

# AICPA Peer Review Program Compliance: Responding to Latest Developments

WEDNESDAY, MAY 31, 2017, 1:00-2:50 pm Eastern

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## *Tips for Optimal Quality*

FOR LIVE PROGRAM ONLY

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# AICPA Peer Review Program Compliance:

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May 31, 2017

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Mary E. MacKrell, CPA, Partner  
LCS&Z, Latham, N.Y.  
[mem@lcszcpa.com](mailto:mem@lcszcpa.com)

Alan Long, CPA, Managing Member  
Baldwin CPAS, Richmond, Ky.  
[alan.long@baldwincpas.com](mailto:alan.long@baldwincpas.com)

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# AICPA PEER REVIEW Program Compliance



G. Alan Long



**LCS&Z, L.L.P.**  
CERTIFIED PUBLIC ACCOUNTANTS AND CONSULTANTS

Mary E. MacKrell

# Employee Benefit Plan Engagements

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- No documentation of evaluation of SOC ® report.
- Failure to obtain sufficient appropriate audit evidence to provide reasonable assurance that fair value measurements (including appropriate leveling) and disclosures in the financial statements are in conformity with generally accepted accounting principles (GAAP).
- Overreliance on SOC® report. Missing testing included no specific testing of
  - Allocation of contributions.
  - Allocation of investment income.
  - Investment elections.

# Employee Benefit Plan Engagements

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- No testing of benefit payments or distributions.
- Lack of testing of eligibility.
- No direct confirmation of existence or valuation of investments in a full scope audit.
- Internal control documentation consisted of generic forms that contained no specific information about the auditee.
- No documentation identifying the parties-in-interest or consideration of any party-in-interest transactions to consider whether any prohibited transactions had occurred during the year under audit.

# Employee Benefit Plan Engagements

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- No documentation of testing of employer contributions.
- Inadequate testing of investment transactions or earning for a full scope audit.
- No documentation of procedures to test eligibility of active participants or comparing participant data used by the actuary to the plan sponsor records for a frozen plan.
- No testing of participant loans.
- No documentation of significant processes or internal control.



# Employee Benefit Plan Engagements

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- Audit programs missing for significant areas, including preliminary and final analytical review, related parties or parties in interest, allocations to participant accounts, fraud brainstorming, commitments or contingencies, subsequent events, and required communications with those charged with governance.
- Auditor's report was not modified based on missing participant data in accordance with DOL field assistance bulletin 2009-02.

# Employee Benefit Plan Engagements

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- Auditor's report indicated that the audit was performed and reported on the cash basis of accounting when it was actually performed under the modified cash basis of accounting. The required additional language was not included in the auditor's report.
- The risk assessment for all audit areas was low except for participant data and employee contributions, which was moderate with extended procedures. Extended procedures and the linkage to tests of controls were not documented in the working papers or the audit program in accordance with AU-C section 230, Audit Documentation (AICPA, Professional Standards).

# Single Audit/A-133 and Government Auditing Standards Engagements

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- Compliance requirements were documented as applicable, but no testing was performed for the compliance requirement.
- Lack of testing of internal controls over direct and material compliance requirements.
- Lack of documentation of skills, knowledge, or experience.
- Lack of documentation or incomplete documentation of risk assessment of Type A or Type B programs.

# Single Audit/A-133 and Government Auditing Standards Engagements

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- Lack of documentation supporting the assessment that compliance requirements were not applicable.
- No documentation of fraud risk regarding noncompliance for major programs.
- No documentation of internal control over preparation of SEFA.
- Schedule of Findings and Questioned cost did not contain all required elements.

# Single Audit/A-133 and Government Auditing Standards Engagements

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- Auditor provided a clean opinion on an entity that met the definition of a government but prepared their financial statement using FASB standards (instead of GASB standards).
- No materiality calculation on opinion units.
- No documentation of risk of managements override of controls.
- No documentation to support designation as a low risk auditee.

# Single Audit/A-133 and Government Auditing Standards Engagements

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- Type A program designated as low risk when it did not meet all of the requirements.
- Auditor's report on internal control did not include all required elements.
- The report on compliance with requirements applicable to each major program and internal controls over compliance did not contain all required elements.
- Data Collection Form did not properly summarize auditor's results.

# Single Audit/A-133 and Government Auditing Standards Engagements

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- Calculation of amounts tested as major programs was incorrect; amount of expenditures tested did not reach the required percentage for an entity that did not qualify as low-risk auditee.
- Federal program was part of a cluster and was not included in testing of major programs.
- Improper surplus cash calculation performed that led to the improper identification of noncompliance findings for HUD engagement.





# SOC 1®Engagement

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- The SOC 1®report was missing a critical elements in that it did not include a description of the system of controls provided by the service organization. The requirement for management to include this description is fundamental to AT section 801, Reporting on Controls at a Service Organization (AICPA, Professional Standards), as the assertion provided by management of the service organization and the opinion provided by the service auditor are attesting to and opining on the completeness and accuracy thereof; this component of the overall report is created to provide user auditors with an understanding of why the service auditor tested the specific controls that were tested.

# SOC 1® Engagement

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- Acknowledgements and assurances that the standard requires the auditor to obtain from the service organization during client acceptance were not obtained or documented. AT section 801.09 requires that the service auditor only accept the engagement when specific conditions exist, including several acknowledgements to be provided by management of the service organization.
- The extent of testing performed for numerous control activities was insufficient. Numerous instances were identified in which sample testing would appear to have been appropriate, yet the service auditor chose to perform observations, tests of one, or inquiry only. Inquiry only is insufficient to determine the operating effectiveness of controls.

# When A Review Has An A-133/ Uniform Guidance Engagement:

- Team captains are required to submit the following:
  - Profile sheet on the engagement
  - The Part A Checklist the reviewer prepares.
  - Program determination worksheet on Federal programs.

# SSARS 21 Impact on Peer Review

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- Failure to have correct reports will result in an engagement being considered non-conforming.
- Engagement letters not being corrected will result in a Matter for Further Consideration.

# System Reviews

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- The above will be evaluated to the systemic issue and then could be elevated to a finding or a deficiency.

# Engagement Reviews

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- Failure to have the correct report will result in a deficiency or a significant deficiency and a Pass with Deficiencies or fail report.
- Not having all the elements in the engagement letter will result in at least a finding.

# Peer Review Standards are Principle Based

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- One set of standards for all peer reviews
  1. This helps create uniformity.
- Clarifications that are more like the “rules” are in the interpretations
  1. Allows for more rapid guidance changes to allow peer review to adapt as standards change.

# Peer Review Integrates Management Application (PRIMA)

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- Web-based tool, to replace PRISM website.
- Will allow change and adaption quicker to the needs of practice monitoring.
- Updated functionality for the Public File, Reviewer Search and Facilitated State Board Access (FSBA) will be integrated into this new website, with access continuing to be available on the [aicpa.org](http://aicpa.org) website.
- Our expected launch timeframe is May 1, 2017.
- [Prima.aicpa.org](http://Prima.aicpa.org)



# Enhanced Oversight Have Shown Some Peer Review Weaknesses

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1. AICPA initiative in response to improving audit quality.
2. Reviews performed by “industry experts”.
3. Proved the DOL statistics as being correct.

# Peer Review Transparency

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1. If in one of the AICPA Audit Quality Centers peer review is in the public domain.
2. Facilitated State Board Access.
3. New Voluntary AICPA website.

# We Will Review

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- Documentation of System of Quality Control
- Elements of Quality Control and deficiencies
- Must vs Should
- Documentation issues
- Common findings and how to avoid them

# Quality Control System

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- Documented system of quality control is essential, form 4400 Quality Control Policies and Procedures is no longer sufficient.
- Free practice aid available on AICPA website for sole member and small-medium firms.
- The objective of a Quality Control (QC) system is to provide reasonable assurance that firm personnel comply with professional standards and that the reports issued are appropriate under the circumstances.
- QC system should include policies and procedures.

# Six Elements Of QC System

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- Tone at the top-promote a quality oriented culture
- Ethical requirements-protect independence, integrity and objectivity
- Acceptance and continuance-ensure independence and competence
- Human resources-ensure sufficient and well trained, ethical personnel
- Engagement performance-consistent performance, appropriate reports
- Monitoring-internal evaluation

# Customize Your Firm's QC System

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- Start with a templates or samples available see AICPA website, PPC other sources-but make sure to customize to your firm's needs.
  - Common finding:
    - EQCR- Engagement Quality Control Review
    - QC document should require that all engagements be evaluated against criteria for determining if the engagement should undergo EQCR.
    - EQCR must be performed on all engagements that meet the criteria and must be completed before the report is released
    - EQCR reviewer must have sufficient and appropriate experience and may not be a part of the engagement team.

# Monitoring

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- Monitoring is not only required but very helpful in finding exceptions prior to peer reviewer.
- Consider outside firm for monitoring
- Use peer review checklists-AICPA
- Make sure to test and document testing of all QC elements.
- Document findings and how those findings were communicated to firm, and how the system was changed to ensure deficiencies will not recur.

# QC Deficiencies

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- Practice aids out of date or not correctly completed
- EQCR not performed on engagements that meet the criteria
- No policy established for work paper retention
- CPE not complete and or appropriate
- Monitoring documentation not complete
- Annual independence confirmations
- Collect fees for prior years professional service prior to beginning current year- independence issue



# Must vs Should

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- **Unconditional requirements**– the auditor is required to comply with an unconditional requirements in all cases. The standards use **MUST** to indicate an unconditional requirement.
- **Presumptively mandatory requirements**- the auditor is required to comply with a presumptively mandatory requirement in all cases, however, in rare circumstances, the auditor may depart from a presumptively mandatory requirement. The standards use **SHOULD** to indicate a presumptively mandatory requirement.
- **Should consider**-auditor must document consideration.

# Must vs Should

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- **May, Might, Could** - procedures or actions require the auditor's attention and understanding; how and whether the auditor carries out such procedures or actions in the engagement depends on the exercise of professional judgment in the circumstances consistent with the objective of the standard. The words may, might, and could are used to describe these actions and procedures.

# Examples

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- The auditor **must** plan the audit to obtain sufficient, appropriate audit evidence about the financial statement assertions.
- The auditor is required **to consider** whether external confirmation procedures are to be performed as substantive audit procedures and **is required** to use external confirmation procedures for accounts receivable unless...
  - the overall account balance is immaterial,
  - external confirmation procedures would be ineffective, or
  - the auditor's assessed level of risk of material misstatement at the relevant assertion level is low, and the other planned substantive procedures address the assessed risk

# AU-C 300

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- **.07** The auditor **should** establish an overall audit strategy that sets the scope, timing, and direction of the audit and that guides the development of the audit plan.
- **.09** The auditor **should** develop an audit plan that includes a description of the following...
- **.10** The auditor **should** update and change the overall audit strategy and audit plan, as necessary, during the course of the audit. (Ref: par. .A15)
- **.11** The auditor **should** plan the nature, timing, and extent of direction and supervision of engagement team members and the review of their work. (Ref: par. .A16–.A17)

# AU-C 501.18

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- **Communication With the Entity's Legal Counsel**
- **.18** Unless the audit procedures required by paragraph .16 indicate that no actual or potential litigation, claims, or assessments that may give rise to a risk of material misstatement exist, the auditor **should**, in addition to the procedures required by other AU-C sections, seek direct communication with the entity's external legal counsel. The auditor should do so through a letter of inquiry prepared by management and sent by the auditor requesting the entity's external legal counsel to communicate directly with the auditor. (Ref: par. .A40 and .A46–.A63)
- **.20** The auditor **should** document the basis for any determination not to seek direct communication with the entity's legal counsel, as required by paragraphs .18–.19.

# Documentation Issues— Hot Topic!!

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- **Not documented = not done**
- One in four engagements is non-conforming because of poor documentation.
- Documentation must include sufficient appropriate audit evidence to support the report issued.
- An experienced auditor with no connection to the audit should be able to follow the procedures performed and the conclusions reached for each procedure performed to support the opinion issued.
- Nature, timing, extent and results of procedures.

# More Documentation

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- Documentation must include:
  - Planning and analytics
  - Understanding of client environment – corporate and IT
  - Internal control testing or document why controls will not be tested
  - Risk assessments
  - Audit strategy
  - Safeguards related to non-attest services and independence

# Testing Documentation

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- Documentation of sampling methodology
- Who tested, who reviewed and when?
- Objective of procedures performed and identifying characteristics of items tested
- Results of testing
- Conclusions reached



# Engagement Performance

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- Tests performed not responsive to risks identified
- Sample size not sufficient, or methodology not properly documented
- Insufficient documentation of understanding of system of internal controls and testing-



# SAS 99- Consideration of Fraud

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- The auditor has a responsibility to plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether caused by error or fraud.
  - Documentation of engagement team discussion to consider how the financial statements might be susceptible to fraud.-- brainstorming
  - Documentation of inquiries of management and others about the risk of fraud
  - Identify risks that may result in material misstatement due to fraud
  - Controls in place to mitigate risks
  - Documentation of an audit strategy that is responsive to the identified risks.

# Documentation of Independence and Non-attest Services

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- Non-attest services provided to audit clients, particularly with respect to evaluation and documentation of the sufficiency of the client's **skills, knowledge and experience (SKE)** to oversee the services.
- Client should designate an individual with appropriate SKE to oversee non-attest services, evaluate results and accept responsibility
- Document your assessment of designated individual's ability – they do not have to be able to perform the services, just understand them.

# Common Review Deficiencies

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- Reports
- Management representation letters
- Engagement letters
- Disclosures
- Documentation
- Engagement performance

# Reporting Deficiencies

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- Report dating
- Supplemental information—SSARS 23 changes
- Titles and headings
- Periods covered in report
- Omitted disclosures or statements of cash flow not mentioned
- Other matter paragraph when required

# Management Representation Letters

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- Dated same as related report
- Periods covered-Must include all periods covered in the report
- Stale language
- Include appropriate representations:
  - Legal contingencies
  - Representations related to type of entity, passed adjustments

# Engagement Letters

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- Failure to obtain an engagement letter
- Failure to use current required language and or elements
  - Preparation of financial statements must be included in engagement letter
  - Special purpose language
  - Include supplementary information



# Disclosures

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- Missing policy notes
- Debt note does not include all required elements
- Fair value:
  - Description of levels
  - Tabular presentation
  - Methods used to value
  - Fair value hierarchy of investments

# Disclosures

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- The election of the accounting alternative
- Related party activities
- Incorrect classification of items on statement of cash flow
- Using net amounts on long term cash flow changes
- Subsequent events note missing or improperly dated
- Tax related notes-deferred
- ASU 2015-03 Simplifying the presentation of long term debt is effective for 12/31/2016 engagements

# Make Peer Review An Opportunity

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- Build a relationship so that you can use your reviewer as a sounding board for technical questions
- Discuss any matters or findings in detail with your peer reviewer
- Talk about engagement and process efficiencies
- Respond fully and timely to all inquiries and requests

# Thank You

- G. Alan Long, CPA, CITP, CGMA
  - Email: [alan.long@baldwincpas.com](mailto:alan.long@baldwincpas.com)
  - Office Phone: 859.626.4962
  - Office Fax: 859.626.8522
- Mary E. MacKrell, CPA
  - Email: <mailto:MEM@lcszcpa.com>
  - Office Phone: 518.640.1415
  - Office Fax: 518.640.1465