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AICPA Professional Standards: Accounting and Review Standards as of June 1, 1980

American Institute of Certified Public Accountants. Accounting and Review Services Committee

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AICPA PROFESSIONAL
STANDARDS

VOLUME 1

AUDITING
MANAGEMENT ADVISORY
SERVICES
TAX PRACTICE
ACCOUNTING AND REVIEW
SERVICES

AS OF JUNE 1, 1980

ACCOUNTING AND REVIEW SERVICES

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AR Section

STATEMENTS ON STANDARDS FOR ACCOUNTING AND REVIEW SERVICES

Statements on Standards for Accounting and Review Services are issued by the AICPA Accounting and Review Services Committee, the senior technical committee of the Institute designated to issue pronouncements in connection with the unaudited financial statements or other unaudited financial information of a nonpublic entity. Council has designated the AICPA Accounting and Review Services Committee as a body to establish technical standards under Rule 204 of the Institute's Rules of Professional Conduct. Rule 204 requires adherence to those technical standards and requires that members be prepared to justify departures from them.

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AR Section 100**Compilation and Review of
Financial Statements**

Issue date, unless
otherwise indicated:
December, 1978

.01 This statement defines the *compilation of financial statements* and the *review of financial statements* of a nonpublic entity and provides guidance to accountants concerning the standards and procedures applicable to such engagements.¹ The accountant is required to issue a report whenever he completes a compilation or review of the financial statements of a nonpublic entity in compliance with the provisions of this statement. The accountant should not issue any report on the unaudited financial statements of a nonpublic entity or submit such financial statements to his client or others unless he complies with the provisions of this statement.

.02 The statement recognizes that accountants may perform other accounting services either in connection with the compilation or review of financial statements or as a separate service. The statement distinguishes such services from a compilation and from a review. The statement does not establish standards or procedures for such other accounting services, examples of which follow:

- a. Preparing a working trial balance.
- b. Assisting in adjusting the books of account.
- c. Consulting on accounting, tax, and similar matters.
- d. Preparing tax returns.
- e. Providing various manual or automated bookkeeping or data processing services unless the output is in the form of financial statements.
- f. Processing financial data for clients of other accounting firms.

General

.03 This statement provides guidance considered necessary to enable the accountant to comply with the general standards of the profession set forth in rule 201 [ET section 201.01] of the rules of conduct of the AICPA Code of Professional Ethics (see Appendix E) in the context of a compilation engagement or a review engagement and

1. Statements on auditing standards provide guidance to the accountant who performs services in connection with the unaudited financial statements of a public entity.

establishes additional standards deemed appropriate for such engagements.

Definitions

.04 Certain terms are defined for purposes of this statement as follows:

Nonpublic entity. A nonpublic entity is any entity other than (a) one whose securities trade in a public market either on a stock exchange (domestic or foreign) or in the over-the-counter market, including securities quoted only locally or regionally, (b) one that makes a filing with a regulatory agency in preparation for the sale of any class of its securities in a public market, or (c) a subsidiary, corporate joint venture, or other entity controlled by an entity covered by (a) or (b). [As amended, October, 1979 by Statement on Standards for Accounting and Review Services No. 2.] (See section 200.)

Financial statement. A presentation of financial data, including accompanying notes, derived from accounting records and intended to communicate an entity's economic resources or obligations at a point in time, or the changes therein for a period of time, in accordance with generally accepted accounting principles or a comprehensive basis of accounting other than generally accepted accounting principles.³ Financial forecasts, projections and similar presentations, and financial presentations included in tax returns are not financial statements for purposes of this statement. The following financial presentations are examples of financial statements:⁴

- Balance sheet.
- Statement of income.
- Statement of retained earnings.
- Statement of changes in financial position.
- Statement of changes in owners' equity.
- Statement of assets and liabilities (with or without owners' equity accounts).
- Statement of revenue and expenses.
- Summary of operations.
- Statement of operations by product lines.
- Statement of cash receipts and disbursements.

[2.] Footnote deleted.

3. The term *comprehensive basis of accounting other than generally accepted accounting principles* is defined in SAS no. 14, paragraph 4 [AU section 621.04]. Hereafter, reference to generally accepted accounting principles in this statement includes, where applicable, another comprehensive basis of accounting.

4. SAS no. 14, paragraph 7 [AU section 621.07], provides guidance with respect to suitable titles for financial statements that are prepared in conformity with a comprehensive basis of accounting other than generally accepted accounting principles.

A financial statement may be, for example, that of a corporation, a consolidated group of corporations, a combined group of affiliated entities, a not-for-profit organization, a government unit, an estate or trust, a partnership, a proprietorship, a segment of any of these, or an individual. The method of preparation (for example, manual or computer preparation) is not relevant to the definition of a financial statement.

Compilation of financial statements. Presenting in the form of financial statements⁵ information that is the representation of management (owners) without undertaking to express any assurance on the statements. (The accountant might consider it necessary to perform other accounting services to enable him to compile financial statements. See paragraph .11.)

Review of financial statements. Performing inquiry and analytical procedures that provide the accountant with a reasonable basis for expressing limited assurance that there are no material modifications that should be made to the statements in order for them to be in conformity with generally accepted accounting principles or, if applicable, with another comprehensive basis of accounting. (The accountant might consider it necessary to compile the financial statements or to perform other accounting services to enable him to perform a review. See paragraph .28.)

The objective of a review differs significantly from the objective of a compilation. The inquiry and analytical procedures performed in a review should provide the accountant with a reasonable basis for expressing limited assurance that there are no material modifications that should be made to the financial statements. No expression of assurance is contemplated in a compilation.

The objective of a review also differs significantly from the objective of an examination of financial statements in accordance with generally accepted auditing standards. The objective of an audit is to provide a reasonable basis for expressing an opinion regarding the financial statements taken as a whole. A review does not provide a basis for the expression of such an opinion because a review does not contemplate a study and evaluation of internal accounting control, tests of accounting records and of responses to inquiries by obtaining corroborating evidential matter through inspection, observation or confirmation, and certain other procedures ordinarily performed during an audit. A review may bring to the accountant's attention significant matters affecting the financial statements, but it does not provide assurance that the accountant

5. Paragraphs .19-.21 of this statement provide guidance to the accountant engaged to compile financial statements that omit substantially all of the disclosures required by generally accepted accounting principles or another comprehensive basis of accounting.

will become aware of all significant matters that would be disclosed in an audit.

The Accountant's Reporting Obligation

.05 Management, shareholders, credit grantors, and others who use financial statements should be able to readily identify the degree of responsibility, if any, the accountant is taking with respect to such financial statements. A written report is recognized by users of financial statements as the vehicle by which an accountant indicates that responsibility. Accordingly, whenever an accountant compiles or reviews financial statements of a nonpublic entity, he should issue a report prepared in accordance with the applicable standards in this statement. However, when the accountant performs more than one service (for example, a compilation and an audit), he should issue the report that is appropriate for the highest level of service rendered.

.06 An accountant should not consent to the use of his name in a document or written communication containing unaudited financial statements of a nonpublic entity unless (a) he has compiled or reviewed the financial statements and his report accompanies them, or (b) the financial statements are accompanied by an indication that the accountant has not compiled or reviewed the financial statements and that he assumes no responsibility for them. If an accountant becomes aware that his name has been used improperly in any client-prepared document containing unaudited financial statements, he should advise his client that the use of his name is inappropriate and should consider what other actions might be appropriate, including consultation with his attorney.

.07 The accountant should not submit unaudited financial statements of a nonpublic entity to his client or others unless, as a minimum, he complies with the provisions of this statement applicable to a compilation engagement. This precludes the accountant from merely typing or reproducing financial statements as an accommodation to his client.

Understanding With the Entity

.08 The accountant should establish an understanding with the entity, preferably in writing, regarding the services to be performed. The understanding should include a description of the nature and limitations of the services to be performed and a description of the report the accountant expects to render. The understanding should also provide (a) that the engagement cannot be relied upon to disclose errors, irregularities, or illegal acts and (b) that the accountant will inform the entity of any such matters that come to his

attention. Examples of engagement letters are presented in Appendixes B and C.

Compilation of Financial Statements

.09 Paragraphs .10-.22 provide additional guidance applicable to a compilation of financial statements.

.10 The accountant should possess a level of knowledge of the accounting principles and practices of the industry in which the entity operates that will enable him to compile financial statements that are appropriate in form for an entity operating in that industry.⁶ This standard does not prevent an accountant from accepting a compilation engagement for an entity in an industry with which the accountant has no previous experience. It does, however, place upon him a responsibility to obtain the required level of knowledge. He may do so, for example, by consulting AICPA guides, industry publications, financial statements of other entities in the industry, textbooks and periodicals, or individuals knowledgeable about the industry.

.11 To compile financial statements, the accountant should possess a general understanding of the nature of the entity's business transactions, the form of its accounting records, the stated qualifications of its accounting personnel, the accounting basis on which the financial statements are to be presented, and the form and content of the financial statements. The accountant ordinarily obtains knowledge of these matters through experience with the entity or inquiry of the entity's personnel. On the basis of that understanding, the accountant should consider whether it will be necessary to perform other accounting services, such as assistance in adjusting the books of account or consultation on accounting matters, when he compiles financial statements.

.12 The accountant is not required to make inquiries or perform other procedures to verify, corroborate, or review information supplied by the entity. However, the accountant may have made inquiries or performed other procedures (see paragraphs .02 and .11). The results of such inquiries or procedures, knowledge gained from prior engagements, or the financial statements on their face may cause the accountant to become aware that information supplied by the entity is incorrect, incomplete, or otherwise unsatisfactory for the purpose of compiling financial statements. (However, see paragraphs .19-.21 for guidance when management elects to omit substantially all of the disclosures required by generally accepted accounting principles.) In such circumstances, the accountant

6. For purposes of this statement, the term *industry* includes not-for-profit activities.

should obtain additional or revised information. If the entity refuses to provide additional or revised information, the accountant should withdraw from the compilation engagement. (See paragraphs .39-.41 for the accountant's responsibilities when he is aware of departures from generally accepted accounting principles.)

.13 Before issuing his report, the accountant should read the compiled financial statements and consider whether such financial statements appear to be appropriate in form and free from obvious material errors. In this context, the term *error* refers to mistakes in the compilation of financial statements, including arithmetical or clerical mistakes, and mistakes in the application of accounting principles, including inadequate disclosure.

Reporting on the Financial Statements

.14 Financial statements compiled without audit or review by an accountant should be accompanied by a report stating that—

- a. A compilation has been performed.
- b. A compilation is limited to presenting in the form of financial statements information that is the representation of management (owners).
- c. The financial statements have not been audited or reviewed and, accordingly, the accountant does not express an opinion or any other form of assurance on them.

Any other procedures that the accountant might have performed before or during the compilation engagement should not be described in his report.

.15 The date of completion of the compilation should be used as the date of the accountant's report.

.16 Each page of the financial statements compiled by the accountant should include a reference such as "See Accountant's Compilation Report."

.17 The following form of standard report is appropriate for a compilation:

The accompanying balance sheet of XYZ Company as of December 31, 19XX, and the related statements of income, retained earnings, and changes in financial position for the year then ended have been compiled by me (us).

A compilation is limited to presenting in the form of financial statements information that is the representation of management (owners). I (we) have not audited or reviewed the accompanying financial statements and, accordingly, do not express an opinion or any other form of assurance on them.

.18 An accountant may be asked to issue a compilation report on one financial statement, such as a balance sheet, and not on other related financial statements, such as the statements of income, retained earnings, and changes in financial position. This statement does not preclude the accountant from doing so.

Reporting on Financial Statements That Omit Substantially All Disclosures

.19 An entity may request an accountant to compile financial statements that omit substantially all of the disclosures required by generally accepted accounting principles, including disclosures that might appear in the body of the financial statements.⁷ (As previously noted, reference to generally accepted accounting principles in this statement includes, where applicable, another comprehensive basis of accounting.) The accountant may compile such financial statements provided the omission of substantially all disclosures is clearly indicated in his report and is not, to his knowledge, undertaken with the intention of misleading those who might reasonably be expected to use such financial statements. When the entity wishes to include disclosures about only a few matters in the form of notes to such financial statements, such disclosures should be labeled "Selected Information—Substantially All Disclosures Required by Generally Accepted Accounting Principles Are Not Included."

.20 Notwithstanding the above, if financial statements compiled in conformity with a comprehensive basis of accounting other than generally accepted accounting principles do not include disclosure of the basis of accounting used, the basis should be disclosed in the accountant's report.

.21 When financial statements that the accountant has compiled omit substantially all disclosures, the following form of standard report is appropriate:

The accompanying balance sheet of XYZ Company as of December 31, 19XX, and the related statements of income, retained earnings, and changes in financial position for the year then ended have been compiled by me (us).

A compilation is limited to presenting in the form of financial statements information that is the representation of management (owners). I (we) have not audited or reviewed the accompanying financial statements and, accordingly, do not express an opinion or any other form of assurance on them.

7. See paragraphs .39-.41 for the accountant's responsibilities when he is aware of other departures from generally accepted accounting principles.

Management has elected to omit substantially all of the disclosures (and the statement of changes in financial position) required by generally accepted accounting principles.⁸ If the omitted disclosures were included in the financial statements, they might influence the user's conclusions about the company's financial position, results of operations, and changes in financial position. Accordingly, these financial statements are not designed for those who are not informed about such matters.

Reporting When the Accountant Is Not Independent

.22 An accountant is not precluded from issuing a report with respect to his compilation of financial statements for an entity with respect to which he is not independent.⁹ If the accountant is not independent, he should specifically disclose the lack of independence. However, the reason for the lack of independence should not be described. When the accountant is not independent, he should include the following as the last paragraph of his report:

I am (we are) not independent with respect to XYZ Company.

Review of Financial Statements

.23 Paragraphs .24-.38 provide additional guidance applicable to a review of financial statements.

.24 The accountant should possess a level of knowledge of the accounting principles and practices of the industry in which the entity operates and an understanding of the entity's business¹⁰ that will provide him, through the performance of inquiry and analytical procedures, with a reasonable basis for expressing limited assurance that there are no material modifications that should be made to the financial statements in order for the statements to be in conformity with generally accepted accounting principles. (As previously noted, reference to generally accepted accounting principles in this statement includes, where applicable, another comprehensive basis of accounting.)

.25 The requirement that the accountant possess a level of knowledge of the accounting principles and practices of the industry in

8. If the statement of changes in financial position is omitted, the first and third paragraphs of the report should be modified accordingly.

9. In making a judgment about whether he is independent, the accountant should be guided by the AICPA Code of Professional Ethics. For example, the accountant should be aware that interpretation 101-3 under rule 101 [ET section 101.04] of the rules of conduct indicates that independence is not necessarily impaired when an accountant provides manual or automated bookkeeping or data processing services to a client.

10. For purposes of this statement, the term *business* includes not-for-profit entities.

which the entity operates does not prevent an accountant from accepting a review engagement for an entity in an industry with which the accountant has no previous experience. It does, however, place upon the accountant a responsibility to obtain the required level of knowledge. He may do so, for example, by consulting AICPA guides, industry publications, financial statements of other entities in the industry, textbooks and periodicals, or individuals knowledgeable about the industry.

.26 The accountant's understanding of the entity's business should include a general understanding of the entity's organization, its operating characteristics, and the nature of its assets, liabilities, revenues, and expenses. This would ordinarily involve a general knowledge of the entity's production, distribution, and compensation methods, types of products and services, operating locations, and material transactions with related parties. An accountant's understanding of an entity's business is ordinarily obtained through experience with the entity or its industry and inquiry of the entity's personnel.

.27 The accountant's inquiry and analytical procedures should ordinarily consist of the following:

- a. Inquiries concerning the entity's accounting principles and practices and the methods followed in applying them (see Appendix A).
- b. Inquiries concerning the entity's procedures for recording, classifying, and summarizing transactions, and accumulating information for disclosure in the financial statements (see Appendix A).
- c. Analytical procedures designed to identify relationships and individual items that appear to be unusual. For the purposes of this statement, analytical procedures consist of (1) comparison of the financial statements with statements for comparable prior period(s), (2) comparison of the financial statements with anticipated results, if available (for example, budgets and forecasts), and (3) study of the relationships of the elements of the financial statements that would be expected to conform to a predictable pattern based on the entity's experience. In applying these procedures, the accountant should consider the types of matters that required accounting adjustments in preceding periods. Examples of relationships of elements in financial statements that would be expected to conform to a predictable pattern may be the relationships between changes in sales and changes in accounts receivable and expense accounts that ordinarily fluctuate with sales, and between changes in property, plant, and equipment and changes in depreciation expense

and other accounts that may be affected, such as maintenance and repairs.

- d. Inquiries concerning actions taken at meetings of stockholders, board of directors, committees of the board of directors, or comparable meetings that may affect the financial statements.
- e. Reading the financial statements to consider, on the basis of information coming to the accountant's attention, whether the financial statements appear to conform with generally accepted accounting principles.
- f. Obtaining reports from other accountants, if any, who have been engaged to audit or review the financial statements of significant components of the reporting entity, its subsidiaries, and other investees.¹¹
- g. Inquiries of persons having responsibility for financial and accounting matters concerning (1) whether the financial statements have been prepared in conformity with generally accepted accounting principles consistently applied, (2) changes in the entity's business activities or accounting principles and practices, (3) matters as to which questions have arisen in the course of applying the foregoing procedures, and (4) events subsequent to the date of the financial statements that would have a material effect on the financial statements.

.28 Knowledge acquired in the performance of audits of the entity's financial statements, compilation of the financial statements, or other accounting services may result in modification of the review procedures described in the preceding paragraph. However, such modification would not reduce the degree of responsibility the accountant assumes with respect to the financial statements he has reviewed.

.29 A review does not contemplate a study and evaluation of internal accounting control, tests of accounting records and of responses to inquiries by obtaining corroborating evidential matter, and certain other procedures ordinarily performed during an audit. Thus, a review does not provide assurance that the accountant will become aware of all significant matters that would be disclosed in an audit. However, if the accountant becomes aware that infor-

11. The financial statements of the reporting entity ordinarily include an accounting for all significant components, such as unconsolidated subsidiaries and investees. If other accountants are engaged to audit or review the financial statements of such components, the accountant will require reports from other accountants as a basis, in part, for his report on his review of the financial statements of the reporting entity. The accountant may decide to make reference to the work of other accountants in his review report on the financial statements. If such reference is made, the report should indicate the magnitude of the portion of the financial statements audited or reviewed by the other accountants.

mation coming to his attention is incorrect, incomplete, or otherwise unsatisfactory, he should perform the additional procedures he deems necessary to achieve limited assurance that there are no material modifications that should be made to the financial statements in order for the statements to be in conformity with generally accepted accounting principles. (See paragraph .36 for guidance when an accountant is unable to complete a review and paragraphs .39-41 for the accountant's responsibilities when he is aware of departures from generally accepted accounting principles.)

.30 Although it is not possible to specify the form or content of the working papers that an accountant should prepare in connection with a review of financial statements because of the different circumstances of individual engagements, the accountant's working papers should describe—

- a. The matters covered in the accountant's inquiry and analytical procedures.
- b. Unusual matters that the accountant considered during the performance of the review, including their disposition.

.31 The accountant may wish to obtain a representation letter from the owner, manager, or chief executive officer, and, if appropriate, the chief financial officer. An example of a representation letter is presented in Appendix D.

Reporting on the Financial Statements

.32 Financial statements reviewed by an accountant should be accompanied by a report stating that—

- a. A review was performed in accordance with standards established by the American Institute of Certified Public Accountants.
- b. All information included in the financial statements is the representation of the management (owners) of the entity.
- c. A review consists principally of inquiries of company personnel and analytical procedures applied to financial data.
- d. A review is substantially less in scope than an audit, the objective of which is the expression of an opinion regarding the financial statements taken as a whole and, accordingly, no such opinion is expressed.
- e. The accountant is not aware of any material modifications that should be made to the financial statements in order for them to be in conformity with generally accepted accounting principles, other than those modifications, if any, indicated in his report.

Any other procedures that the accountant might have performed before or during the review engagement, including those performed in connection with a compilation of the financial statements, should not be described in his report.

.33 The date of completion of the accountant's inquiry and analytical procedures should be used as the date of his report.

.34 Each page of the financial statements reviewed by the accountant should include a reference such as "See Accountant's Review Report."

.35 The following form of standard report is appropriate for a review.¹²

I (we) have reviewed the accompanying balance sheet of XYZ Company as of December 31, 19XX, and the related statements of income, retained earnings, and changes in financial position for the year then ended, in accordance with standards established by the American Institute of Certified Public Accountants. All information included in these financial statements is the representation of the management (owners) of XYZ Company.

A review consists principally of inquiries of company personnel and analytical procedures applied to financial data. It is substantially less in scope than an examination in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, I (we) do not express such an opinion.

Based on my (our) review, I am (we are) not aware of any material modifications that should be made to the accompanying financial statements in order for them to be in conformity with generally accepted accounting principles.

.36 When an accountant is unable to perform the inquiry and analytical procedures he considers necessary to achieve the limited assurance contemplated by a review, his review will be incomplete. A review that is incomplete is not an adequate basis for issuing a review report. In such a situation, the accountant should consider whether the circumstances resulting in an incomplete review also preclude him from issuing a compilation report on the entity's financial statements. In making that judgment, the accountant should consider matters similar to those discussed in paragraphs .44-.49.

.37 An accountant may be asked to issue a review report on one financial statement, such as a balance sheet, and not on other related financial statements, such as the statements of income, retained earnings, and changes in financial position. He may do

12. See paragraphs .39-.41 for the accountant's responsibilities when he is aware of departures from generally accepted accounting principles.

so if the scope of his inquiry and analytical procedures has not been restricted.

.38 An accountant is precluded from issuing a review report on the financial statements of an entity with respect to which he is not independent.¹³ If the accountant is not independent, he may issue a compilation report provided he complies with the compilation standards.

Departures From Generally Accepted Accounting Principles

.39 An accountant who is engaged to compile or review financial statements may become aware of a departure from generally accepted accounting principles (which include adequate disclosure) that is material to the financial statements. (As noted previously, reference in this statement to generally accepted accounting principles includes, where applicable, another comprehensive basis of accounting.) Paragraphs .19-.21 provide guidance to the accountant when the departure relates to the omission of substantially all disclosures in the financial statements he has compiled. In all other circumstances, if the financial statements are not revised, the accountant should consider whether modification of his standard report is adequate to disclose the departure.

.40 If the accountant concludes that modification of his standard report is appropriate,¹⁴ the departure should be disclosed in a separate paragraph of his report, including disclosure of the effects of the departure on the financial statements if such effects have been determined by management or are known as the result of the accountant's procedures. The accountant is not required to determine the effects of a departure if management has not done so, provided the accountant states in his report that such determination has not been made. Examples of compilation and review reports that disclose departures from generally accepted accounting principles follow.

Compilation Report

The accompanying balance sheet of XYZ Company as of December 31, 19XX, and the related statements of income, retained earnings, and changes in financial position for the year then ended have been compiled by me (us).

13. See footnote 9.

14. Normally, neither an uncertainty nor an inconsistency in the application of accounting principles would cause the accountant to modify the standard report provided the financial statements appropriately disclose such matters. Nothing in this statement, however, is intended to preclude an accountant from emphasizing in a separate paragraph of his report a matter regarding the financial statements.

**Statements on Standards for Accounting and
Review Services**

A compilation is limited to presenting in the form of financial statements information that is the representation of management (owners). I (we) have not audited or reviewed the accompanying financial statements and, accordingly, do not express an opinion or any other form of assurance on them. However, I (we) did become aware of a departure (certain departures) from generally accepted accounting principles that is (are) described in the following paragraph(s).

(Separate paragraph)

As disclosed in note X to the financial statements, generally accepted accounting principles require that land be stated at cost. Management has informed me (us) that the company has stated its land at appraised value and that, if generally accepted accounting principles had been followed, the land account and stockholders' equity would have been decreased by \$500,000.

or

A statement of changes in financial position for the year ended December 31, 19XX, has not been presented. Generally accepted accounting principles require that such a statement be presented when financial statements purport to present financial position and results of operations.¹⁵

Review Report

I (we) have reviewed the accompanying balance sheet of XYZ Company as of December 31, 19XX, and the related statements of income, retained earnings, and changes in financial position for the year then ended, in accordance with standards established by the American Institute of Certified Public Accountants. All information included in these financial statements is the representation of the management (owners) of XYZ Company.

A review consists principally of inquiries of company personnel and analytical procedures applied to financial data. It is substantially less in scope than an examination in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, I (we) do not express such an opinion.

Based on my (our) review, with the exception of the matter(s) described in the following paragraph(s), I am (we are) not aware of any material modifications that should be made to the accompanying financial statements in order for them to be in conformity with generally accepted accounting principles.

(Separate paragraph)

As disclosed in note X to the financial statements, generally accepted accounting principles require that inventory cost consist of

15. If a statement of changes in financial position is not presented, the first paragraph of the compilation or review report should be modified accordingly.

material, labor, and overhead. Management has informed me (us) that the inventory of finished goods and work in process is stated in the accompanying financial statements at material and labor cost only, and that the effects of this departure from generally accepted accounting principles on financial position, results of operations, and changes in financial position have not been determined.

or

As disclosed in note X to the financial statements, the company has adopted (description of newly adopted method), whereas it previously used (description of previous method). Although the (description of newly adopted method) is in conformity with generally accepted accounting principles, the company does not appear to have reasonable justification for making a change as required by Opinion no. 20 of the Accounting Principles Board.

.41 If the accountant believes that modification of his standard report is not adequate to indicate the deficiencies in the financial statements taken as a whole, he should withdraw from the compilation or review engagement and provide no further services with respect to those financial statements. The accountant may wish to consult with his legal counsel in those circumstances.

Subsequent Discovery of Facts Existing at Date of Report

.42 Subsequent to the date of the report on the financial statements that the accountant has compiled or reviewed, he may become aware that facts may have existed at that date which might have caused him to believe that information supplied by the entity was incorrect, incomplete, or otherwise unsatisfactory had he then been aware of such facts. In such circumstances, the accountant may wish to consider the guidance in section 561 of Statement on Auditing Standards no. 1 [AU section 561] in determining an appropriate course of action, giving due consideration to the different objectives of compilation, review, and audit engagements. Because of the legal implications involved in actions contemplated under section 561 of SAS no. 1 [AU section 561], the accountant should consider consulting with his attorney.

Supplementary Information

.43 When the basic financial statements are accompanied by information presented for supplementary analysis purposes, the

accountant should clearly indicate the degree of responsibility, if any, he is taking with respect to such information. When the accountant has reviewed the basic financial statements, this may be accomplished by an explanation in his review report, or in a separate report on the other data, that the review has been made primarily for the purpose of expressing limited assurance that there are no material modifications that should be made to the financial statements in order for them to be in conformity with generally accepted accounting principles, and either

- a. The other data accompanying the financial statements are presented only for supplementary analysis purposes and have been subjected to the inquiry and analytical procedures applied in the review of the basic financial statements, and the accountant did not become aware of any material modifications that should be made to such data, or
- b. The other data accompanying the financial statements are presented only for supplementary analysis purposes and have not been subjected to the inquiry and analytical procedures applied in the review of the basic financial statements, but were compiled from information that is the representation of management, without audit or review, and the accountant does not express an opinion or any other form of assurance on such data.

When the accountant has compiled both the basic financial statements and other data presented only for supplementary analysis purposes, his compilation report should also include the other data.

Change in Engagement From Audit to Review or Compilation

.44 An accountant who has been engaged to examine the financial statements of a nonpublic entity in accordance with generally accepted auditing standards may, before the completion of his examination, be requested to change the engagement to a review or compilation of financial statements. A request to change the engagement may result from a change in circumstances affecting the entity's requirement for an audit, a misunderstanding as to the nature of an audit or the alternative review or compilation services originally available, or a restriction on the scope of the examination, whether imposed by the client or caused by circumstances.

.45 Before an accountant who was engaged to perform an examination in accordance with generally accepted auditing standards agrees to change the engagement to a review or compilation, at least the following should be considered:

- a. The reason given for the client's request, particularly the implications of a restriction on the scope of the examination, whether imposed by the client or by circumstances.
- b. The additional audit effort required to complete the examination.
- c. The estimated additional cost to complete the examination.

.46 A change in circumstances that affects the entity's requirement for an audit or a misunderstanding concerning the nature of an audit or the alternative review or compilation services originally available would ordinarily be considered a reasonable basis for requesting a change in the engagement.

.47 In considering the implications of a restriction on the scope of the examination, the accountant should evaluate the possibility that information affected by the scope restriction may be incorrect, incomplete, or otherwise unsatisfactory. Nevertheless, when the accountant has been prohibited by the client from corresponding with the entity's legal counsel, or when management (owners) has refused to sign a client representation letter, the accountant ordinarily would be precluded from issuing a review or compilation report on the financial statements.

.48 In all circumstances, if the auditing procedures are substantially complete or the cost to complete such procedures is relatively insignificant, the accountant should consider the propriety of accepting a change in the engagement.

.49 If the accountant concludes, based upon his professional judgment, that there is reasonable justification to change the engagement and if he complies with the standards applicable to the changed engagement, he should issue an appropriate review or compilation report. The report should not include reference to (a) the original engagement, (b) any auditing procedures that may have been performed, or (c) scope limitations that resulted in the changed engagement.

Comparative Financial Statements

[.50] [Superseded by Statement on Standards for Accounting and Review Services No. 2, effective for reports on comparative financial Statements for periods ending on or after November 30, 1979.] (See section 200.)

[16.] Footnote deleted.

Effective Date

.51 This statement will be effective for compilations and reviews of financial statements for periods ending on or after July 1, 1979.

APPENDIX A

**Review of Financial Statements —
Illustrative Inquiries****.52**

The inquiries to be made in a review of financial statements are a matter of the accountant's judgment. In determining his inquiries, an accountant may consider (a) the nature and materiality of the items, (b) the likelihood of misstatement, (c) knowledge obtained during current and previous engagements, (d) the stated qualifications of the entity's accounting personnel, (e) the extent to which a particular item is affected by management's judgment, and (f) inadequacies in the entity's underlying financial data. The following list of inquiries is for illustrative purposes only. The inquiries do not necessarily apply to every engagement, nor are they meant to be all-inclusive. This list is not intended to serve as a program or checklist in the conduct of a review; rather it describes the general areas in which inquiries might be made. For example, the accountant may feel it is necessary to make several inquiries to answer one of the questions listed below, such as item 3(a).

1. General
 - a. What are the procedures for recording, classifying, and summarizing transactions (relates to each section discussed below)?
 - b. Do the general ledger control accounts agree with subsidiary records (for example, receivables, inventories, investments, property and equipment, accounts payable, accrued expenses, non-current liabilities)?
 - c. Have accounting principles been applied on a consistent basis?
2. Cash
 - a. Have bank balances been reconciled with book balances?
 - b. Have old or unusual reconciling items between bank balances and book balances been reviewed and adjustments made where necessary?
 - c. Has a proper cutoff of cash transactions been made?
 - d. Are there any restrictions on the availability of cash balances?
 - e. Have cash funds been counted and reconciled with control accounts?
3. Receivables
 - a. Has an adequate allowance been made for doubtful accounts?
 - b. Have receivables considered uncollectible been written off?
 - c. If appropriate, has interest been reflected?
 - d. Has a proper cutoff of sales transactions been made?
 - e. Are there any receivables from employees and related parties?
 - f. Are any receivables pledged, discounted, or factored?
 - g. Have receivables been properly classified between current and noncurrent?

4. Inventories
 - a. Have inventories been physically counted? If not, how have inventories been determined?
 - b. Have general ledger control accounts been adjusted to agree with physical inventories?
 - c. If physical inventories are taken at a date other than the balance sheet date, what procedures were used to record changes in inventory between the date of the physical inventory and the balance sheet date?
 - d. Were consignments in or out considered in taking physical inventories?
 - e. What is the basis of valuation?
 - f. Does inventory cost include material, labor, and overhead where applicable?
 - g. Have write-downs for obsolescence or cost in excess of net realizable value been made?
 - h. Have proper cutoffs of purchases, goods in transit, and returned goods been made?
 - i. Are there any inventory encumbrances?
5. Prepaid Expenses
 - a. What is the nature of the amounts included in prepaid expenses?
 - b. How are these amounts amortized?
6. Investments, Including Loans, Mortgages, and Intercorporate Investments
 - a. Have gains and losses on disposal been reflected?
 - b. Has investment income been reflected?
 - c. Has appropriate consideration been given to the classification of investments between current and noncurrent, and the difference between the cost and market value of investments?
 - d. Have consolidation or equity accounting requirements been considered?
 - e. What is the basis of valuation of marketable equity securities?
 - f. Are investments unencumbered?
7. Property and Equipment
 - a. Have gains or losses on disposal of property or equipment been reflected?
 - b. What are the criteria for capitalization of property and equipment? Have such criteria been applied during the fiscal period?
 - c. Does the repairs and maintenance account only include items of an expense nature?
 - d. Are property and equipment stated at cost?
 - e. What are the depreciation methods and rates? Are they appropriate and consistent?
 - f. Are there any unrecorded additions, retirements, abandonments, sales, or trade-ins?
 - g. Does the entity have material lease agreements? Have they been properly reflected?

- d.* Do amounts of outstanding shares of capital stock agree with subsidiary records?
 - e.* Have capital stock preferences, if any, been disclosed?
 - f.* Have stock options been granted?
 - g.* Has the entity made any acquisitions of its own capital stock?
 - h.* Are there any restrictions on retained earnings or other capital?
14. Revenue and Expenses
- a.* Are revenues from the sale of major products and services recognized in the appropriate period?
 - b.* Are purchases and expenses recognized in the appropriate period and properly classified?
 - c.* Do the financial statements include discontinued operations or items that might be considered extraordinary?
15. Other
- a.* Are there any events that occurred after the end of the fiscal period that have a significant effect on the financial statements?
 - b.* Have actions taken at stockholder, board of directors, or comparable meetings that affect the financial statements been reflected?
 - c.* Have there been any material transactions between related parties?
 - d.* Are there any material uncertainties? Is there any change in the status of material uncertainties previously disclosed?

APPENDIX B

**Compilation of Financial Statements —
Illustrative Engagement Letter****.53**

(Appropriate Salutation)

This letter is to confirm our understanding of the terms and objectives of our engagement and the nature and limitations of the services we will provide.

We will perform the following services:

1. We will compile, from information you provide, the annual and interim balance sheets and related statements of income, retained earnings, and changes in financial position of XYZ Company for the year 19XX. We will not audit or review such financial statements. Our report on the annual financial statements of XYZ Company is presently expected to read as follows:

The accompanying balance sheet of XYZ Company as of December 31, 19XX, and the related statements of income, retained earnings, and changes in financial position for the year then ended have been compiled by us.

A compilation is limited to presenting in the form of financial statements information that is the representation of management. We have not audited or reviewed the accompanying financial statements and, accordingly, do not express an opinion or any other form of assurance on them.

Our report on your interim financial statements, which statements will omit substantially all disclosures, will include an additional paragraph that will read as follows:

Management has elected to omit substantially all of the disclosures required by generally accepted accounting principles. If the omitted disclosures were included in the financial statements, they might influence the user's conclusions about the company's financial position, results of operations, and changes in financial position. Accordingly, these financial statements are not designed for those who are not informed about such matters.

If, for any reason, we are unable to complete the compilation of your financial statements, we will not issue a report on such statements as a result of this engagement.

2. We will also . . . (discussion of other services).

Our engagement cannot be relied upon to disclose errors, irregularities, or illegal acts, including fraud or defalcations, that may exist. However, we will inform you of any such matters that come to our attention.

Our fees for these services. . . .

We shall be pleased to discuss this letter with you at any time.

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Review Services

If the foregoing is in accordance with your understanding, please sign the copy of this letter in the space provided and return it to us.*

Sincerely yours,

(Signature of accountant)

Acknowledge:
XYZ Company

President

Date

* Some accountants prefer not to obtain an acknowledgment, in which case their letter would omit the paragraph beginning "If the foregoing . . ." and the spaces for the acknowledgment. The first paragraph of their letter might begin as follows: "This letter sets forth our understanding of the terms and objectives of our engagement. . . ."

APPENDIX C

**Review of Financial Statements—
Illustrative Engagement Letter****.54**

(Appropriate Salutation)

This letter is to confirm our understanding of the terms and objectives of our engagement and the nature and limitations of the services we will provide.

We will perform the following services:

1. We will review the balance sheet of XYZ Company as of December 31, 19XX, and the related statements of income, retained earnings, and changes in financial position for the year then ended, in accordance with standards established by the American Institute of Certified Public Accountants. We will not perform an audit of such financial statements, the objective of which is the expression of an opinion regarding the financial statements taken as a whole, and, accordingly, we will not express such an opinion on them. Our report on the financial statements is presently expected to read as follows:

We have reviewed the accompanying balance sheet of XYZ Company as of December 31, 19XX, and the related statements of income, retained earnings, and changes in financial position for the year then ended, in accordance with standards established by the American Institute of Certified Public Accountants. All information included in these financial statements is the representation of the management of XYZ Company.

A review consists principally of inquiries of company personnel and analytical procedures applied to financial data. It is substantially less in scope than an examination in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our review, we are not aware of any material modifications that should be made to the accompanying financial statements in order for them to be in conformity with generally accepted accounting principles.

If, for any reason, we are unable to complete our review of your financial statements, we will not issue a report on such statements as a result of this engagement.

2. We will also . . . (discussion of other services).

Our engagement cannot be relied upon to disclose errors, irregularities, or illegal acts, including fraud or defalcations, that may exist. However, we will inform you of any such matters that come to our attention.

Our fees for these services. . . .

We shall be pleased to discuss this letter with you at any time.

Statements on Standards for Accounting and
Review Services

If the foregoing is in accordance with your understanding, please sign the copy of this letter in the space provided and return it to us.*

Sincerely yours,

(Signature of accountant)

Acknowledge:
XYZ Company

President

Date

* Some accountants prefer not to obtain an acknowledgment, in which case their letter would omit the paragraph beginning "If the foregoing . . ." and the spaces for the acknowledgment. The first paragraph of their letter might begin as follows: "This letter sets forth our understanding of the terms and objectives of our engagement. . . ."

APPENDIX D**Review of Financial Statements—
Illustrative Representation Letter****.55**

A review of financial statements consists principally of inquiries of company personnel and analytical procedures applied to financial data. Because a review does not contemplate tests of accounting records and of responses to inquiries by obtaining corroborating evidential matter, among other things, the accountant may consider it advisable to obtain a written representation from his client to confirm the oral representations made to him. The following representation letter is included for illustrative purposes only. The accountant may decide, based on the circumstances of his review engagement, that other matters should be specifically included in the letter and that some of the representations included in the illustrative letter are not necessary.

(Date of Accountant's Report)

(To the Accountant)

In connection with your review of the (identification of financial statements) of (name of client) as of (date) and for the (period of review) for the purpose of expressing limited assurance that there are no material modifications that should be made to the statements in order for them to be in conformity with generally accepted accounting principles, we confirm, to the best of our knowledge and belief, the following representations made to you during your review.

1. The financial statements referred to above present the financial position, results of operations, and changes in financial position of (name of client) in conformity with generally accepted accounting principles. In that connection, we specifically confirm that—
 - a. The company's accounting principles, and the practices and methods followed in applying them, are as disclosed in the financial statements.
 - b. There have been no changes during the (period reviewed) in the company's accounting principles and practices.
 - c. We have no plans or intentions that may materially affect the carrying value or classification of assets and liabilities.
 - d. There are no material transactions that have not been properly reflected in the financial statements.
 - e. There are no material losses (such as from obsolete inventory or purchase or sales commitments) that have not been properly accrued or disclosed in the financial statements.

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Review Services**

- f. There are no violations or possible violations of laws or regulations whose effects should be considered for disclosure in the financial statements or as a basis for recording a loss contingency, and there are no other material liabilities or gain or loss contingencies that are required to be accrued or disclosed.
 - g. The company has satisfactory title to all owned assets, and there are no liens or encumbrances on such assets nor has any asset been pledged.
 - h. There are no related party transactions or related amounts receivable or payable that have not been properly disclosed in the financial statements.
 - i. We have complied with all aspects of contractual agreements that would have a material effect on the financial statements in the event of noncompliance.
 - j. No events have occurred subsequent to the balance sheet date that would require adjustment to, or disclosure in, the financial statements.
2. We have advised you of all actions taken at meetings of stockholders, board of directors, and committees of the board of directors (or other similar bodies, as applicable) that may affect the financial statements.
3. We have responded fully to all inquiries made to us by you during your review.

(Name of Owner or Chief Executive
Officer and Title)

(Name of Chief Financial Officer and
Title, where applicable)

APPENDIX E

**Rule 201 of the Rules of Conduct of the AICPA
Code of Professional Ethics [ET section 201.01]**

.56

*Rule 201—General Standards.** A member shall comply with the following general standards as interpreted by bodies designated by Council, and must justify any departures therefrom.

- A. Professional competence. A member shall undertake only those engagements which he or his firm can reasonably expect to complete with professional competence.
- B. Due professional care. A member shall exercise due professional care in the performance of an engagement.
- C. Planning and supervision. A member shall adequately plan and supervise an engagement.
- D. Sufficient relevant data. A member shall obtain sufficient relevant data to afford a reasonable basis for conclusions or recommendations in relation to an engagement.
- E. Forecasts. A member shall not permit his name to be used in conjunction with any forecast of future transactions in a manner which may lead to the belief that the member vouches for the achievability of the forecast.

➤ *The next page is 3351.* ←

* The general standards of the profession are applicable to the performance of engagements in all major areas of accounting practice. However, the general standard of the profession entitled "Forecasts" is not applicable to compilation and review engagements because the scope of this statement, *Compilation and Review of Financial Statements*, does not include financial forecasts, projections, and similar presentations.

AR Section 200**Reporting on Comparative
Financial Statements**

Issue date, unless
otherwise indicated:
October, 1979

.01 This statement establishes standards for reporting on comparative financial statements¹ of a nonpublic entity when financial statements of one or more periods presented have been compiled or reviewed in accordance with SSARS 1 [section 100].²

.02 When comparative financial statements are presented, the accountant should issue an appropriate report(s) covering each period presented in accordance with the provisions of this statement.³

.03 Client-prepared financial statements of some periods that have not been audited, reviewed, or compiled may be presented on separate pages of a document that also contains financial statements of other periods on which the accountant has reported if they are accompanied by an indication by the client that the accountant has not audited, reviewed, or compiled those financial statements and that the accountant assumes no responsibility for them. Whenever the accountant becomes aware that financial statements of other periods that have not been audited, reviewed, or compiled have been presented in columnar form in a document with financial statements on which he has reported and that his name has been used or his report included in the document, he should advise his client that the use of his name or report is inappropriate and should consider what other actions might be appropriate, including consultation with his attorney.

1. This statement supersedes Statement on Standards for Accounting and Review Services 1, paragraph 50.

2. For purposes of this statement, a nonpublic entity is any entity other than (a) one whose securities trade in a public market either on a stock exchange (domestic or foreign) or in the over-the-counter market, including securities quoted only locally or regionally, (b) one that makes a filing with a regulatory agency in preparation for the sale of any class of its securities in a public market, or (c) a subsidiary, corporate joint venture, or other entity controlled by an entity covered by (a) or (b). This statement amends SSARS 1, paragraph 4 [section 100.04], by substituting the foregoing definition of a nonpublic entity. The terms *financial statements*, *compilation*, and *review* are defined in paragraph 4 of SSARS 1 [section 100.04].

3. See paragraphs .33 to .35 for guidance during the transition period when an accountant has previously issued a disclaimer of opinion in accordance with the provisions of SAS no. 26 [AU section 504].

.04 An accountant may modify his report with respect to one or more financial statements for one or more periods while issuing an unmodified report on the other financial statements presented.

.05 Compiled financial statements that omit substantially all of the disclosures required by generally accepted accounting principles⁴ are not comparable to financial statements that include such disclosures. Accordingly, the accountant should not issue a report on comparative financial statements when statements for one or more, but not all, of the periods presented omit substantially all of the disclosures required by generally accepted accounting principles. (See paragraphs .29 and .30 for guidance on reporting on financial statements that previously did not omit substantially all of the disclosures required by generally accepted accounting principles.)

.06 Each page of the comparative financial statements compiled or reviewed by the accountant should include a reference such as "See Accountant's Report."

Definitions

.07 The following definitions apply for purposes of this statement:

Comparative financial statements. Financial statements of two or more periods presented in columnar form.

Continuing accountant. An accountant who has been engaged to audit, review, or compile and report on the financial statements of the current period and one or more consecutive periods immediately prior to the current period.

Updated report. A report issued by a continuing accountant that takes into consideration information that he becomes aware of during his current engagement and that reexpresses his previous conclusions or, depending on the circumstances, expresses different conclusions on the financial statements of a prior period as of the date of his current report.⁵

Reissued report. A report issued subsequent to the date of the original report that bears the same date as the original report. A reissued report may need to be revised for the effects of specific events; in these circumstances, the report should be dual-dated with the original date and a separate date that applies to the effects of such events.

4. For purposes of this statement, reference to generally accepted accounting principles includes, where applicable, a comprehensive basis of accounting other than generally accepted accounting principles as defined in SAS no. 14, paragraph 4 [AU section 621.04].

5. See paragraphs 15 and 33 of SSARS 1 [sections 100.15 and 100.33].

Continuing Accountant's Standard Report

.08 A continuing accountant who performs the same or a higher level of service with respect to the financial statements of the current period should update his report on the financial statements of a prior period presented with those of the current period.⁶ A continuing accountant who performs a lower level of service with respect to the financial statements of the current period should either (a) include as a separate paragraph of his report a description of the responsibility assumed for the financial statements of the prior period (see paragraphs .11 and .12) or (b) reissue his report on the financial statements of the prior period.

.09 Examples of a continuing accountant's standard report on comparative financial statements when the same level of service has been performed for both periods are presented below:

Compilation Each Period

The accompanying balance sheets of XYZ Company as of December 31, 19X2 and 19X1, and the related statements of income, retained earnings, and changes in financial position for the years then ended have been compiled by me (us).

A compilation is limited to presenting in the form of financial statements information that is the representation of management (owners). I (we) have not audited or reviewed the accompanying financial statements and, accordingly, do not express an opinion or any other form of assurance on them.

February 1, 19X3

Review Each Period

I (we) have reviewed the accompanying balance sheets of XYZ Company as of December 31, 19X2 and 19X1, and the related statements of income, retained earnings, and changes in financial position for the years then ended, in accordance with standards established by the American Institute of Certified Public Accountants. All information included in these financial statements is the representation of the management (owners) of XYZ Company.

A review consists principally of inquiries of company personnel and analytical procedures applied to financial data. It is substantially less in scope than an examination in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, I (we) do not express such an opinion.

Based on my (our) reviews, I am (we are) not aware of any material modifications that should be made to the accompanying financial statements in order for them to be in conformity with generally accepted accounting principles.

March 1, 19X3

6. For purposes of this statement, a *review* is a higher level of service and a *compilation* is a lower level of service. When one of the periods is audited, see paragraphs .27 and .28.

.10 An example of a continuing accountant's standard report on comparative financial statements for two periods when the financial statements of the current period have been reviewed and those of the prior period have been compiled is presented below:

I (we) have reviewed the accompanying balance sheet of XYZ Company as of December 31, 19X2, and the related statements of income, retained earnings, and changes in financial position for the year then ended, in accordance with standards established by the American Institute of Certified Public Accountants. All information included in these financial statements is the representation of the management (owners) of XYZ Company.

A review consists principally of inquiries of company personnel and analytical procedures applied to financial data. It is substantially less in scope than an examination in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, I (we) do not express such an opinion.

Based on my (our) review, I am (we are) not aware of any material modifications that should be made to the 19X2 financial statements in order for them to be in conformity with generally accepted accounting principles.

The accompanying 19X1 financial statements of XYZ Company were compiled by me (us). A compilation is limited to presenting in the form of financial statements information that is the representation of management (owners). I (we) have not audited or reviewed the 19X1 financial statements and, accordingly, do not express an opinion or any other form of assurance on them.

March 1, 19X3

.11 A continuing accountant who performs a compilation of the current-period financial statements and has previously reviewed one or more prior-period financial statements should report as indicated in either (a) or (b) below:

- a. Issue a compilation report on the current-period financial statements that includes a description of the responsibility assumed for the financial statements of the prior period. The description should include the original date of the accountant's report and should also state that he has not performed any procedures in connection with that review engagement after that date.
- b. Combine his compilation report on the financial statements of the current period with his reissued review report on the financial statements of the prior period or present them separately. The combined report should state that the accountant has not performed any procedures in connection with that review engagement after the date of his review report.

.12 An example of a paragraph that may be added to a compilation report on the current-period financial statements describing the responsibilities assumed when prior-period financial statements were reviewed is presented below:

The accompanying 19X1 financial statements of XYZ Company were previously reviewed by me (us) and my (our) report dated March 1, 19X2, stated that I was (we were) not aware of any material modifications that should be made to those statements in order for them to be in conformity with generally accepted accounting principles. I (we) have not performed any procedures in connection with that review engagement after the date of my (our) report on the 19X1 financial statements.

Continuing Accountant's Changed Reference to a Departure from Generally Accepted Accounting Principles

.13 During his current engagement, the accountant should be aware that circumstances or events may affect the prior-period financial statements presented, including the adequacy of informative disclosures. The accountant should consider the effects on his report on the prior-period financial statements of circumstances or events coming to his attention.

.14 When the accountant's report on the financial statements of the prior period contains a changed reference to a departure from generally accepted accounting principles,⁷ his report should include a separate explanatory paragraph indicating—

- a. The date of the accountant's previous report.
- b. The circumstances or events that caused the reference to be changed.
- c. When applicable, that the financial statements of the prior period have been changed.

.15 The following is an example of an explanatory paragraph appropriate when an accountant's report contains a changed reference to a departure from generally accepted accounting principles:

In my (our) previous (compilation) (review) report dated March 1, 19X2, on the 19X1 financial statements, I (we) referred to a departure from generally accepted accounting principles because the company carried its land at appraised values. However, as disclosed in note X, the company has restated its 19X1 financial statements to reflect its land at cost in accordance with generally accepted accounting principles.

7. A changed reference includes the removal of a prior reference or the inclusion of a new reference.

Predecessor's Compilation or Review Report

.16 A predecessor may reissue his report at the client's request if he is able to make satisfactory arrangements with his former client and if he complies with the provisions of paragraphs .20 to .24. However, a predecessor is not required to reissue his compilation or review report on the financial statements of a prior period. If he does not reissue his compilation or review report on the financial statements of a prior period, a successor should either (a) make reference to the report of the predecessor in accordance with the provisions of paragraphs .17 to .19 or (b) perform a compilation, review, or audit of the financial statements of the prior period and report on them accordingly.⁸

Predecessor's Compilation or Review Report Not Presented

.17 When the financial statements of a prior period have been compiled or reviewed by a predecessor whose report is not presented and the successor has not compiled or reviewed those financial statements, the successor should make reference in an additional paragraph(s) of his report on the current-period financial statements to the predecessor's report on the prior-period financial statements. This reference should include the following matters:

- a. A statement that the financial statements of the prior period were
 - compiled or reviewed by another accountant (other accountants).⁹
- b. The date of his (their) report.
- c. A description of the standard form of disclaimer or limited assurance, as applicable, included in the report.
- d. A description or a quotation of any modifications of the standard report and of any paragraphs emphasizing a matter regarding the financial statements.

.18 When the predecessor reviewed the financial statements of the prior period, an example of the last paragraph of the successor's report is as follows:

The 19X1 financial statements of XYZ Company were reviewed by other accountants whose report dated March 1, 19X2, stated that they were not aware of any material modifications that should be made to those statements in order for them to be in conformity with generally accepted accounting principles.

8. The successor accountant may wish to consider the guidance in SAS no. 7 [AU section 315], *Communications Between Predecessor and Successor Auditors*, in determining what communications, if any, with the predecessor accountant are appropriate, giving due consideration to the different objectives of compilation, review, and audit engagements.

9. The successor should not name the predecessor in his report.

.19 When the predecessor compiled the financial statements of the prior period, an example of the last paragraph of the successor's report is as follows:

The 19X1 financial statements of XYZ Company were compiled by other accountants whose report dated February 1, 19X2, stated that they did not express an opinion or any other form of assurance on those statements.

Predecessor's Compilation or Review Report Reissued

.20 Before reissuing a compilation or review report on the financial statements of a prior period, a predecessor should consider whether his report is still appropriate. In making this determination, the predecessor should consider (a) the current form and manner of presentation of the prior-period financial statements, (b) subsequent events not previously known, and (c) changes in the financial statements that require the addition or deletion of modifications to the standard report.

.21 A predecessor should perform the following procedures before reissuing his compilation or review report on the financial statements of a prior period:

- a. Read the financial statements of the current period and the successor's report.
- b. Compare the prior-period financial statements with those previously issued and with those of the current period.
- c. Obtain a letter from the successor that indicates whether he is aware of any matter that, in his opinion, might have a material effect on the financial statements, including disclosures, reported on by the predecessor. The predecessor should not refer in his reissued report to this letter or to the report of the successor.

.22 If a predecessor becomes aware of information, including information about events or transactions occurring subsequent to the date of his previous report, that he believes may affect the prior-period financial statements or his report on them, he should (a) make inquiries or perform analytical procedures similar to those he would have performed if he had been aware of such information at the date of his report on the prior-period financial statements and (b) perform any other procedures he considers necessary in the circumstances. For example, the predecessor may wish to discuss this information with the successor or to review the working papers of the successor as they relate to the matters affecting the prior-period financial statements. If the predecessor decides, based on the information obtained, that his report on the prior-period financial statements

should be revised, he should follow the guidance in paragraphs .14, .15, .23, and .24.

.23 A predecessor's knowledge of the current affairs of his former client is obviously limited in the absence of a continuing relationship. Consequently, when reissuing his report on the prior-period financial statements, a predecessor should use the date of his previous report to avoid any implication that he has performed procedures after that date other than those described in paragraphs .20 to .22. If the predecessor revises his report or if the financial statements are restated, he should dual-date his report (for example, "March 1, 19X1, except for note X, as to which the date is March 15, 19X2"). The predecessor's responsibility for events occurring subsequent to the completion of his engagement is limited to the specific event referred to in the note or otherwise disclosed. He should also obtain a written statement from the former client setting forth the information currently acquired and its effect on the prior-period financial statements and, if applicable, expressing an understanding of its effect on the predecessor's reissued report.

.24 If a predecessor is unable to complete the procedures described in paragraphs .20 to .23, he should not reissue his report and may wish to consult with his attorney regarding the appropriate course of action.

Changed Prior-Period Financial Statements

.25 When the financial statements of the prior period have been changed, either the predecessor or the successor should report on them as restated. If the predecessor accepts the reporting obligation, he should follow the guidance in paragraphs .20 to .24. If the successor reports on the financial statements, he should comply with the compilation or review standards in SSARS 1 [section 100] (or perform an audit) with respect to such restated prior-period financial statements and report on them accordingly. If a successor reports on the restated financial statements, he should not refer in his report to the predecessor's previously issued report.

.26 If the restatement does not involve a change in accounting principles or their application (for example, the correction of an error), the accountant may wish to include an explanatory paragraph in his report with respect to the restatement, but he should not otherwise modify his standard report provided the financial statements appropriately disclose such matters.

Reporting When One Period Is Audited

.27 Notwithstanding the provisions of paragraph .08, the accountant should follow the guidance in statements on auditing standards, which provide guidance on reporting on comparative financial statements when the current-period financial statements have been audited and those for one or more prior periods have been compiled or reviewed.

.28 When the current-period financial statements of a nonpublic entity have been compiled or reviewed and those of the prior period have been audited, the accountant should issue an appropriate compilation or review report on the current-period financial statements and either (a) the report on the prior period should be reissued or (b) the report on the current period should include as a separate paragraph an appropriate description of the responsibility assumed for the financial statements of the prior period. In the latter case, the separate paragraph should indicate (a) that the financial statements of the prior period were examined previously, (b) the date of the previous report, (c) the type of opinion expressed previously, (d) if the opinion was other than unqualified, the substantive reasons therefor, and (e) that no auditing procedures were performed after the date of the previous report. An example of such a separate paragraph is the following:

The financial statements for the year ended December 31, 19X1, were examined by us (other accountants) and we (they) expressed an unqualified opinion on them in our (their) report dated March 1, 19X2, but we (they) have not performed any auditing procedures since that date.

Reporting on Financial Statements That Previously Did Not Omit Substantially All Disclosures

.29 An accountant who has compiled, reviewed, or audited financial statements that did not omit substantially all of the disclosures required by generally accepted accounting principles may subsequently be requested to compile statements for the same period that do omit substantially all of those disclosures when they are to be presented in comparative financial statements. Notwithstanding the provisions of SSARS 1, paragraph 5 [section 100.05], in these circumstances the accountant may report on comparative compiled financial statements that omit such disclosures if he includes in his report an additional paragraph indicating the nature of the previous service rendered with respect to those financial statements and the date of his previous report.

.30 An example of a report appropriate when prior-period financial statements that omit substantially all disclosures have been com-

piled from previously reviewed financial statements for the same period is presented below:

The accompanying balance sheets of XYZ Company as of December 31, 19X2 and 19X1, and the related statements of income, retained earnings, and changes in financial position for the years then ended have been compiled by me (us).

A compilation is limited to presenting in the form of financial statements information that is the representation of management (owners). I (we) have not audited or reviewed the accompanying financial statements and, accordingly, do not express an opinion or any other form of assurance on them.

Management has elected to omit substantially all of the disclosures required by generally accepted accounting principles. If the omitted disclosures were included in the financial statements, they might influence the user's conclusions about the company's financial position, results of operations, and changes in financial position. Accordingly, these financial statements are not designed for those who are not informed about such matters.

The accompanying 19X1 financial statements were compiled by me (us) from financial statements that did not omit substantially all of the disclosures required by generally accepted accounting principles and that I (we) previously reviewed as indicated in my (our) report dated March 1, 19X2.

February 1, 19X3

Change of Status — Public/Nonpublic Entity

.31 When reporting on comparative financial statements for either interim or annual periods, the current status of the entity should govern whether the accountant is guided by statements on auditing standards or statements on standards for accounting and review services. A previously issued report that is not appropriate for the current status of the entity should not be reissued or referred to in the report on the financial statements of the current period.

.32 For example, if the entity is a public entity in the current period and was a nonpublic entity in the prior period, a compilation or review report previously issued on the financial statements of the prior period should not be reissued or referred to in the report on the financial statements of the current and one or more prior periods.¹⁰ If an entity is a nonpublic entity in the current period and was a public entity in the prior period, the annual financial statements of the prior period

10. In these circumstances, the accountant should refer to statements on auditing standards for guidance on the appropriate method of reporting on the comparative financial statements.

may have been audited.¹¹ In these circumstances, the accountant should refer to paragraph .28 for guidance on the appropriate method of reporting on the comparative financial statements.

Transition

.33 A continuing accountant who previously issued a disclaimer of opinion in accordance with SAS no. 26 [AU section 504], on prior-period financial statements of a nonpublic entity that are presented with financial statements for periods ending on or after July 1, 1979, should either (a) reissue his previous report on such prior-period financial statements, (b) include in his report on the financial statements of the current period a description of the responsibility assumed with respect to the financial statements of the prior period, or (c) comply with the compilation or review standards in SSARS 1 [section 100] (or perform an audit) with respect to such prior-period financial statements and report on them accordingly.

.34 An example of the last paragraph of the accountant's report that describes the responsibility assumed for the financial statements of the prior period is as follows:

The 19X1 financial statements of XYZ Company were reported upon by me (us) in accordance with standards then in effect and my (our) report dated March 1, 19X2, stated that I (we) had not audited those financial statements and accordingly did not express an opinion on them.

.35 A predecessor accountant who previously issued a disclaimer of opinion in accordance with SAS no. 26 [AU section 504], on prior-period financial statements of a nonpublic entity that are presented with financial statements for periods ending on or after July 1, 1979, may reissue his previous report or may comply with the compilation or review standards in SSARS 1 [section 100] (or perform an audit) with respect to such prior-period financial statements and report on them accordingly. If the predecessor accountant does not reissue his previous report, the successor accountant should either refer to the predecessor accountant's previous report in his report on the financial statements of the current period or comply with the compilation or review standards in SSARS 1 [section 100] (or perform an

11. If an unaudited disclaimer of opinion was previously issued on the financial statements of the prior period, it should not be reissued or referred to in the report on the financial statements of the current period. In these circumstances, the accountant should comply with the compilation or review standards in SSARS 1 [section 100] (or perform an audit) and report accordingly on the financial statements of the prior period. (However, see also paragraphs .33 to .35 concerning reporting during the transition period.)

audit) with respect to such prior-period financial statements and report on them accordingly.

Effective Date

.36 This statement will be effective for reports on comparative financial statements for periods ending on or after November 30, 1979. However, earlier application is encouraged for periods ending on or after July 1, 1979.

➤ ***The next page is 3501.*** ←

AR Section 9000**ACCOUNTING AND REVIEW
SERVICES INTERPRETATIONS**

The staff of the Accounting and Review Services Committee has been authorized to issue interpretations to provide timely guidance on the application of pronouncements of the Accounting and Review Services Committee. Interpretations are reviewed by members of that Committee. An interpretation is not as authoritative as a pronouncement of the Accounting and Review Services Committee, but members should be aware that they may have to justify a departure from an interpretation if the quality of their work is questioned.

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AR Section 9100**Compilation and Review of Financial Statements: Accounting and Review Services Interpretations of AR Section 100****1. Omission of Disclosures in Reviewed Financial Statements**

.01 *Question*—Section 100.19—.21, “Compilation and Review of Financial Statements,” provide guidance to the accountant when a departure from generally accepted accounting principles relates to the omission of substantially all disclosures in the financial statements that he has compiled. Section 100.39 states that, in all other circumstances, an accountant should consider whether modification of his standard report is adequate to disclose a departure from generally accepted accounting principles. When a departure from generally accepted accounting principles relates to the omission of substantially all disclosures in financial statements that the accountant has reviewed, is disclosure of such omission in a separate paragraph of the accountant’s report similar to the example in section 100.21 an adequate modification of his report?

.02 *Interpretation*—No. The guidance in section 100.19—.21 only applies when financial statements that the accountant has *compiled* omit substantially all of the disclosures required by generally accepted accounting principles or another comprehensive basis of accounting. Because of the reporting requirements of section 100, an accountant ordinarily would not accept an engagement to review financial statements that omit substantially all of the disclosures required by generally accepted accounting principles. When an accountant who undertakes to *review* financial statements subsequently finds that his client declines to include substantially all required disclosures, his review report should include the disclosures omitted from the statements. However, if the information required to be disclosed has not been determined by management or is not known as the result of the accountant’s procedures, the accountant is not required to determine the specific information that should be disclosed. In that circumstance, the accountant’s report should specifically identify the nature of the omitted disclosures.

[Issue Date: December, 1979.]

2. Financial Statements Included in SEC Filings

.03 *Question*—Statements on Standards for Accounting and Review Services are applicable to the unaudited financial statements or other unaudited financial information of nonpublic entities (see definition in section 100.04, as amended by section 200.01, footnote 2). Unaudited financial statements of some entities that are nonpublic are occasionally included in documents filed with the Securities and Exchange Commission. For example, a nonpublic entity may be required to file unaudited financial statements in connection with the issuance of stock to an employee stock purchase plan or in connection with the sale of certain limited partnership units. Do the reporting requirements of section 100 apply in those circumstances?

.04 *Interpretation*—Deciding whether an entity is public or nonpublic for purposes of determining the applicability of section 100 should involve consideration of all relevant facts and the application of professional judgment. Professional standards do not eliminate the need for the exercise of professional judgment, since rules and definitions, no matter how carefully drawn, seldom cover every eventuality.

.05 In the circumstances described in this question, the accountant might note that the definition of a nonpublic entity contained in section 100, developed from the definition of a publicly traded company in APB Opinion No. 28 [AC section 2071], differs from the definition of a nonpublic enterprise in FASB Statement No. 21 [AC section 2083], which excludes any entity “that is required to file financial statements with the Securities and Exchange Commission.” This might lead the accountant to consider the significant responsibilities placed on independent accountants by the various securities acts. He might conclude that the users of unaudited financial statements included in documents filed with the SEC have objectives, needs, and expectations different from those of users of the unaudited financial statements of nonpublic entities that are not included in such filings. He might also conclude that communication with those users, because of the significance they attach to the regulatory and disciplinary responsibilities of the SEC, is not enhanced by including a compilation or review report in a document filed with the SEC, and might responsibly decide that the guidance in Statements on Auditing Standards is more appropriate in those circumstances.

[Issue Date: December, 1979]

3. Reporting on the Highest Level of Service

.06 *Question*—Sections 100.04 and 100.11, “Compilation and Review of Financial Statements,” recognize that an accountant may consider it necessary to perform other accounting services to enable him to compile financial statements. Section 100.05 provides that when an accountant performs more than one service with respect to the finan-

cial statements of an entity he should issue the report that is appropriate for the highest level of service rendered. Does section 100.05 require the accountant to evaluate the extent of other accounting services he has performed in a compilation engagement and to decide whether a review report should be issued instead of a compilation report?

.07 Interpretation—No. Section 100 requires the accountant to issue a report whenever he completes a compilation or review of the financial statements of a nonpublic entity. The statement that the accountant should issue a report that is appropriate for the highest level of service rendered is intended to make clear that if, for example, the accountant has both compiled and reviewed the financial statements that he was engaged to review, he would need to issue only a review report.

.08 Section 100 imposes no requirement for the accountant to “upgrade” his report because he has performed other accounting services. However, the accountant may wish to evaluate whether, as a result of performing such services, he is in a position to issue a review report when he was engaged only to perform a compilation. In such circumstances, he may wish to discuss the matter with his client and they may decide to revise their understanding regarding the nature of the services to be rendered.

.09 Question—An entity may wish to engage an accountant to compile financial statements each month and also to review the financial statements of the entity for a quarterly or an annual period. May an accountant issue a compilation report on the monthly financial statements and a review report on quarterly or annual financial statements for a period ending on the same date as one of the monthly financial statements?

.10 Interpretation—Yes. An accountant may accept an engagement to perform a compilation of financial statements for an interim period and an engagement to review the financial statements for another period that ends on the same date, provided he complies with the applicable standards for each engagement.

.11 Question—An accountant who has been engaged to compile or review the financial statements of an entity may also be requested to perform a higher level of service with respect to the same financial statements. Is the acceptance of such an engagement appropriate?

.12 Interpretation—Yes. Section 100 does not prohibit the accountant from accepting an engagement to perform a higher level of service with respect to financial statements that have been previously compiled or reviewed.

[Issue Date: December, 1979.]

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