



July 31, 2009

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Accounting and Review Services Committee

By e-mail to [mglynn@aicpa.org](mailto:mglynn@aicpa.org)

RE: Proposed Statements on Standards for Accounting and Review Services Exposure Draft

Dear Mike Glynn and the Accounting and Review Services Committee,

The Accounting and Auditing Committee of The Ohio Society of Certified Public Accountants is pleased to express its views on the exposure draft "Accounting and Review Services".

We agree that it was a positive initiative for the committee to evaluate the present compilation and review services standards. The committee has the following comments, questions and suggestions.

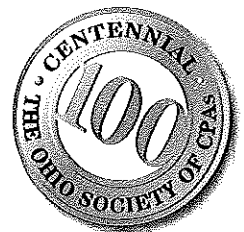
#### **Non-Independent Reviews**

The Committee opposes the provision to allow an accountant to issue a review report disclaiming independence when that accountant provides control activity assistance to the client and is not independent under ET 101-3.

We find it inconsistent to modify the level of assurance being offered from "limited" to "moderate," and at the same time eliminate the requirement for objectivity and independence. A basic tenet of the attest function has always been that if assurance (positive or negative) is being offered, independence is mandatory.

The increase in engagement risk due to impaired independence should be considered in adopting the "non-independent" review. Our committee believes it would be difficult to remain objective when reviewing our own work. In most cases, the CPA would be applying review procedures to his or her own bookkeeping; accordingly, the results would almost always be consistent with what the reviewer expected. There is value in independence which we believe increases the reliability of the review report and financial statements.

International Standards on Review Engagements do not allow an accountant to issue a review report when the accountant is not independent; current SSARS is consistent with this. We question why, when our profession is apparently headed toward convergence with international standards, we would deliberately establish a non-convergent standard. In fact, only last year, ARSC issued SSARS Interpretation 30, which moved SSARS toward such convergence by offering guidance on reporting on various combinations of US and international standards. We would now have to educate third party users that reviews under international standards require independence, but reviews under US standards do not.



The argument that using two CPAs will increase the cost of a review is not necessarily valid. If the CPA who is not independent prepares financial statements and assists with bookkeeping, etc. they should be in a position to provide "review ready" financial statements to the CPA performing the review. The additional cost would then be minimal. Allowing a "non-independent" review may only serve to increase the costs for clients as many users may no longer allow reviews as they change their rules to require the *only* true independent report, the audit.

We also feel that allowing reviews when independence is impaired will have an impact on a firm's peer review. The 2009 Peer Review Standards require peer reviewers to make an engagement risk assessment of a firm as part of the planning phase in a system peer review. This risk assessment is oriented toward the risk that a firm will issue reports that are not appropriate in the circumstances. It is composed of three elements: inherent risk, control risk, and detection risk. Our concern is that, given the way firms conduct engagements, peer reviewers may deem it necessary to elevate both inherent and control risk when they become aware that a firm is performing non-independent reviews.

Inherent risk would be elevated because any non-independent service for which assurance is offered is going to be inherently riskier: firms may be under pressure to issue erroneous reports due to significant fees generated from non-attest services provided to review clients (in fact, the firm undergoing peer review is required to identify their largest clients by fee – not just compilation, review, or audit fee, but total fee.)

Control risk may be elevated due to the potential that the firm:

- a) Does not have a properly-designed system of quality control, or will not sufficiently modify it, to address the additional safeguards necessary to ensure that the lack of independence is mitigated. (SQCS 7 requires firms to have written quality control policies and procedures; that standard includes, as one of its elements, independence and other relevant ethical requirements, and requires firms to identify threats to independence.) In our peer review chairman's view, the only truly adequate way to design these controls for a review in which independence is impaired is to ensure that the engagement partner on the review is not the same partner responsible for supervising the non-attest services, or that a second partner preissuance review of the engagement is performed. We seriously doubt that sole practitioners and small local firms will be able or willing to do this.
- b) Will not adequately enforce its existing policies regarding engagement performance, reasoning that, "since we already do the accounting, we can zip through the review because we know the accounting is right." Most firms, when trying to implement a standard that they will perceive as reducing the level of responsibility (and make no mistake, most firms see non-independent engagements as reduced responsibility) see it as an opportunity to reduce the amount of work needed. In this case, their own risk will go up, not down, and we strongly suspect firms will react inappropriately and ineffectively.
- c) Will not be able to adequately monitor these engagements. Many firms are already struggling with how to maintain objectivity when reviewing engagements

performed when they are independent. Reviewing engagements in which independence is already impaired and (unlike compilations) assurance is being given can only increase the difficulty of maintaining sufficient objectivity in monitoring procedures.

This will likely result in moderate to high inherent and control risk assessments, which will require a low detection risk in order to reduce overall peer review risk to an acceptable level. The only way to achieve that will be to increase the scope of reviews.

If non-independent reviews are allowed, the chair of our Peer Review Committee intends to urge the AICPA peer review committee to make it mandatory to select both an independent and non-independent review engagement when performing engagement peer reviews of non-audit firms, since these reviews do not provide for a risk-based engagement selection.)

*As indicated above, we are against allowing non-independent reviews, but the comments below are made assuming that non-independent reviews will be adopted.*

#### **Limited Assurance vs. Moderate Assurance**

Our committee does not believe that the change from moderate to limited assurance is appropriate for a review. Is moderate assurance intended to be a higher level of assurance than limited assurance or is the terminology changed only for convergence of standards with those of the International Auditing and Assurance Standards Board? By definition moderate means "average in amount, intensity, quantity, or degree..." and limited means "restricted in size, amount, or extent; few, small, or short...". Moderate assurance suggests that users will expect a higher level of assurance than has been required in the past when limited assurance has been the review requirement. Would "moderate assurance" require additional procedures to achieve? If "moderate assurance" is adopted we need a better concept of review risk and examples of when an increase in review risk might occur. This would especially be important if allowing a "non-independent review". Would using moderate assurance as opposed to limited assurance mean anything to third party users? While we appreciate the changes in terminology for an easier convergence with international standards, the change from "limited" to "moderate" is a significant change that may not be justified if the procedures to achieve this level of assurance are not changed.

#### **Internal Control Services**

Internal Control Services defined in ¶'s 16 through 19 of the *Compilation of Financial Statements* and ¶'s 26 through 29 of *Review of Financial Statements* is confusing. The paragraphs seem to change the general requirements for nonattest services under the Professional Code of Ethics Section 101-3, or to add a separate set of services in addition to (and perceived as being exempt from) the provision of that rule. Nowhere in the proposal is this section or any other section of the Code of Ethics referenced. The "Internal Control Services" sections should be removed or only refer to ET Section 101-3. If a change in ET 101-3 is intended, the change should be made there and not in the SSARS. If a definition of internal control services is included, the definition should at least refer to ET 101-3 and the examples included in paragraphs 18 and 28 should be removed or better explained. The COSO definition of "internal control over financial reporting" could be referred to as additional explanatory material as well.

It would appear that much of the convoluted language around this issue could be avoided by simply saying "impairments of independence arise from performing non-attest services in non-independent manner as described in ET 101-3 and related Interpretations." This approach would also be consistent with the approach taken in other professional standards, and would avoid creating a second source of rules (and opportunities for inconsistencies between them) for determining independence.

### **Engagement Letters**

Under ¶2 of *Compilation of Financial Statements* it is stated that "the accountant should establish an understanding with management...and should document the understanding through a written communication with management." This should be an unconditional requirement rather than a presumptively mandatory requirement (change the word "should" to "must"). It is suggested that language should also be included to indicate how often this understanding should be made in writing as many compilations are done on a continuing basis. For example this requirement might read, "the accountant should establish an understanding with management not less than annually regarding the services to be performed for each engagement."

The example engagement letters should include a suggestion to include documentation required by ET 101-3 with "Other Matters" under "What is Required".

### **Representation Letters**

If the standard is changed to allow independence impairment for a review, the management representation letter should incorporate language that explicitly expresses what the reviewer did. The model offered in the exposure draft on page 101, Exhibit E, ¶ 78 does not provide such examples.

### **Review Risk and Review Evidence**

What factors would increase review risk under "moderate assurance"? What types of review evidence would indicate this increase in risk? This review risk and examples could be included in "Designing and Performing Review Procedures" under *Review of Financial Statements* ¶s 14 through 23.

### **Compiled Financial Statements to be Used by a Third Party**

To be consistent with existing standards, it should be stated within ¶ 27 that financial statements compiled for use by an auditor are not considered as "distributed to third parties" when distributed to an auditor for this purpose. Paragraph 27 should specifically state that the accountant does not have a responsibility to find out if the client has distributed the financial statements to a third party and has no duty to control this distribution. The paragraph should refer to ¶ 55 for the outlined steps if they become aware that the client has distributed the financial statements to a third party.

### **Separate Chapters for Compilation and Review Engagements**

The codification of the SSARS into separate paragraphs for compilation and review services is very helpful to the practitioner. We believe that this will promote the understanding of the nature of the services provided.

Our concern is that there are inconsistencies between chapters. For example, ¶18 under *Compilation of Financial Statements* states “internal control services include bookkeeping services” and ¶28 under *Review of Financial Statements* states “internal control services include certain bookkeeping services”. If this difference is correct, we suggest that you explain what certain bookkeeping services impair independence for reviews and explain why all bookkeeping services impair independence for compilations. Other differences between the separate chapters should be highlighted. Again, we prefer simply referencing ET 101-3.

### **Exhibit B- Illustrative Compilation Reports**

The second report example under ¶ 68 indicates that the compilation report is “*in accordance with the cash basis of accounting*”. The financial statement titles shown in the example are for the modified cash basis of accounting.

### **Illustrative Inquiries**

It is suggested that additional illustrative inquiries be added to help practitioners determine inquiries appropriate to understanding client’s internal controls for *Review of Financial Statements*.

### **Reporting on Compiled and Reviewed Financial Statements**

Our committee is in favor of changing the compilation and review reports to the alternatives provided in the exposure draft. We feel that the alternative reporting makes the distinction between the managements and accountants responsibility more understandable to the user’s of the financial statements.

The biggest change in this proposal is the change to allowing “non-independent” reviews and we would like to reiterate our committee’s opposition to this proposal.

We appreciate the opportunity to provide feedback to this exposure draft and welcome any questions that you may have or clarifications that we can make.

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