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## ASB meeting minutes, 1999, April 14; Auditing Standards Board draft highlights, 1999, April 14

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## AUDITING STANDARDS BOARD

**Meeting:** Auditing Standards Board (ASB)

**Date:** April 14, 1999

**Location:** AICPA  
1211 Avenue of the Americas  
New York, NY

### Meeting

**Attendance:** Deborah D. Lambert, Chair  
John Barnum  
Andrew J. Capelli  
Robert F. Dacey  
Richard Dieter  
Sally L. Hoffman  
Stephen D. Holton  
J. Michael Inzina  
Charles E. Landes  
Keith O. Newton  
Alan Rosenthal  
Robert C. Steiner  
George H. Tucker  
Ray Whittington

### Absent

James S. Gerson, Vice Chair

### Other Participants

Barry Barber, Chair, Quality Control Task Force  
Susan Coffey, Vice President, Practice Monitoring  
Arleen R. Thomas, Vice President, Professional Standards and Services  
Thomas Ray, Director, Audit and Attest Standards  
David Brumeloe, Director, Practice Monitoring  
Julie Anne Dilley, Technical Manager, Audit and Attest Standards  
Gretchen Fischbach, Technical Manager, Audit and Attest Standards  
Jane M. Mancino, Technical Manager, Audit and Attest Standards  
Anthony Pugliese, Director, Assurance Services  
Judith M. Sherinsky, Technical Manager, Audit and Attest Standards

Observers

Joseph Bentz  
Gabriel de la Rosa  
Joanne Mary Flood  
Dave Frazier  
Deborah Koebele  
Jeffrey Thomson

**I. CHAIR'S REPORT**

Deborah D. Lambert, Chair, reported on the Audit Issues Task Force (AITF) meetings on February 16, March 18 and April 13, 1999 in New York. A summary of those meetings is attached.

**II. DIRECTOR'S REPORT**

Thomas Ray, AICPA Director, Audit and Attest Standards, reported on the following matters to the Auditing Standards Board.

1. The International Auditing Practices Committee (IAPC) of the International Federation of Accountants met in March.
  - The IAPC issued an International Auditing Practices Statement (IAPS), *Special Considerations in Audits of Small Enterprises*. IAPSs are designed to provide auditors of financial statements with practice guidance and are not intended to have the same authority as International Standards on Auditing.
  - The IAPC also voted to expose for comment a proposed International Standard on Assurance Services. This document is intended to be a framework for the provision of assurance services, including audits and reviews of financial statements and other services designed to provide assurance on financial and non-financial information. This redraft of an earlier exposure draft, *Reporting on the Credibility of Information*, resulted from significant international interest and comment on this project. The AICPA commented on the first exposure draft and is an active participant in the IAPC deliberations.
2. T. Ray participated in a meeting in London with representatives of the five largest auditing firms in the United Kingdom, staff of the UK's Auditing Practices Board, and the Director of Assurance Standards of the Canadian Institute of Chartered Accountants. The purpose of the meeting, which was organized by the UK staff as a part of its ongoing research efforts, was to discuss the firms' approach to considering the "control environment" and how an assessment of the control environment might affect other aspects of the audit. The results of

the meeting will be shared with the members of the international working group considering the audit risk model.

3. D. Lambert, J. Gerson, A. Thomas, Susan Coffey, AICPA Vice President, Practice Monitoring and SECPS, and T. Ray met to discuss the approach to the development of the quality control standards. The group believes it is appropriate for the Statements on Quality Control Standards to remain under the purview of the ASB. The group also believes that the ASB, in consultation with AICPA staff, should form a cross functional task force to prepare a strategic plan on the future development of the quality control standards and related guidance.
4. D. Lambert, R. Dieter, Arleen Thomas, AICPA Vice President, Professional Standards and Services, and T. Ray met with Lynn Turner, Chief Accountant, and Scott Bayless, Assistant Chief Accountant, of the Office of the Chief Accountant of the Securities and Exchange Commission (SEC), and Greg Corso, Special Counsel to the Chairman, SEC. The matters discussed included the ASB's plan to respond to the recommendations of the Blue Ribbon Committee on Audit Committee Effectiveness, initiatives regarding financial reporting materiality, and the development of guidance on auditing restructuring provisions and other unusual charges.

### III. AGENDA ITEMS PRESENTED AT MEETING

#### **Joint Task Force on Quality Control Standards**

Mr. Barry Barber, representing the Joint Task Force on Quality Control Standards, reported on the Task Force activities to date. Mr. Barber presented a proposed quality control standard (the "competency standard") that would incorporate certain requirements of the Uniform Accountancy Act into professional standards. The Task Force concluded that a qualitative approach to competencies was preferable.

After discussion, Ms. Lambert asked Board members to vote on the issuance of a proposed exposure draft concerning the competency standard. The Board voted unanimously to issue the exposure draft, subject to certain editorial revisions, with a 60-day comment period.

Mr. Barber also discussed a revision to Statement on Quality Control Standards (SQCS) No. 2. The Task Force proposed that this standard be revised to incorporate the SEC Practice Section's membership requirement concerning a second partner review of a SEC registrant's financial statements. Mr. Barber stated that the revision would require firms to adopt policies and procedures to adhere to the membership requirement, if applicable to the firm's practice.

After discussion, Ms. Lambert asked Board members to vote on the issuance of an exposure draft concerning the revision to SQCS No. 2, to be issued in conjunction with the proposed competency standard. The Board voted unanimously to issue the revision to SQCS No. 2 with the exposure draft on the proposed competency standard.

**Financial Instruments (File Ref. No. 2405)**

Stephen D. Holton, chair of the Financial Instruments Task Force, presented a revised draft of a proposed SAS titled *Auditing Financial Instruments*. The proposed SAS would supersede SAS No. 81, *Auditing Investments*. The scope of the new SAS includes all financial instruments; whereas, SAS No. 81 covers only (1) debt and equity securities, as that term is defined in FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities*, and (2) investments accounted for under APB Opinion No. 18, *The Equity Method of Accounting*. The November 1999 draft of the proposed SAS had been circulated to various AICPA industry committees for comment and revised to reflect some of those comments. The ASB recommended that—

- Paragraph 14 of the SAS, which addresses the subjectivity of the assumptions underlying assertions about financial instruments, be revised to state that competent persons could reach different conclusions as to the estimated fair value or range of fair values of a financial instrument.
- A footnote be added to paragraph 34 of the SAS referring the reader to Independence Standards Board Interpretation 99-1, “Impact on Auditor Independence of Assisting Clients in the Implementation of FAS 133.”

The ASB unanimously voted to ballot the draft for issuance as an exposure draft.

The task force is concurrently working on nonauthoritative implementation guidance that will serve as a companion to the SAS. The task force will present various issues related to that guidance at the June, July, and September 1999 ASB meetings.

## **ATTACHMENT TO HIGHLIGHTS OF ASB APRIL 14, 1999 MEETING**

### **Highlights of AITF Meeting held on February 16, 1999**

The Audit Issues Task Force (AITF) met on February 16, 1999 in New York. The following are highlights of that meeting:

#### ***Comment Letter on Proposed FDIC Statement of Policy***

The FASB 125 Audit Issues Task Force (task force) has drafted an ASB comment letter on the proposed FDIC *Statement of Policy Regarding Treatment of Securitizations and Loan Participations After Appointment of the Federal Deposit Insurance Corporation as Conservator or Receiver*. Deborah D. Lambert, Chair, AITF, led a discussion about the appropriate strategy for sharing the conclusions expressed in the comment letter with other interested groups prior to issuance of the letter. Tracey Barber, task force Chair, reported that task force representatives had been asked to meet with MBNA and representatives of major law firms. AITF members concluded that conference call meetings also should be arranged with representatives from the American Bar Association's Committee on Law and Accounting and the American Bankers Association prior to sending the comment letter. All of the meetings would include participation by representatives of the ASB, the task force, AICPA staff, and the AICPA Banking and Savings Institution Committee.

#### ***GASB Y2K Issue***

Participants discussed a proposed letter (ASB letter) drafted by James S. Gerson, AITF member, in response to a letter (GASB letter) that David R. Bean, Director of Research, Governmental Accounting Standards Board (GASB) had sent to Mary Foelster, Technical Manager, Professional Standards and Services. The GASB letter proposes that the GASB amend Technical Bulletin (TB) 98-1, *Disclosures about Year 2000 Issues*, to allow the required disclosures to be presented as required supplemental information (RSI) rather than as part of the financial statements. This would permit auditors to issue an unqualified opinion on the financial statements. In return, the letter asks the AICPA to eliminate or substantially modify its guidance to auditors that was issued on October 22, 1998. The guidance states that "sufficient audit evidence may not exist to support the required TB disclosures. Therefore, auditors may need to consider issuing qualified opinions (scope limitations) with respect to such disclosures."

The proposed ASB letter states that the ASB is pleased to have an opportunity to continue the dialogue with the GASB about these issues. It concurs that the placement of disclosures in RSI, an option that the ASB previously had proposed in a letter to the GASB dated December 7, 1998, rather than in the financial statements, would allow auditors to issue an unqualified opinion on the basic financial statements. However, if the Y2K disclosures are presented in RSI, auditors may determine that they are unable to perform the procedures required by professional standards on the RSI.

The draft ASB letter also proposes that the required disclosures be permitted elsewhere in the document containing the financial statements, such as in a transmittal letter, which would result in no report modifications. Disclosures presented outside the financial statements, and other than in RSI, would accomplish the objective of conveying information about the Year 2000 Issue to users of governmental financial statements and at the same time eliminate auditor association with the disclosures.

AITF participants suggested minor changes to the draft ASB letter.

### ***Government Materiality Issue***

J. Michael Inzina, member, ASB and M. Foelster led a discussion about proposed guidance on materiality in financial statements of governmental entities. A working group of Government Accounting and Auditing Committee (GAAC) and ASB members will be formed to draft such guidance, perhaps as an interpretation of SAS No. 47, *Audit Risk and Materiality in Conducting an Audit*. AITF participants agreed that guidance related to governmental entities should not be deferred pending a possible ASB project on qualitative materiality. AITF participants asked the working group to develop an issues paper for discussion at the March or April AITF meeting.

### ***GASB Infrastructure Project***

M. Inzina and M. Foelster led a discussion about the GASB's current plans regarding the reporting of infrastructure in governmental entities' financial statements under the new reporting model. The GASB tentatively has agreed to incorporate a "maintenance preservation approach" into infrastructure reporting which will require an assessment of the condition of the infrastructure assets. At the same time, the GASB recognizes that there does not appear to be one (or even several) methods of assessing the condition of infrastructure assets that is being used by different types of entities that will result in comparable condition assessments between entities. AITF participants voiced concerns about the auditability issues that may arise as a result. D. Lambert asked that proposed guidance that has been developed by the Attestable Criteria Task Force be sent to M. Foelster to share with the GASB and with members of GAAC who are monitoring issues relating to the GASB reporting model.

### ***SEC Letter to POB Panel***

Thomas Ray, Director, Audit and Attest Standards, led a discussion about a letter that was sent by the Securities and Exchange Commission (SEC) to the Public Oversight Board's Panel on Audit Effectiveness (Panel) regarding issues that the SEC feels that the Panel should address in its deliberations. He recommended that the AITF analyze the issues raised in this letter and in the Panel's proposed work plan and summary of potential issues and consider what the appropriate ASB action might be. He volunteered to draft an issues paper for discussion at the

March 18 AITF meeting. J. Gerson and George Tucker, AITF members, agreed to help draft the paper.

### ***Taxpayer Confidentiality Act***

Andrew Capelli, AITF member, led a discussion about the final draft of *Confidentiality Privileges Relating to Taxpayer Communications – Practice Guide* (Guide) that was issued in January 1999 by the AICPA’s Tax Division. The guidance includes a statement that the client should be asked to acknowledge that tax information shared with attest professionals who are not involved in the giving of the tax advice might cause a waiver of the Confidentiality Privilege. It also states that the practitioner should make the client aware of the possibility that the IRS may contend that use or communication of otherwise privileged information to or by the audit team results in a waiver of the privilege. The final section of the Guide is intended for distribution by the tax practitioner to his or her tax clients. That section includes a discussion concerning the possible waiver of the privilege when privileged information is used by auditors in auditing the financial statements, or when members of the audit team discuss matters that may affect the audit with firm personnel responsible for nonaudit services. AITF members agreed that the Guide adequately alerts the profession about the issues.

### ***Evaluation of Accounting Exposure Drafts for Auditability***

T. Ray noted that the staff of the POB’s Panel on Audit Effectiveness had raised a question about whether the ASB and Audit and Attest Standards staff should consider, as a routine matter, exposure drafts issued by accounting standards-setters for their auditability and provide comments as deemed necessary. A discussion followed regarding subject matter being difficult to audit as distinct from being not auditable. AITF participants noted that audit firms typically consider this matter in their own comment letters on accounting standards exposure drafts.

### ***Investment Performance Statistics Engagements Update***

Karyn Vincent, Chair, Investment Performance Statistics Task Force (task force), provided an update on the task force’s progress at its first two meetings. The task force focus to date has been on crafting a report for a “Level I” engagement where the practitioner attests to management’s assertion of firmwide compliance to Association of Investment Management and Research Performance Presentation Standards (AIMR-PPS<sup>TM</sup>). The AIMR representative on the task force has agreed to present to AIMR a list of selected “verification assertions” that the practitioner will test. AIMR in the meantime has exposed for comment its Global Investment Performance Standards (GIPS) which it expects to finalize early in 1999. Since the proposed GIPS verification guidelines differ from those in the current AIMR-PPS, the task force will wait for publication of the final GIPS and explore whether AIMR will amend the verification guidance in the AIMR-PPS to bring it more in conformity with GIPS.

### ***Y2K Update***



Richard Dieter, AITF member, distributed an e-mail message he had sent to D. Lambert regarding Y2K issues that may need to be considered in connection with December 31, 1999 audits. He also reported that representatives of the largest accounting firms will begin meeting in mid-March to discuss areas where guidance may be needed. D. Lambert requested that the AITF members receive an update on the issues at subsequent AITF meetings.

### ***Money Laundering***

T. Ray presented comment letters that the Financial Crimes Enforcement Network (FinCEN) of the Department of the Treasury had submitted on the exposure drafts of the Audit and Accounting Guides (AAGs) *Life and Health Insurance Entities* and *Audits of Investment Companies*. The comment letters recommend including guidance in the AAGs on the vulnerability of the respective industries to abuse by money launderers. The letters include a draft of recommended guidance.

AITF members discussed the comment letters and concluded that the AICPA should open a dialogue with FinCEN to discuss any modifications to the proposed guidance that may be required by professional standards. T. Ray will meet with Arleen Thomas, Vice President, Professional Standards & Services, and with George Dietz, Senior Manager, Audit and Accounting Guides, to discuss how to coordinate inclusion of such guidance in all the appropriate AAGs and in the Industry Risk Alerts.

### ***Report of Blue Ribbon Panel on Audit Committees***

AITF members discussed the recently issued recommendations of the Blue Ribbon Panel on Audit Committees. It was agreed that an ASB task force should be established to consider whether and what additional auditing guidance may be appropriate in response to the recommendations. Recommendations directed to the auditing profession include requirements that the auditor discuss with the audit committee—

- The auditor's judgments about the quality, not just the acceptability, of the company's accounting principles as applied in its financial reporting.
- The matters discussed in SAS No. 61, *Communications with Audit Committees*, pursuant to performing an interim review and prior to the filing of the company's Form 10-Q. This recommendation is incorporated into a recommendation to the SEC to require an interim review prior to filing of the company's Form 10-Q.

B. The AITF met on March 18, 1999 in New York. The following are highlights of that meeting.

### ***Responses to Fraud Research RFP***

Andrew Capelli and Jane Mancino provided an update on the responses to the RFP for research on SAS No. 82, *Consideration of Fraud in a Financial Statement Audit*, that had been received by the Fraud Standard Steering Task Force (task force). The task force received 25 responses to the RFP. Task force members were very impressed both with the thoughtfulness of the proposals and the quality of the researchers who submitted them. The task force has selected four proposals and recommends that the AITF approve the contracts when they are finalized (minor modifications of two of the selected proposals are being negotiated). Letters will be sent to researchers whose projects were not selected. Three proposals require a stipend of \$15,000 each. The fourth proposal will be done gratis, and is somewhat unique in that a model will be devised using input from forensic accountants to show how they identify indicators of fraud and how that process and the risk factors identified compare to SAS No. 82. Most of the research being done will rely on questionnaires that will be developed and sent to the firms. All projects will be completed, including submission of final reports, by January or February 2000. A press release has been drafted that will be issued by the AICPA shortly. AITF participants asked that copies of the selected proposals be sent to the ASB members.

#### ***Healthcare Corporate Integrity Agreement AUP Engagements***

Deborah D. Lambert, Chair, provided an update on the SOP, *Reporting on Management's Compliance with a Corporate Integrity Agreement entered into with the Office of Inspector General of the U.S. Department of Health and Human Services*, that had been submitted to the ASB for fatal flaw review. Two comments were received that have been addressed by the task force in the final SOP. One comment was that the practitioner needs to obtain an appropriate assertion from management regarding corporate compliance that is relevant to the procedures to be performed. An example of a statement of assertions is provided in the SOP. The other comment was to put a 90-day timeframe on the negative clearance period for receiving comments from OIG on the procedures.

#### ***POB Panel on Audit Effectiveness Update & Current Agenda Impact***

Thomas Ray, Director, Audit and Attest Standards, presented a paper that he prepared with James S. Gerson and George Tucker, AITF members, summarizing comments from various sources, including the Securities and Exchange Commission and the Public Oversight Board's Panel on Audit Effectiveness, about the effectiveness of the audit process. The paper identified possible ASB actions and initial recommendations regarding their disposition. It was observed that many of the matters identified are already being addressed within existing ASB projects. AITF members discussed each item and decided to undertake the following additional actions.

- Establish a working group to consider firm policies and practices on audit documentation and develop recommendations. In conjunction with this, the Technical Audit Advisors Task Force will develop a paper summarizing existing documentation requirements in the professional standards.

- Establish a working group to consider whether guidance on auditing management's intent, such as that provided in SAS No. 81 with regard to investments, is needed in other areas such as restructurings.
- Maintain the dialogue with the Panel on Audit Effectiveness to keep apprised of the Panel's concerns and to provide updated information to the Panel on ASB actions and initiatives. Members of the Panel's Staff will be invited to the April 13 AITF meeting.

### ***GASB Y2K Update***

D. Lambert, T. Ray, and Mary Foelster, Technical Manager, Professional Standards and Services, led a discussion about a proposed ASB comment letter to the GASB and related proposed guidance to auditors concerning the option of governmental entities to report Year 2000 disclosures in required supplementary information (RSI) rather than in notes to the financial statements.

AITF participants discussed the draft guidance to auditors that illustrates various report language options when a governmental entity includes the required Year 2000 disclosures in RSI, and guidance relating to reissuance of financial statements upon the retroactive application of the proposed TB. The guidance will be posted on the AICPA Web site upon issuance of the GASB Technical Bulletin.

**AITF members recommended several changes to the draft guidance. The changes will be made and submitted on March 19 to the AITF members for their final comments. Comments will be sent to M. Foelster or T. Ray no later than Tuesday, March 23.**

### ***Draft Outline of Comment Letter on SEC "Aircraft Carrier" Proposal***

Amelia A. Ripepi, member, SEC Regulations Committee (Committee), presented a draft outline of a comment letter prepared by the Committee on the Securities and Exchange Commission Notice of Proposed Rulemaking (Release No. 33-7606), *The Regulation of Securities Offerings* (the Release). Anne Schumacher-Barr, Technical Manager, Professional Standards & Services, and Ian MacKay, Director – Regulated Services, also participated. The purpose of the proposed Release, also termed the "aircraft carrier" proposal because of its length, is to eliminate unnecessary obstacles to capital formation while improving the quality and timing of disclosure. AITF members were asked to express their views about specific auditing matters addressed in the proposed comment letter. The following were among the AITF comments:

- The SEC should develop objective criteria to identify "issuers that appear more likely to face potentially significant liquidity problems" who would be prohibited from designating the

effective date of their registration statements. The AITF objected to any suggestion that the SEC rules refer to the criteria in SAS 59 for this purpose.

- The letter should comment positively on SAS 71 reviews and SSAE engagements on MD&A but in the context of investor protection, not underwriter due diligence defenses. It also is not clear what the SEC intends by “a report issued by a qualified independent professional on whether any non-expertized disclosures in the annual report were untrue...” or why anyone would issue such a report.
- The proposed responses on whether management should be required to file a report addressed to its audit committee which would disclose the procedures, if any, established by management to assure the accuracy and adequacy of Exchange Act reports should be reviewed for consistency with prior AICPA releases related to this matter.
- Accelerating the timeframe for reporting a change in auditor to one day, or reporting of the withdrawal of an audit report or withholding a consent to within one day of notification, is not feasible.

AITF members Richard Dieter and J. Gerson agreed to clear the draft of the comment letter on behalf of the ASB when the letter has been revised to incorporate comments received.

### ***Task Force Assignments & Project Scheduling***

T. Ray distributed a schedule of task force assignments and project scheduling that he and D. Lambert had prepared. AITF participants recommended some changes, including giving the Technical Audit Advisors Task Force the responsibility for drafting a summary of the documentation requirements in the professional standards. D. Lambert asked that a request be sent to all task force chairs to write task force charges and to develop project timetables (to the extent feasible) by the April 13 AITF meeting.

### ***ASB Project Timetable***

Lambert asked that the Financial Instruments Task Force’s proposed SAS be scheduled as the first and last agenda items at the ASB’s April 14-15 meeting to facilitate balloting of an exposure draft at that meeting. A proposed SSAE being drafted by the Attestation Recodification II Task Force also will be discussed. G. Fischbach will follow up on whether the proposed Quality Control standard being drafted by the Joint Task Force on Quality Control Standards will be available for discussion at the April meeting.

**C. The AITF met on April 13, 1999 in New York. The following are highlights of that meeting.**

### ***Task Force Charges and ASB Project Timetable***

Deborah D. Lambert, ASB chair, Richard Dieter, ASB member, Thomas Ray, Director, Audit and Attest Standards, and Arleen Thomas, Vice President, Professional Standards and Services, met on April 12 with Lynn Turner, Chief Accountant, and Scott Bayless, Assistant Chief Accountant, of the Office of the Chief Accountant of the Securities and Exchange Commission (SEC) and Greg Corso, Special Counsel to the Chairman, SEC. T. Ray summarized topics discussed at the meeting as follows:

- Pursuant to recommendations of the Blue Ribbon Committee (Committee) on Improving the Effectiveness of Corporate Audit Committees—
  - The SEC is in the process of formulating a rule to require a timely quarterly review.
  - An ASB task force has been formed to consider recommendations that auditors be required to discuss with the audit committee: (1) judgments about the quality, not just the acceptability, of the company's accounting principles as applied in its financial reporting and (2) the matters described in SAS No. 61, *Communications with Audit Committees*, pursuant to performing an interim review. Robert Steiner, AITF member, will chair this task force.
- The SEC will be issuing Staff Accounting Bulletins (SABs) on restructuring reserves, materiality, and revenue recognition. An ASB Steering task force has been formed to oversee the development of guidance for auditing revenues of industries that are not the subject of existing AICPA Audit and Accounting Guides. R. Steiner will chair this task force. The AITF will consider other appropriate ASB action on restructuring reserves and on materiality when the SABs on those topics are released.
- The AITF will have a liaison meeting with the SEC on May 10 to discuss other current ASB activities.

AITF members discussed drafts of new and revised task force objectives prepared by task force chairs and Audit and Attest Standards staff. Participants also established the timetable for various projects and recommended that the ASB Project Timeline be expanded to include all ASB task forces and working groups whether or not their objective is standards-level guidance.

Finally, the AITF discussed the timing and proposed review process for nonauthoritative practice guidance that will be released simultaneous with the proposed SAS, *Auditing Financial Instruments*, and with the proposed amendments to the Attestation Standards that are being drafted.

#### ***Update on GAO Advisory Council***

Ian MacKay, Director—Regulated Services, and Mary Foelster, Technical Manager, Professional Standards and Services, provided an update on the recent activity of the Advisory Council (Council) on Government Auditing Standards of the Government Accounting Office

(GAO). Several meetings of AICPA and GAO representatives have been held since January to discuss matters including the GAO/AICPA standard-setting relationship and the ASB's comment letters on two recent GAO exposure drafts, *Additional Documentation Requirements When Assessing Control Risk at Maximum for Computer-Related Controls*, and *Auditor Communication*.

The Council met in February and approved the exposure draft on EDP controls (consideration of the other exposure draft was deferred until the next meeting). Council members also submitted issues that they believe should be added to the Council's technical agenda. Many of the proposed projects have the potential for overlap with ASB projects.

AITF members agreed that increased communication with the Council and GAO staff would be mutually beneficial. Richard C. Tracy, new Council chair, will be invited to an ASB meeting to brief the ASB on the Council agenda, and D. Lambert similarly offered to update the Council on ASB initiatives at a future Council meeting. D. Lambert and T. Ray will keep apprised of ongoing activities via conference calls with the AICPA representatives on the Council. Council members will be included on the mailing lists for highlights of various AICPA Committees, including the ASB. I. MacKay also suggested that GAO staff be invited to the Continuous Auditing roundtable.

### ***GASB Planning Issues***

D. Lambert and T. Ray led a discussion about the recent communications with the Governmental Accounting Standards Board (GASB) regarding the exposure draft of Technical Bulletin (TB) No. 99-1, *Disclosures about Year 2000 Issues – an amendment of Technical Bulletin 98-1*, and the ASB guidance to auditors that was issued in response to the TB.

AITF members proposed that the ASB draft a letter addressed to all members of the GASB reiterating concerns expressed by members of the Government Accounting and Auditing Committee (GAAC) at its March meeting with the GASB about the auditability of infrastructure criteria and about materiality issues related to the upcoming issuance of a standard on the proposed model. GAAC's comment letter and various other communications with the GASB on the reporting model will be reviewed prior to drafting this letter.

J. Michael Inzina and M. Foelster will present recommendations of the working group on materiality in governmental reporting to the AITF at its May 10 meeting.

### ***Reporting on NPO Comparative Financial Statements***

Gregory B. Capin, Chair, Not-for-Profit Organizations Committee, and Joel M. Tanenbaum, Technical Manager, Accounting Standards, led a discussion about a practice issue regarding the appropriate auditor's report for comparative financial statements of a not-for-profit entity when the prior-year balance sheet and statement of cash flows are full presentations in conformity with

GAAP but the statement of activities is not presented in conformity with GAAP because it includes amounts in total rather than by net asset class.

AITF participants concluded that a continuing auditor should follow the guidance in AU section 552, *Reporting on Condensed Financial Statements and Selected Financial Data*, paragraphs .05-.06, and indicate that the prior year financial statements were audited, the date of the report, the type of opinion expressed, and whether the summarized information is fairly stated in relation to the financial statements from which it has been derived. The entity also should include a note in the financial statements fully describing the nature of the prior-period information. An example of an appropriate note is contained in paragraph 3.21 of the AICPA Audit and Accounting Guide, *Not-for-Profit Organizations*. AITF participants also agreed that if an entity wants the auditor to opine on comparative financial statements, then the full set of financial statements for the prior year should be presentations in conformity with GAAP.

J. Tanenbaum will draft revised guidance for the AICPA Audit and Accounting Guide, *Not-for-Profit Organizations*, before the current revision is published. Charles Landes, AITF member, R. Dieter, and T. Ray agreed to review the draft guidance. The guidance will be publicized through *The CPA Letter*, the Audit Risk Alert, the upcoming AICPA Not-for-Profit Conference, and the AICPA Web site.

### ***NPO Reporting Issue Regarding Consistency***

G. Capin and J. Tanenbaum led a discussion about a practice issue that will arise for auditors reporting on financial statement of not-for-profit entities pursuant to the adoption of SOP 98-2, *Accounting for Costs of Activities of Not-for-Profit Organizations and State and Local Governmental Entities That Include Fund Raising*, which is effective for financial statements for years beginning on or after December 15, 1998. AITF participants were asked to consider whether the implementation of SOP 98-2 is a change in accounting principle that requires an explanatory paragraph in the auditor's report, or a reclassification of amounts that does not require an explanatory paragraph.

AITF members agreed that if implementation of the SOP affects the comparability of the amounts reported as program expense, management and general expense, and fundraising expense, and the effect is material, then the auditor should include an explanatory paragraph in his or her report referring to the change in accounting principle. J. Tanenbaum will draft an AITF Advisory to communicate this guidance to the profession.

### ***IT Impact on Standards***

George H. Tucker, member, presented a discussion paper that he had prepared on how the growing use of information technology and paperless systems present auditing questions that are not addressed by AU section 326, *Evidential Matter*, AU section 319, *Consideration of Internal*

*Control in a Financial Statement Audit*, and AU section 350, *Audit Sampling*, when considered as a whole.

AITF members agreed that a task force should be established to address the impact of technology on the standards that are raised in this paper and in the recommendations presented to the ASB by the Computer Auditing Subcommittee (CAS) at the ASB's December meeting. A task force will be formed with members from the ASB, CAS, the Technical Audit Advisors Task Force and the SAS 70 Task Force.

### ***Financial Instruments***

Stephen Holton, Chair, Financial Instruments task force, provided an update on comments received from various AICPA committees to whom he had sent a draft of the proposed SAS, *Auditing Financial Instruments*. The proposed SAS is expected to be voted for exposure at the ASB's April 14 meeting.

### ***Bank Confirmation Issue***

Andrew Capelli, AITF member, led a discussion about several instances where auditors have received a bank's own audit confirmation form in response to the standard audit bank confirmation form that the auditors mailed. The bank's form contains caveats regarding the information provided, including that its accuracy is not guaranteed, the information may not be complete, and other "disclaimers."

Management of the bank has stated that use of such confirmations does not conform to the bank's institutional policy and that the matter will be investigated.

### ***Systems Reliability Update***

G. Tucker provided an update on the status of the AICPA/CICA SysTrust engagement. A draft of the engagement is about to be released for a pre-exposure review by associates. SysTrust is an engagement to provide examination-level assurance that an entity has maintained effective controls over an entity's system to provide reasonable assurance that the system was reliable for a period of time. A reliable system, as defined by the AICPA/CICA SysTrust Principles and Criteria, meets criteria of availability, security, integrity, and maintainability.

A review group comprised of G. Tucker, D. Lambert, Kurt Pany, T. Ray, J. Mancino and J. Sherinsky will look at the preexposure draft for fatal flaws.

### ***Big 5 Y2K Group***



G. Tucker reported that the Big 5 Y2K group met to discuss various matters including the SEC's Notice of Proposed Rule relating to broker/dealers that, among other issues for discussion, asks whether the SEC should require independent third party verification of an entity's remediation efforts. AITF participants agreed that additional Y2K guidance should be developed as follows:

- Guidance will be included in the 1999/2000 *Audit Risk Alert* stating that a Y2K "meltdown" subsequent to the balance sheet date but before issuance of the financial statements is a Type II subsequent event. The *Alert* should be available in September.
- Going concern guidance drawn from the existing interpretation will be included in the June or July *CPA Letter*.
- Guidance on changes that might affect client business practices also will be included in the *Audit Risk Alert*.