements	All	705	Modifications to the Opinion in the Independent Auditor's Report	Formatting
508	Reports on Audited Financial Statements	.01-.11, .14-.15, .19-.32, .35-.52, .58-.70, and .74-.76	700	Forming an Opinion and Reporting on Financial Statements	Substantive
			705	Modifications to the Opinion in the Independent Auditor's Report	Formatting
			706	Emphasis-of-Matter Paragraphs and Other-Matter Paragraphs in the Independent Auditor's Report	Substantive
530	Dating of the Independent Auditor's Report	.01-.02	700	Forming an Opinion and Reporting on Financial Statements	Substantive



# AU-C 700: Opinion & Report

- “Clean opinion” / “unqualified opinion” → “Unmodified opinion”
  - Modified opinions covered in AU-C 705
- Report adds detailed description of management’s responsibilities
- New report headers
- Addresses procedures on forming an opinion on comparative F/S



# AU-C 705: Modification Headers

## ***Basis for Qualified Opinion***

The Company has stated inventories at cost in the accompanying balance sheets. Accounting principles generally accepted in the United States of America require inventories to be stated at the lower of cost or market. If the Company stated inventories at the lower of cost or market, a write down of \$XXX and \$XXX would have been required as of December 31, 20X1 and 20X0, respectively. Accordingly, cost of sales would have been increased by \$XXX and \$XXX, and net income, income taxes, and stockholders' equity would have been reduced by \$XXX, \$XXX, and \$XXX, and \$XXX, \$XXX, and \$XXX, as of and for the years ended December 31, 20X1 and 20X0, respectively.

## ***Qualified Opinion***

In our opinion, except for the effects of the matter described in the Basis for Qualified Opinion paragraph, the financial statements referred to above present fairly, in all material respects, the financial position of ABC Company as of December 31, 20X1 and 20X0, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.



# AU-C 706: Emphasis-of-Matter & Other-Matter Paragraphs

Emphasis of Matter (EOM)	Other Matter (OM)
<p>A matter appropriately <b>presented in the F/S</b> that is of such importance that it is fundamental to users' understanding of the F/S</p>	<p>A matter <b>other than those presented in the F/S</b> that is relevant to users' understanding of the audit, the auditor's responsibilities, or the auditor's report</p>
<p>Include in report immediately after the opinion paragraph</p> <p>Indicate that the opinion is not modified with respect to the matter</p>	<p>Include in report</p> <ul style="list-style-type: none"><li>•Immediately after the opinion and EOM</li><li>•Elsewhere if relevant</li></ul>



# AU-Cs 700 & 706: Report Headers Exercise

- Report on the Financial Statements
- Management's Responsibility for the Financial Statements [new section]
- Auditor's Responsibility [replaces scope paragraph]
- Basis for Qualified Opinion
- Qualified Opinion
- Emphasis of Matter
- Other Matter
- Report on Other Legal and Regulatory Requirements



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# AU-C 935: Compliance Audits

Extant AU Section		AU Section Superseded	New AU-C Section		Type of Change
801	Compliance Audits	All	935	Compliance Audits	Formatting

- SAS 117 was originally issued in clarity format and codified as AU 801
- Effective for fiscal periods ending on or after June 15, 2010
- Recodified in SAS 122 as AU-C 935



# AU-C 935: Compliance Audits

Applicable when an auditor is engaged, or required by law or regulation, to perform a compliance audit in accordance with all of the following:

- Generally accepted auditing standards (GAAS)
- The standards for financial audits under *Government Auditing Standards*
- A governmental audit requirement that requires an auditor to express an opinion on compliance



**Independent Auditor's Report on Compliance in Accordance  
with the *State of Utah Legal Compliance Audit Guide***

[appropriate addressee]

We have audited [name of city]'s (the City) compliance with general and major state program compliance requirements described in the *State of Utah Legal Compliance Audit Guide* applicable to the City for the year ended June 30, 20XX.

The general compliance requirements applicable to the City are identified as follows:

- Public Debt
- Cash Management
- Purchasing Requirements
- Budgetary Compliance
- Truth in Taxation and Property Tax Limitations
- Liquor Law Enforcement
- Justice Courts Compliance
- B and C Road Funds
- Other General Compliance Issues
- Uniform Building Code Standards
- Impact Fees
- Asset Forfeiture
- Utah Retirement System Compliance
- Fund Balance

The City received the following major state programs from the State of Utah:

- Community Library Enhancement Funds (Department of Heritage and Arts)
- Critical Needs Housing (Department of Workforce Services, Housing and Community Development Division)
- Sidewalk Construction (Department of Transportation)

***Management's Responsibility***

Management is responsible for compliance with the requirements referred to above.

***Auditor's Responsibility***

Our responsibility is to express an opinion on the City's compliance based on our audit of the compliance requirements referred to above.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the *State of Utah Legal Compliance Audit Guide*, issued by the Office of the Utah State Auditor. Those standards and the *State of Utah Legal Compliance Audit Guide* require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the compliance requirements referred to above that could have a material effect on a general compliance requirement or a major state program occurred. An audit includes examining, on a test basis, evidence about the City's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.



We believe that our audit provides a reasonable basis for our opinion on compliance for each general compliance requirement and each major state program. However, our audit does not provide a legal determination of the City's compliance.

***Basis for Qualified Opinion on [Identify General Compliance Requirement or Major State Program]***

As described below, the City did not comply with requirements regarding *[identify general compliance requirement or major state program and related compliance requirements]*. Compliance with such requirements is necessary, in our opinion, for the City to comply with the requirements applicable to that *[general compliance requirement]* *[program]*.

*[Describe material instances of noncompliance]*

*[Insert views of responsible officials]*

***Qualified Opinion on [Identify General Compliance Requirement or Major State Program]***

In our opinion, except for the noncompliance described in the Basis for Qualified Opinion paragraph, *[name of city]* complied, in all material respects, with the compliance requirements referred to above applicable to its *[identify the general compliance requirement or the major state program]* for the year ended June 30, 20XX.

***Unmodified Opinion on Each of the Other General Compliance Requirements and on Each of the Other Major State Programs***

In our opinion, *[name of city]* complied, in all material respects, with the compliance requirements referred to above that are applicable to each of its other general compliance requirements and each of its other major state programs for the year ended June 30, 20XX.

***Other Matters***

The results of our auditing procedures disclosed other instances of noncompliance, which are required to be reported in accordance with the *State of Utah Legal Compliance Audit Guide* and which are described below. Our opinion on compliance is not modified with respect to these matters.

*[Describe other instances of noncompliance]*

*[Insert views of responsible officials]*

The City's response to the noncompliance findings identified in our audit is described above. The City's response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

*[auditor's signature]*

*[auditor's city and state]*

*[date of the auditor's report]*



# AU-C 905: Alerts

Extant AU Section		AU Section Superseded	New AU-C Section		Type of Change
532	Restricting the Use of an Auditor's Report	All	905	Alert That Restricts the Use of the Auditor's Written Communication	Clarifying

- Alert = language that restricts the use of the auditor's written communication
  - Auditor's written communication – auditor's reports, letters, presentation materials
  - When the potential exists for the auditor's written communications to be misunderstood if taken out of the context in which it is intended to be used



# When Are Alerts Required?

- Measurement or disclosure criteria are determined to be suitable only for a limited number of users who can be presumed to have an adequate understanding of the criteria
- Measurement or disclosure criteria are available only to the specified parties, or
- By-product reports - Matters identified by the auditor during the audit when the identification of such matters is not the primary objective of the audit.



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# Restricted “Use” Alerts

- State that the auditor’s written communication is intended solely for the information and **use** of the specified parties
- Identify the specified parties for whom **use** is intended (restrictions on who may be a specified party for by-product reports)
- State that the auditor’s written communication is not intended to be and should not be **used** by anyone other than the specified parties.
- See Appendix A for a list of specific requirements for restricted “use” alerts



# Restricted “Purpose” Alerts

- Engagement performed in accordance with GAS
- AND Auditor’s written communication issued in accordance with
  - AU-C 265 – Communicating Internal Controls Related Matters Identified in an Audit
  - AU-C 806 – Reporting on Compliance With Aspects of Contractual Agreements or Regulatory Requirements in Connection With Audited Financial Statements
  - AU-C 935 – Compliance Audits



# Restricted “Purpose” Alerts

- Describe the **purpose** of the auditor’s written communication AND
- State that the auditor’s written communication is not suitable for any other **purpose**



# Illustrative Alerts

## “Restricted” Intended Use

“This [*report, letter, or communication*] is intended solely for the information and use of [*list or refer to the specified parties*] and is not intended to be and should not be used by anyone other than these specified parties.”

## “Restricted” Purpose

“The purpose of this [*report, letter, or communication*] is to [*describe the purpose of the communication*]. Accordingly, this [*report, letter, or communication*] is not intended to be and should not be used for any other purpose.”



# AU-C 600: Group Audits

Extant AU Section		AU Section Superseded	New AU-C Section		Type of Change
508	Reports on Audited Financial Statements	.12-.13	600	Special Considerations - Audits of Group Financial Statements (Including the Work of Component Auditors)	Substantive
543	Part of Audit Performed by Other Independent Auditors	All			



# Q&A

[www.aicpa.org/SASClarity](http://www.aicpa.org/SASClarity)

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