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ASB meeting minutes, 1997, November 18-20

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ASB Meeting Minutes, November 18-20, 1997

Meeting: Auditing Standards Board

Date: November 18-20, 1997

Location: AICPA
1211 Avenue of the Americas
New York, NY 10036

Meeting Attendance: Edmund R. Noonan, Chair
John L. Archambault
Luther E. Birdzell
John A. Fogarty, Jr.
James S. Gerson
Stephen D. Holton
J. Michael Inzina
John J. Kilkeary
Charles E. Landes
Stephen McEachern
Kurt Pany
Edward F. Rockman
Alan Rosenthal
W. Ronald Walton

Other Participants

Tracey C. Barber, Chair, FASB 125 Audit Issues Task Force (via conference call)

Beth Schneider, Deloitte & Touche LLP

Patrick Shouvin, Price Waterhouse

Dan M. Guy, Vice President, Professional Standards and Services

Thomas Ray, Director, Audit and Attest Standards

Julie Anne Dilley, Technical Manager, Audit and Attest Standards

Gretchen Fischbach, Technical Manager, Audit and Attest Standards

Kim M. Gibson, Technical Manager, Audit and Attest Standards

Elaine Lehnert, Technical Manager, Accounting Standards

Jane M. Mancino, Technical Manager, Audit and Attest Standards

Judith M. Sherinsky, Technical Manager, Audit and Attest Standards

I. CHAIRS REPORT (File 1220)

Edmund R. (Randy) Noonan, Chair, presented to the Auditing Standards Board the highlights of the Audit Issues Task Force's October 16, 1997 meeting, and the meeting with the Canadian Institute of Chartered Accountants' Auditing Standards Board and American Bar Association.

II. DIRECTORS REPORT (File 1221)

Thomas Ray, AICPA Director, Audit and Attest Standards, reported the following matters to the ASB.

A. Year 2000

AICPA staff and the Year 2000 Task Force completed the initial phase of its consideration of the Year 2000 Issue and its implications on the profession. The Year 2000 Issue: Current Accounting and Auditing Guidance, was posted to the AICPA's Web

site on October 31, and will be published in print form in November. It generally provides guidance to auditors of financial statements, although the guidance also can benefit management and accountants providing other types of services, such as compilations and reviews of financial statements. The document includes the ASB's interpretations relating to the Year 2000 Issue. Gretchen Fischbach, AICPA Technical Manager, Audit and Attest Standards, served as staff liaison to the Year 2000 Task Force. Alan Anderson, AICPA Senior Vice President, Technical Services, and T. Ray also participated in the task force's deliberations.

B. International

T. Ray briefed the ASB on recent international activities, including the World Congress of Accountants, which was held in Paris, France, October 26-29, 1997, and the International Auditing Practices Committee meeting, which took place in Copenhagen, Denmark, November 3-7, 1997.

IMSA Ethical Market Conduct Project

Patrick Shoumlin, chair of the Insurance Companies Committee and Elaine Lehnert, technical manager, presented a draft auditing SOP, Reporting on Management's Assessment Pursuant to the Life Insurance Ethical Market Conduct Program of the Insurance Marketplace Standards Association. The draft SOP provides guidance to practitioners in conducting and reporting on an independent examination performed pursuant to the AICPA Statement on Standards for Attestation Engagements to assist an entity in meeting the requirements of the Insurance Marketplace Standards Association (IMSA) program (the IMSA program). IMSA requires that such engagements use the criteria it sets forth. The SOP assumes that users of the SOP would be familiar with the IMSA program and its Assessment Handbook and requirements.

The ASB discussed several issues with the SOP. Mr. Shoumlin and Ms. Lehnert agreed to make the changes discussed. The ASB approved the SOP for final issuance subject to negative clearance by the ASB. The final issuance of the SOP is anticipated for the first quarter of 1998.

Restricted-Use (File Ref. No. 4275)

The Restricted-Use Task Force (task force) has been considering areas of the auditing and attestation standards that prescribe restrictions on the use or distribution of accountants' reports to determine whether standards should be developed that describe the characteristics of the subject matter, nature of the engagement, or other factors that might necessitate a restriction on the use of an accountant's report.

John J. Kilkeary, Chair of the task force, led the ASB in a discussion of a revised draft of a proposed Statement on Auditing Standards (SAS), titled Restricting the Use of an Auditor's Report, that would provide guidance for engagements performed under the SASs. The ASB recommended that the task force —

- Identify other SASs that will require conforming changes as a result of the proposed SAS.
- Replace the words "ordinarily should advise" with the words "should consider informing" in the first sentence of paragraph 16 so that the revised sentence will read, "The auditor should consider informing his or her client that restricted-use reports are not intended for distribution by the client to non-specified parties."
- Add a paragraph after paragraph 9 of the proposed SAS indicating that an auditor may issue a by-product report in connection with other engagements performed in accordance with generally accepted auditing standards.
- Voted to expose the draft for comment.

Summary of ASB Preference Vote

Restricted-Use Task Force (File Ref. No. 4275)	For	Against	Abstain	Absent
Should the 11/19/97 draft of Restricting the Use of an Auditor's Report be exposed for comment?	12	0	0	3

OWNERSHIP, EXISTENCE, AND VALUATION (File Ref. No. 2405)

The Ownership, Existence, and Valuation Task Force (task force) is considering the auditor's responsibility for auditing financial-statement assertions about the ownership, existence, and valuation of financial instruments, commodity contracts, and similar instruments.

Tom Birdzell, Chair of the task force, led the ASB in a discussion of a draft of a proposed SAS titled Auditing Financial Instruments. The proposed SAS revises the scope of SAS No. 81, Auditing Investments, to include all financial instruments. The current scope of SAS No. 81 includes (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 ASB reviewed the draft and recommended that the task force —

- Revise paragraph 1 to indicate where the auditing guidance for various types of financial instruments is located in the SAS.
- Provide an example, in paragraph 3, of a "complex use of a financial instrument."
- Revise paragraph 6 to indicate that in some circumstances involving financial instruments, it may not be possible to reduce detection risk to an acceptable level by only performing substantive tests and that an auditor may have to perform tests of controls to assess control risk for certain financial-statement assertions.
- Revise paragraph 8 to clarify the extent of the procedures an auditor should perform to address the completeness assertion.
- Revise paragraph 17 to indicate that management should obtain a valuation that is as of a date closer to the date of the financial statements if an existing valuation is as of a date other than the date of the financial statements and intervening events may have caused a significant change in the valuation.
- Revise paragraph 17 to clarify that management, rather than the auditor, is responsible for obtaining a valuation of financial instruments.

FASB 125 AUDIT ISSUES TASK FORCE (File Ref. No. 2605)

Tracey C. Barber, Chair, FASB 125 Audit Issues Task Force (task force), presented via conference call a working draft of a proposed interpretation, "The Use of Legal Interpretations As Evidential Matter to Support Management's Assertion That a Transfer of Financial Assets Qualifies As a Sale," of SAS No. 73, Using the Work of a Specialist. The proposed interpretation provides guidance to auditors regarding the use of a legal specialist's findings as audit evidence to support management's assertion that a transfer of financial assets meets the legal isolation criterion of paragraph 9(a) of Statement of Financial Accounting Standards (SFAS) No. 125, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities. The legal isolation criterion of paragraph 9(a) is one of several criteria that must be met in order for a transferor of financial assets to demonstrate surrender of control over the financial assets and to account for a transfer as a sale.

The proposed interpretation addresses: i) when the use of a legal specialist's work may be appropriate; ii) factors that should be considered in assessing the adequacy of the legal response; and iii) the use, as audit evidence, of legal responses that are restricted to the client's use.

The task force has initiated discussions with the Financial Accounting Standards Board (FASB) about the guidance contained in paragraphs 58 and 121 of SFAS 125 regarding the isolation of financial assets in "single-step" securitizations by banks subject to FDIC receivership. The task force also has discussed certain issues related to this matter with FDIC representatives. The task force plans to include guidance based on the outcome of those discussions in the final interpretation.

The ASB approved the task force's plan to post the proposed interpretation on the AICPA Web site and to mail it to constituents identified by the task force for comments simultaneous with the ASB's "fatal flaw" review period from November 24 through December 15, 1997. Comments on the proposed interpretation and the disposition of open issues relating to securitizations by banks subject to FDIC receivership will be discussed at the December ASB meeting. The task force plans to issue the interpretation by the end of the year.

MANAGEMENT'S DISCUSSION AND ANALYSIS (File Ref. No. 3507)

John A. Fogarty, chair of the Management's Discussion and Analysis (MD&A) Task Force, led the Board's discussion of issues relating to the proposed SSAE, Management's Discussion and Analysis (MD&A).

The Board:

- Discussed the effect of the Year 2000 Issue on the proposed SSAE on MD&A. J. Fogarty noted that a vote for final issuance of the standard would be postponed until the December 1997 ASB meeting to give the task force sufficient time to consider all the ramifications involved, meet with the AICPA's Y2K task force, and develop a draft interpretation on the issue for consideration by the Board.
- Discussed the criteria for MD&A. The SEC's requirements for MD&A have been placed in paragraph 4. All subsequent references to Item 303 of Regulation S-K, Item 303 of Regulation S-B, Item 9 of Form 20-F and the term "published" have been replaced with "the rules and regulations adopted by the SEC."
- Discussed review reports. Paragraph 87.k has been revised to include the rationale for restricting review reports and when review reports should be restricted. The restrictive paragraphs in the review report examples in Appendix B and the combined examination and review reports in Appendix C have been revised to be consistent with the Restricted Use exposure draft.
- Performed a paragraph by paragraph review of the draft SSAE.
- Agreed to make both the SSAE and the SAS, Amendment to SAS No. 72, effective upon issuance.

The Board hopes to vote to ballot for issuance of the proposed SSAE as a final SSAE at the next meeting.

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