AICPA Peer Review Program Compliance
Leveraging the Revised Standards for Optimal Peer Review Outcomes

A Live 90-Minute Audio Conference with Interactive Q&A

Today's panel features:
Albert (Bert) Denny, Director of Audit and Accounting, Regier Carr and Monroe, Wichita, Kan.
Brent Silva, Managing Partner, Silva and Associates, Mandeville, La.

Tuesday, May 12, 2009
The conference begins at:
1 pm Eastern
12 pm Central
11 am Mountain
10 am Pacific

The audio portion of this conference will be accessible by telephone only. Please refer to the dial in instructions emailed to registrants to access the audio portion of the conference.

CLICK ON EACH FILE IN THE LEFT HAND COLUMN TO SEE INDIVIDUAL PRESENTATIONS.

If no column is present: click Bookmarks or Pages on the left side of the window.
If no icons are present: Click View, select Navigational Panels, and chose either Bookmarks or Pages.

If you need assistance or to register for the audio portion, please call Strafford customer service at 800-926-7926 ext. 10
AICPA Peer Review Program
Compliance Teleconference

May 12, 2009

New Peer Review Standards

Albert (Bert) Denny, Regier Carr & Monroe LLP
bert.denny@rcmcpa.com
Principles V. Rules-Based Standards

• Detailed guidance is in the interpretations
• All guidance was reevaluated, reengineered, updated and clarified
• Allows standards to be applicable to a diverse population of users that includes large and small firms
• Allows Peer Review Board to be more responsive to changes through interpretive guidance
• Effective for reviews commencing on or after Jan. 1, 2009
New Reporting Process

• Why?
  – Redesigned to be more understandable and easier to use
  – Provides transparency by being more easily understood
  – Promotes consistency for all types of peer reviews
  – Streamlines process at all levels

• How?
  – Defines terms and provides enhanced process guidance
  – Integrates expanded use of practice aids to communicate findings to the firm (new forms not part of the reporting process)
  – New reporting format (eliminates the former letter of comments)
Defined Terms

The revisions:

• Define the terms “matter,” “finding,” “deficiency” and “significant deficiency”

• Describe how they may affect the type of report issued on a system or engagement review

• Eliminate use of the term “substandard” due to an increased systems-oriented focus
Expanded Use Of Practice Aids

- Finding for further consideration (FFC) form communicates findings to the reviewed firm that don’t affect the opinion or type of peer review report issued

- This change eliminates the separate letter of comment, and in doing so makes the reporting model more efficient

- FFC form will be retained by the AEs along with the peer review reports

- Peer review committees will determine need for:
  - Follow-up actions based on the deficiencies/significant deficiency in the report
  - Implementation plans based on the FFCs
New Peer Review Report

• One-page, stand-alone document
• Three paragraphs
  – What was reviewed, under what standards, reviewer and firm responsibilities
    • Includes a URL to the standards for nature, objectives, scope, limitations and procedures performed, in plain English
  – If applicable, reference to GAGAS, EBP &/or FDICIA practice
  – Opinion and peer review grade
    • Pass
    • Pass with deficiency
    • Fail
New Peer Review Report

• Includes descriptions of deficiencies only for reports with a grade other than “Pass”
  – Identifies the industry and level of service for any deficiencies or significant deficiencies that are determined to be industry specific included in the report

• Requires little tailoring
Report With A Peer Review Rating Of “Pass,” In A System Review

System Review Report

To the Partners of [or other appropriate terminology]
XYZ & Co.
and the Peer Review Committee of the [insert the name of the applicable Administering Entity]

We have reviewed the system of quality control for the accounting and auditing practice of XYZ & Co. (the firm) in effect for the year ended June 30, 20XX. Our peer review was conducted in accordance with the Standards for Performing and Reporting on Peer Reviews (“Standards”) established by the Peer Review Board of the American Institute of Certified Public Accountants. The firm is responsible for designing a system of quality control and complying with it to provide the firm with reasonable assurance of performing and reporting in conformity with applicable professional standards in all material respects. Our responsibility is to express an opinion on the design of the system of quality control and the firm’s compliance therewith based on our review. The nature, objectives, scope, limitations of and the procedures performed in a System Review are described in the Standards at www.aicpa.org/prsummary.

As required by the Standards, engagements selected for review included (engagements performed under the Government Auditing Standards; audits of Employee Benefit Plans, and audits performed under FDICIA).

In our opinion, the system of quality control for the accounting and auditing practice of XYZ & Co. in effect for the year ended June 30, 20XX has been suitably designed and complied with to provide the firm with reasonable assurance of performing and reporting in conformity with applicable professional standards in all material respects. Firms can receive a rating of pass, pass with deficiency(ies) or fail. The firm has received a peer review rating of pass.

Smith, Jones and Associates
[name of team captain’s firm]
Consolidates Report And Engagement Reviews

- Folds report reviews into engagement reviews while maintaining several attributes of the report review process, and makes other revisions to engagement reviews
  - For compilation engagements, the reviewer evaluates the firm’s documentation by reviewing background and engagement profile information, firm representations and inquiries rather than reading the actual documentation
  - Revises the definition of what constitutes a repeat finding; the disclosure, presentation or measurement finding should be the same or very similar to that noted in the previous review
Other Engagement Review Enhancements

- Provides guidance for the type of report to be issued when the exact same significant deficiency occurs on each of the engagements submitted for review, and there are no other significant deficiencies.
- The report:
  - States that the reviewer’s objective is to “evaluate” whether the engagements submitted for review were performed and reported on in conformity with applicable professional standards in all material respects.
  - States that it is the firm’s responsibility to design and comply with a system of quality control.
  - Indicates that no opinion or other form of assurance is being expressed because the system of quality control and the firm’s compliance therewith have not been reviewed.
- Provides that the technical reviewer can be delegated the acceptance responsibility for certain peer reviews with no MFC forms.
Other Changes

- Team members not required to take the two-day “how to” course
- Independence impairment for internal inspectors, consulting reviewers and pre-issuance reviewers intending to perform peer reviews
- Reporting on scope limitations under the revised standards
- Performing a system review at a location other than the reviewed firm’s office, when it is cost-prohibitive and/or extremely difficult to arrange
Effect On CPCAF Peer Review Program

• CPCAF PRP merged into AICPA PRP
  – National Peer Review Committee (National PRC) to be the 42nd administering entity
  – Handles reviews for 55 licensing jurisdictions
• Administers:
  – Firms required to be registered with and inspected by the PCAOB
  – Firms that perform audits of non-SEC issuers pursuant to the standards of the PCAOB
  – Firms that elect to have their reviews administered by the National PRC
Revised Peer Review Manual

• Peer Review Manual’s new format will include:
  – Section 1000: Standards
  – Section 2000: Interpretations
  – Section 3000: Other Guidance
    • Supplemental information
    • Peer review alerts
    • RAB Handbook

• To be issued in an electronic format with “search” capabilities
AICPA Peer Review Program
Compliance Teleconference
May 12, 2009

Peer Review Transparency, Statement on Quality Control Standards (SQCS) No. 7, Common Peer Review Deficiencies

Brent A. Silva, CPA
Silva & Associates, LLC, CPAs
bsilva@silva-cpa.com
Today’s environment focuses on “open book” policy

Perception issues

Prior reporting confusing to users
- Problems linking unmodified report with LOCs
- Differentiating between LOCs that lead to modified and LOCs

Regulatory relationships

Future expectations
Perception Issues

- Overall lack of understanding of peer review process
  - Became apparent after Enron/Worldcom scandals
- Profession sees peer review as remedial, not compliance-driven
- Public does see peer review as compliance-driven
  - Professional liability/state board/regulatory bodies
Regulatory Compliance

- 45 state boards require peer review
- New York finally enacted mandatory peer review into law
- GAO requires peer reviews and disclosure for firms that report under Yellow Book
- Most professional liability insurance firms require a copy of the report for applications and/or renewals
Transparency Of Reports

- Should be proud of achieving an outstanding result
- Should take responsibility for any issues that arose during process
- A bad mark doesn’t scar you for life, just as a good mark doesn’t let you rest on your laurels
Future Expectations

- An agreement between the AICPA and state societies will allow state boards access to peer review results
  - “Opt out” provision – compromise to push for full transparency
    - Allows a firm to elect not to allow state boards access to results (states vary on agreements)
Statement on Quality Control Standards (SQCS) No. 7
SQCS No. 7

- Issued October 2007
- Effective as of January 1, 2009
- Supersedes SQCS nos. 1-6
Professional Requirements

- Firms must establish and document a system of quality control
  - Extent of documentation based on firm’s structure and approach
- Firms must communicate QC policies and procedures to personnel
  - Documentation of communication not required
Professional Requirements (Cont.)

- Documentation and communication of QC policies and procedures will vary based on various factors.
- Use professional judgment in determining method of documentation.
  - Checklist provided by review for QC is adequate.
  - Must be completed at least one year prior to beginning of peer review.
Professional Requirements (Cont.)

- Two categories of degree of responsibility
  - Unconditional – must follow in all cases
  - Presumptively mandatory – expected to comply but departure requires documentation of reason
Elements Of Quality Control System

- Leadership responsibility ("tone at the top")
- Relevant ethical requirements
- Client engagement acceptance/continuance
- Human resources
- Engagement performance
- Monitoring
SAS No. 115 Report

- Improper assessment of control deficiency, significant deficiency or material weakness
- Improper identification of deficiency as design or operational
- No follow-up on previous deficiencies communicated to management
- Lack of restriction on the use of the report
Fair Value

- Improper understanding of management’s assessment of nature, assumptions and factors
- Lack of documentation of work performed on fair value
Areas Firms Have Recurring Deficiencies

- AICPA PRB OTF identifies and compiles deficiency commonalities and patterns as part of its oversight visits
  - Report acceptance body (RAB) reviews and accepts submitted peer reviews
  - As part of oversight process, OTF compiles deficiencies from all jurisdictions
Minor Engagement Deficiencies

- Departures from standards that, by themselves, would not cause an engagement to be substandard
Tone At The Top

- Objective is to promote a quality culture
- Firms must assign management responsibilities, so that financial reasons do not override quality of work
- Addresses personnel performance evaluation, compensation and advancement to demonstrate overarching commitment to quality
Engagement Quality Control Review

☐ Establish criteria to determine whether a review should be performed
☐ Evaluate all engagements against the criteria
☐ Establish procedures addressing nature, timing, extent and documentation of review
☐ Perform the review for engagements that meet the criteria and complete prior to release of report
Engagement Quality Control
Review Procedures

☐ Evaluate significant judgments and conclusions reached
☐ Read financial statements or other information and report to consider appropriateness of report
☐ Discuss significant findings and issues with engagement partner
☐ Extent of procedures is contingent on complexity and risk that the report might not be appropriate
Monitoring

- Asserting that QC policies and procedures are:
  - Relevant
  - Adequate
  - Operating effectively, and
  - Complied with in practice
Monitoring Requirements

- Ongoing evaluation to determine whether the QC system is properly designed and operates effectively
- Assign responsibility of oversight to a partner
- Assign performance to competent individuals
- Perform sufficiently comprehensive procedures
Monitoring Procedures

- Monitoring can be accomplished through various means:
  - Engagement quality control review
  - Post-issuance review of selected engagements
  - Inspections
Self-inspection (sole-proprietor)
- Not prohibited
- High risk of non-compliance that QC policies and procedures will not be detected
- Reviewers cannot rely on self-inspections
Communication Of Findings

☐ To those charged with governance
  ■ Deficiencies noted
  ■ Recommendations

☐ To relevant personnel
  ■ Results of monitoring at least annually
Complaints/Disagreements

☐ Provide open door for personnel to raise questions/concerns without fear of reprisal

☐ Document complaints and responses
Ethical Requirements

- We are facing huge challenges from market, governmental and internal forces
  - Reliability framework
  - Subjectivity
  - Overkill of government intrusion
- We must know and respect our standards
- Understand proper reporting and disclosure considerations
Ethical Requirements (Cont.)

☐ Know proper and value-oriented responses to ethical dilemmas
☐ What must I do?
  ■ Remember key points from Code of Professional Responsibility
    ☐ Fulfill responsibilities to all stakeholders
    ☐ Am I doing what a person with integrity would do?
    ☐ Avoid conflicts of interest in services rendered
Ethical Requirements (Cont.)

- Organizational ethics are driven by individual ethics
- Your behavior reflects your values and ethics, and those of our profession
- What you do – and how you respond – can make a difference
Common Peer Review Deficiencies
Areas Of Concern For Deficiencies

- Risk Assessment Standards
- SAS No. 115
- Fair value (SAS Nos. 115, 157 and 159)
- Recurring deficiencies
Regulatory Reviews Vs. Peer Reviews

- All meet the same objective
- Regulators’ approach is engagement-driven
- Peer review approach is system-driven
  - Forcing reviewers to link findings to system of quality control
  - Limits reliance on checklists (yes/no) and forces more interaction with firm
Risk Assessment Standards

- Improper audit planning – primary focus on “client/engagement acceptance/continuance form”
- Improper documentation of understanding of the entity and its environment including internal control
- Improper assessment of risk of material misstatement at all levels
- Improper linkage of risk assessment to tailoring of audit programs
Risk Assessment Standards (Cont.)

- Lack of documentation to support risk assessments

- Firm’s viewpoint of “no change” or “overkill” to risk assessment standards
SAS No. 115 Report

- Improper assessment of control deficiency, significant deficiency or material weakness
- Improper identification of deficiency as design or operational
- No follow-up on previous deficiencies communicated to management
- Lack of restriction on the use of the report
Fair Value

- Improper understanding of management’s assessment of nature, assumptions and factors

- Lack of documentation of work performed on fair value
Areas Firms Have Recurring Deficiencies

- AICPA PRB OTF identifies and compiles deficiency commonalities and patterns as part of its oversight visits
  - Report acceptance body (RAB) reviews and accepts submitted peer reviews
  - As part of oversight process, OTF compiles deficiencies from all jurisdictions
Minor Engagement
Deficiencies

- Departures from standards that, by themselves, would not cause an engagement to be substandard
Reports, Financial Statement Measurement, Presentation And Disclosure

☐ Supplemental information
  ■ Failure to report
  ■ Not clearly segregated or marked
  ■ Inconsistency of titles as presented on basic financial statements

☐ Report
  ■ Failure to reference all time periods
  ■ Failure to cover all periods by F/S but periods covered identified in F/S
Omitted or inadequate disclosures related to accounting policies, inventory, valuation allowances, long-term debt, related party transactions, concentration of credit risk

Incorrect use of F/S titles for basis of accounting used

Failure to accrue income taxes

Presentation of treasury stock in a state that does not recognize treasury stock

Incorrect reference to omission of GAAP-basis statements under OCBOA
Failure to refer to accountant’s report on each page of F/S

Failure to identify country of origin for GAAP in audit report
Audit Procedures And Documentation

- Failure to document assessment of control risk
- Not utilizing current audit programs
- Failure to evaluate “passed” adjustments
- Dating deficiencies between rep letters and/or attorney letters and last day of field work
Audit Procedures And Documentation (Cont.)

- Failure to document
  - Inspection of board minutes
  - Collectability of accounts receivable
  - Reportable conditions
  - Sample selection and results of sampling applications
- Failure to sign off on audit program steps
- Failure to have a firm license to practice
SSARS Procedures And Documentation

☐ SSARS No. 8 engagement letter did not refer to supplemental information

☐ Failure to comply QCS as it relates to work programs and/or reporting and disclosure checklist
Significant Engagement Deficiencies

- Matters material to understanding the report or F/S or represent critical auditing or SSARS procedures
  - Engagement with significant deficiency is considered “substandard”
  - Use judgment to form the conclusion
Reports, Financial Statement Measurement, Presentation And Disclosure

- Failure to qualify audit report for scope limitation or departure from basis of accounting
- Issuance of audit or review report when accountant is not independent
- Failure to issue a report on compliance and internal control under Governmental Auditing Standards
- Failure to disclose lack of independence in a compilation report
Reports, Financial Statement Measurement, Presentation And Disclosure (Cont.)

☐ Failure to disclose omission of substantially all disclosures
☐ Failure to disclose omission of statement of cash flows
☐ Failure to disclose OCBOA, if not readily determinable
☐ Failure to disclose a material departure from professional standards
Include or failure to include material balances not appropriate/appropriate for basis of accounting

Significant departures from financial statement formats prescribed by industry audit guides

Omission of disclosures related to significant accounting policies
Improper accounting of a material transaction
Misclassification of a material balance
Failure to segregate components of statement of cash flows
Omission of significant required disclosures
Failure to disclose cumulative effect of change in accounting principle
Omission of statement of income and retained earnings when referred in report
Audit Procedures And Documentation

- Failure to use a written audit program
- Failure to tailor audit programs specific to engagement or industry
- Failure to request a legal rep letter, if attorney was consulted
- Failure to obtain management rep letter
  - Failure to include significant components
Audit Procedures And Documentation (Cont.)

- Failure to document consideration of I/C structure
- Lack of documentation to substantiate key audit areas
- Failure to document test of controls and compliance for engagements subject to OMB A-133
- Failure to assess or document fraud risk
Audit Procedures And Documentation (Cont.)

- Failure to observe inventory or perform alternative procedures, if material
- Failure to assess level of materiality and control risk
- Failure to document analytical procedures
- Failure to review loan covenants
- Failure to document communications between successor and predecessor
Audit Procedures And Documentation (Cont.)

☐ Failure to perform review of subsequent events

☐ Failure to test unrecorded liabilities
SSARS Procedures And Documentation

- Failure to perform and/or document inquiry and analytical procedures
- Failure to obtain management rep letter
- SSARS 8 engagement letter does not include understanding that F/S are “for management’s use only”
Attestation Procedures And Documentation

- Failure to obtain management rep letter for examination of I/C
- Failure to obtain management rep letter on management’s assumptions for pro forma statements
- Failure to label pro forma financial information
Financial Statement Deficiencies

- Assets
  - Improper classification of current and long-term
  - Cash overdrafts shown as negative
  - Accounts receivable shown on cash basis F/S
  - Investments in debt and equity securities not classified or measured correctly
Financial Statement Deficiencies (Cont.)

- Liabilities
  - Improper classification of current and long-term
  - On-demand liabilities classified as long-term
  - Non-recognition of:
    - Compensated absences
    - Capital leases
Statement Of Income

- Income tax provision not recorded on interim F/S
- Reporting period not clearly identified
- Significant components of income tax expense not disclosed
Statement Of Cash Flows

- Components not properly segregated
  - Operating, investing and financing
- Misclassification of activities
- No disclosure of non-cash investing and financing activities
- No disclosure of interest and taxes paid for indirect method
  - Can be disclosed in notes to F/S
Statement Of Cash Flows (Cont.)

☐ Certain amounts do not agree with change in amounts from comparative balance sheets

☐ Statement not presented for each period of income statement presented
Functional Area Deficiencies

- Engagement performance
  - Failure to review working papers, report and F/S
  - Common areas of non-compliance with QC policy
    - Pre-issuance review
    - Disclosure and reporting checklist
    - Third-party A&A practice aids
    - Engagement letters
Functional Area Deficiencies (Cont.)

- Failure to consult professional literature or outside source for specialized industry or high-risk engagement
Functional Area Deficiencies (Cont.)

- Personnel management
  - Failure to take adequate CPE in A&A subjects and/or specialized industries, which resulted in deficiencies in engagements selected for review
Functional Area Deficiencies (Cont.)

- Monitoring
  - Failure to implement monitoring policies and procedures
  - Failure to document compliance with QC policies and procedures
  - Failure to perform annual inspection
  - Failure to extend monitoring to non-audit services (e.g. compilations and/or reviews)
Deficiencies In Specialized Industries

- Government Auditing Standards
  - I/C and compliance not prepared
  - Failure to include A-133 reports
  - Compliance and control tests do not support reports issued
  - Inadequate or outdated reference material used
  - F/S reports do not refer to I/C and compliance reports
Deficiencies In Specialized Industries (Cont.)

- Government Auditing Standards
  - Yellow Book CPE requirements not met
  - Improper accounting for a particular fund
  - Failure to restrict use of accountant’s report to proper oversight agency
  - Failure to apply GASBs
Deficiencies In Specialized Industries (Cont.)

- Not-for-profit organizations
  - Failure to apply FASB Nos. 116, 117 and 124
  - Failure to identify voluntary health and welfare
  - Improper accounting for restricted funds
  - Inadequate format, titles and presentation of F/S
Deficiencies In Specialized Industries (Cont.)

- Employee benefit plans
  - Inadequate testing of participant data and investments
  - Inadequate disclosures related to participant directed investment programs
  - Failure to understand testing requirements in a limited-scope engagement
  - Incomplete description of plan and provisions
Deficiencies In Specialized Industries (Cont.)

- Employee benefit plans
  - Inadequate or missing disclosures on investments and/or participant data
  - Failure to properly report on DOL limited-scope audit
  - Failure to report and/or include required supplement schedules
  - If member of a quality center, not retaining a reviewer that is a member as well
Deficiencies In Specialized Industries (Cont.)

- Common-interest realty associations (CIRAs)
  - Accounting policy for common property not disclosed
  - Required supplemental information not presented
  - Report does not indicate responsibility for required supplemental information
  - Disclosures for major repairs and replacements not included
Deficiencies In Specialized Industries (Cont.)

- Construction contractors
  - Failure to disclose accounting policies for construction revenue and construction-in-progress
  - Improper recognition methods for construction-in-progress
  - Improper classification and disclosure of billings, related costs and estimated revenue
  - Improper netting of account balances
Deficiencies In Specialized Industries (Cont.)

- Other Comprehensive Basis of Accounting (OCBOA)
  - Failure to disclose basis of accounting
  - Failure to state basis of presentation is a basis other than GAAP
  - Failure to modify report to reflect appropriate titles
  - Inadequate description of basis and how it differs from GAAP
Click here for a link to the revised AICPA Peer Review Standards: