

University of Mississippi

eGrove

American Institute of Accountants

Deloitte Collection

1965

Letters for underwriters; Statement on auditing procedure, No. 35

American Institute of Accountants. Committee on Auditing Procedure

Follow this and additional works at: https://egrove.olemiss.edu/dl_aia



Part of the [Accounting Commons](#), and the [Taxation Commons](#)

Recommended Citation

American Institute of Accountants. Committee on Auditing Procedure, "Letters for underwriters; Statement on auditing procedure, No. 35" (1965). *American Institute of Accountants*. 261.
https://egrove.olemiss.edu/dl_aia/261

This Article is brought to you for free and open access by the Deloitte Collection at eGrove. It has been accepted for inclusion in American Institute of Accountants by an authorized administrator of eGrove. For more information, please contact egrove@olemiss.edu.

STATEMENT ON AUDITING PROCEDURE

35

Letters for Underwriters

1. The services of independent accountants include examination of financial statements and supplemental schedules contained in registration statements under the Securities Act of 1933 and in registration statements or applications and annual reports under the Securities Exchange Act of 1934, as well as other Acts administered by the Securities and Exchange Commission. In connection with these services, independent accountants often are called upon to advise and consult with clients, underwriters, and counsel concerning the accounting and auditing requirements of the SEC and to perform other services. One of these other services is the issuance of letters for underwriters in connection with the distribution of securities. This Statement indicates guides which, in the opinion of the committee, should have the careful consideration of independent accountants as they prepare letters for underwriters, commonly referred to as "comfort letters." Comfort letters are not required under the Acts administered by the Securities and Exchange Commission, and copies of the letters are not filed with the Commission. (See paragraphs 10 through 16, chapter 1, Statements on Auditing Procedure No. 33 for a discussion of certain

*Issued by the Committee on Auditing Procedure
American Institute of Certified Public Accountants*

responsibilities of accountants resulting from inclusion of their reports in registration statements.)

2. A usual condition of an underwriting agreement in connection with the offering for sale of securities registered with the Securities and Exchange Commission under the Securities Act of 1933 is that the independent accountants perform certain procedures and, based thereon, furnish a comfort letter for the underwriters. Such a letter is intended to aid in discharging underwriters' responsibilities under the Act; it is regarded by the underwriters as one means of learning promptly of any event subsequent to the date of the latest financial statements appearing in the registration statement (which in all cases includes the prospectus) which might require disclosure. If, in the opinion of the accountants, their procedures have disclosed any such event, they should advise the registrant (that is, the client) promptly so that the matter may be called to the underwriters' attention. Because of the possible consequences of discovery of material information which might have to be disclosed in the registration statement or the comfort letter, the accountants should plan their procedures so that possible discoveries will not be delayed unduly.

3. Comfort letters from accountants typically will refer to one or more of the following subjects:

- (a) The independence of the accountants.
- (b) Compliance of the audited financial statements and schedules with the applicable accounting requirements of the Securities Act of 1933 and of the published rules and regulations of the Securities and Exchange Commission.
- (c) Unaudited financial statements and schedules in the registration statement.
- (d) Changes in capital stock and long-term debt.
- (e) Material adverse changes in the financial position or results of operations during a period subsequent to the date and period of the latest financial statements, summary of earnings, or related financial data in the registration statement.

- (f) Tables and other compilations of financial information in the registration statement.

The matters dealt with in the letter usually should be limited to those specified in the underwriting agreement.

4. The accountants should obtain a draft of the agreement as early as practicable so that they can advise the registrant as to wording the agreement in a manner that will not place demands on the accountants with which they cannot comply.

5. The various matters that usually are covered in a letter for underwriters are discussed below.

Dating

6. The letter ordinarily is dated on or shortly before the date, commonly referred to as the "closing date," on which the related securities are delivered to the underwriters in exchange for the net proceeds from their sale. The underwriting agreement ordinarily will specify the date (that is, the cut-off date) to which the letter is to relate (e.g., a date within five business days before the date of the letter); the accountants should see that the date specified will not place an unreasonable burden on them.

Address

7. The letter may be addressed to the registrant (considered by many accountants to be preferable), to the registrant and the underwriters, or to the underwriters.

Introductory Paragraphs

8. It is desirable to include an introductory paragraph substantially as follows:

We have made an examination of the consolidated financial statements and schedules of The Blank Company, Inc., and its subsidiaries as of December 31, 1964 and for the

three years then ended, and of the related summary of earnings for the five years ended December 31, 1964, and our opinions with respect to the foregoing are included in the registration statement (No. 2-00000) filed by the Company under the Securities Act of 1933 (the "Act"). Such registration statement and the related prospectus, as amended at the time such registration statement became effective, are herein referred to respectively as the "Registration Statement" and the "Prospectus."

Sometimes the foregoing paragraph is preceded by a paragraph somewhat as follows:

This letter is written at your request (or at the request of The Blank Company, Inc., if the letter is not addressed to the registrant) pursuant to Section 8 of an agreement of April 18, 1965 between the Company and The Blank Underwriters.

Independence

9. It is customary for the accountants to make a statement in the letter concerning their independence, somewhat as follows:

We are independent public accountants as required by the Act and the applicable published rules and regulations thereunder.

Compliance with SEC Requirements

10. The accountants may be requested to make a direct statement concerning compliance (usually solely as to form) of the financial statements covered by their opinion with the pertinent accounting requirements of the Securities and Exchange Commission. This may be done substantially as follows:

In our opinion, the financial statements and schedules and the summary of earnings examined by us and included or incorporated by reference in the Prospectus or elsewhere

in the Registration Statement comply (as to form) in all material respects with the applicable accounting requirements of the Act and of the published rules and regulations thereunder with respect to registration statements on Form ____.

Unaudited Financial Statements and Subsequent Changes

In General

11. Comments may be required in the letter concerning (a) unaudited financial statements and schedules, if any, included in the registration statement, (b) changes in capital stock and long-term debt, and (c) material adverse changes in financial position and results of operations subsequent to the date or period of the latest financial statements included in the registration statement, whether audited or unaudited. In commenting on these matters the following guides are important:

- (a) The procedures followed should be specified. These may include (1) reading interim financial statements, (2) reading minutes, and (3) making inquiries of and obtaining a letter of representation from company officers who have responsibility for financial and accounting matters. These also should include such additional procedures, if any, as may be required by the underwriting agreement with respect to particular items or matters. Terms such as "review," "general review," or "limited review" should not be used in describing the work, unless the procedures comprehended by the term are clearly specified in the letter for the underwriters.
- (b) Except as to specific matters which have been in fact checked or tested, any statement that the accounting records have been checked or tested should be avoided.

- (c) The letter should state that an examination of the financial statements for the interim period has not been made, and that the work done does not constitute an examination made in accordance with generally accepted auditing standards.
- (d) An opinion as to the interim period should be specifically disclaimed; any statement as to such period should be limited to negative assurance.
- (e) The procedures followed with respect to the interim period manifestly may not disclose adverse changes in financial position or results of operations or inconsistencies in the application of generally accepted accounting principles or instances of non-compliance as to form with accounting requirements of the SEC. If the underwriting agreement calls for comments on these or other matters, the letter should state that the procedures would not necessarily reveal them.
- (f) The working papers relating to letters for underwriters should be so prepared as to constitute adequate evidence of what has been done, what comparisons have been made, and the substance of discussions with corporate officials and others (including representatives of underwriters).

Unaudited Financial Statements

12. Comments in the comfort letter concerning unaudited financial statements appearing in the registration statement should always be made in the form of negative assurance,¹ ordinarily with respect to (a) conformity with generally accepted accounting principles consistently applied, (b) material adjustments required for fair presentation, and (c) compliance as to form with applicable accounting requirements. An appropriate manner of expressing the comments is shown in the examples at the end of this Statement.

¹ See *Statements on Auditing Procedure No. 33*, page 61, concerning restricted use of negative assurance.

13. When the most recent figures included in a summary of earnings are for a period of less than one year, the SEC usually requires that comparative figures be shown for the corresponding short period of the preceding year. Frequently the financial statements for the latest interim period are unaudited; financial statements for the interim period of the preceding year are ordinarily presented as unaudited, even though this period is part of a year for which financial statements have been audited. In these circumstances the accountants' position with reference to the financial statements of the earlier period should be made clear in the letter for underwriters. This may be done by indicating that no opinion is expressed on the financial statements for such period because the purpose of the examination was to enable the accountants to express an opinion as to the financial statements for the full year rather than for any interim date or period within such year.

Subsequent Changes

14. Comments as to subsequent changes also should be in the form of negative assurance. These ordinarily relate to the absence of any change in capital stock or long-term debt, or any material adverse change in financial position or results of operations. With respect to material adverse changes, the following paragraphs discuss the periods involved, the comparisons to be made, and the types of changes contemplated.

15. Comments as to material adverse changes relate to the period, referred to hereinafter as the "comfort" period, ending on the cut-off date and beginning (a) as to changes in financial position, immediately after the date of the latest balance sheet in the registration statement, and (b) as to changes in results of operations, immediately after the latest period included in the summary of earnings (or in some cases immediately after the latest period for which unaudited interim data such as sales or net income are disclosed in narrative form immediately following the summary of earnings).

16. The underwriting agreement may specify the period or periods with which the results of operations for the "comfort"

period (or the latest period for which financial statements are available) are to be compared. Such periods might be, for example, (1) the corresponding period of the preceding year, (2) the corresponding number of months immediately preceding the "comfort" period, (3) a proportionate part of the preceding fiscal year, or (4) any other period relevant in the circumstances. Some accountants believe that the period or periods with which comparison is made should be mentioned in the letter, even though they are not specified in the underwriting agreement. The comparison should comprehend the amounts, relationships, or averages, as appropriate, with respect to significant captions and items in the statements of income (including any special items) and of surplus for the respective periods. Similar comparison should be made between the latest balance sheet in the registration statement and the latest one available prior to the cutoff date. In addition to making comparisons based on the latest financial statements available, the accountants should read minutes and make inquiries of and obtain letters of representation from company officers who have responsibility for financial and accounting matters concerning not only the period covered by such statements but also the period extending to the cutoff date.

17. The type of change contemplated in letters for underwriters is limited to matters the effect of which would be shown in financial statements (and related notes) at the cutoff date and for the "comfort" period then ended, if statements (and their notes) could be prepared as of that date. This limitation should be indicated by stating specifically that:

The terms "financial position" and "results of operations" are used in this letter in their conventional accounting sense; accordingly, they relate to the financial statements of the business as a whole and have the same meaning when used in this letter as in our opinion contained in the Registration Statement and Prospectus.

18. It is not practicable to describe in detail changes which might be regarded as adverse. As indicated above, such changes are limited to those whose effects would be shown in financial statements of the type included in the registration statement and

prospectus. There is sometimes a difference of opinion as to what constitutes an "adverse change" and as to the responsibility of the accountants in this determination. Some believe that the accountants should investigate the reasons underlying the apparently adverse changes shown in the financial statements. The purpose of this investigation would be to determine whether, in their opinion, the change was in fact "adverse." Thus, a decrease in net income compared with a prior period might not be considered an adverse change if the accountants were reasonably well satisfied that the causes would be beneficial to the long-range prospects of the company. Others believe that the adverse nature of a change reflected in the financial statements is determined by absolute relationships between the amounts shown in the financial statements and corresponding amounts shown in statements for the periods of comparison. Under this concept, the adverse nature is not based on an evaluation of the apparent cause of the change or of its possible effects, if any, on future prospects or operations of the business. This latter group believes that independent accountants usually do not hold themselves out as possessing the detailed knowledge of the business necessary to make such a determination.

19. Whichever concept of the nature of an adverse change the accountants support, it is important that any indications of material adverse changes, of whatever type, be discussed with the client so that the client may consider whether disclosure thereof should be made in the registration statement. If disclosure is not to be made, the accountants should, if in their opinion the change is a material adverse change, advise the client that mention thereof will be made in their letter and suggest that the underwriters be so advised. Although in most cases there are informal discussions between the accountants and underwriters or the latter's counsel, there may be situations in which the client would prefer to deal with the underwriters. Since the accountants may, under these circumstances, have no direct contact with the underwriter, except through the submission of their letter, they should make sure that their client understands the significance of any exception which would be contained in the letter.

20. While the discussion in the preceding paragraph refers

to matters to be considered for disclosure in the registration statement as amended to the effective date, any material adverse changes that come to the accountants' attention prior to the end of the comfort period also should be discussed with the client in a like manner.

Disclosure in Prospectus

21. The negative assurances as to material adverse changes in financial position and in results of operations and as to changes in capital stock or long-term debt (hereinafter referred to as "changes") do not require specific reference to any such changes which are disclosed in the registration statement. This exclusion is effected by using the phrase "except as set forth in or contemplated by the registration statement and prospectus." Whenever it appears to the accountants that a change may have occurred during the comfort period, they should scrutinize the registration statement to determine whether the change is "set forth in or contemplated by" the material appearing therein. Examples of changes which ordinarily would be set forth in or contemplated by the registration statement would be the following: payment of long-term debt, issuance of common stock under a stock option plan, payment of dividends, an adverse trend in earnings due to seasonal factors, an adverse trend in earnings due to changes in income tax rates, or changes in application of accounting principles. In many cases, the question of whether a change is "set forth in or contemplated by" the registration statement and prospectus is a matter of judgment. In applying judgment to disclosures in the registration statement, the accountants should bear in mind that the disclosure should be presented in such a manner that a reasonably prudent reader could understand its significance. When questions of this type arise, it is often possible for the accountants to discuss the matter with their client in order to improve or clarify the disclosure in the registration statement.

Effect of Qualified Opinion

22. The foregoing discussion contemplates that the accountants' opinion on the financial statements and schedules and summary of earnings in the registration statement and the related prospectus is unqualified. This usually is the case. Except in extraordinary circumstances, the requirements of the SEC will not permit a registration statement to become effective when the accountants' opinion is qualified as to the scope of their examination or as to the accounting principles reflected in the financial statements and schedules and summary of earnings. However, such circumstances do occasionally arise. For example, it may be necessary to qualify the opinion on the financial statements of a public utility because the company has been ordered by regulatory authority to do something which does not conform with generally accepted accounting principles, and the amount involved is material. In these circumstances, although the Commission may permit the registration statement to become effective even though the opinion is qualified, the accountants may not be in a position to give an opinion that the financial statements in the registration statement comply as to form in all material respects with the rules and regulations of the Commission under the Securities Act of 1933.

23. The SEC ordinarily will accept a "subject to" type of qualification in the accountants' opinion where there is uncertainty as to the outcome of negotiations or litigation concerning income taxes, renegotiation, or other controversies, recovery of research and development costs or other deferred charges, or similar matters which are not susceptible to reasonable accounting determination, but might have a material effect on financial position or results of operations.

24. If the opinion is qualified, the qualification should be referred to in the opening paragraph of the letter for underwriters by saying, for example, "and our opinion (which is qualified as set forth therein) with respect to the foregoing is included in the Registration Statement and Prospectus. . . ."

The accountants also should consider the effect, if any, of the qualification on the representations as to compliance with applicable SEC requirements.

25. If the letter for underwriters includes negative assurance as to a fair presentation of subsequent unaudited financial statements in the registration statement, the effect thereon of the subject matter of the qualification should also be considered. An illustration of how this type of qualification may be expressed is shown in Example C at the end of this Statement.

Concluding Paragraph

26. Since the letter for underwriters is prepared solely to enable the registrant to comply with the terms of an agreement with the underwriters, it should be concluded along the following lines:

This letter is solely for the information of the Company and the underwriters and is not to be referred to in whole or in part in the registration statement, prospectus, or any other similar document, or quoted by excerpt or reference outside the underwriting group in connection with the registration under the Act or the sale of securities, except for any reference to it in the underwriting agreement or in any list of closing documents.

Other Accountants

27. Comfort letters are occasionally requested from more than one accountant, particularly in connection with registration statements to be used in the subsequent sale of shares issued in connection with recently effected mergers. In these circumstances, each accountant must, of course, be independent with respect to his client. The accountants for companies recently merged into the registrant would not be required to have been independent with respect to the company whose shares are being registered. However, these accountants should make clear the extent of their independence in their letters. This is usually accomplished by

adding the underlined phrase to the representation as to independence as follows:

We are independent public accountants with respect to Company B within the meaning of the Securities Act of 1933 and the rules and regulations thereunder.

28. There may be situations in which more than one accountant is involved in the examination of financial statements of a business. For example, certain significant divisions, branches, or subsidiaries may be examined by other accountants. The accountants who report on the consolidated financial statements should consider obtaining a letter from the accountants reporting on significant units. This letter should contain representations and negative assurances similar to those contained in the comfort letter prepared by the accountants reporting on the consolidated financial statements. Since the other accountants also are required to be independent with respect to the parent company, the representation in their letters as to their independence should relate to the parent company and its subsidiaries. The accountants reporting on the consolidated financial statements might disclose in their comfort letter that receipt of letters from other accountants was one of the procedures followed.

29. At the earliest practicable date, the accountants for the parent company should advise any other accountants that may be involved as to any requirements for a letter from them, so that they may make arrangements at an early date for the completion of their procedures and the preparation of a draft of their letter.

Tables and Other Compilations of Financial Information

30. The underwriting agreement occasionally provides that the accountants shall comment on tables, statistics, and other compilations of financial information appearing in the registration statement. The material to be covered may range from information with a reasonably close relationship to accounting matters (such as the capital structure or the remuneration of

directors and officers) to data which are primarily statistical or legal in nature (such as tabulations of units of product sold or information as to recent sales of unregistered securities).

31. The usual examination of financial statements by accountants for the purpose of expressing an opinion thereon is not sufficiently detailed to enable the accountants to give representations as to certain of the data in the positive form sometimes requested by underwriters. This situation is complicated by the fact that certain of the information may be presented as of a date subsequent to the period covered by the financial statements examined by the accountants, or in some cases subsequent to the date of the latest available unaudited financial statements. The limited procedures followed with respect to the comfort period cannot be expected to furnish a basis for an opinion or other representation in positive form on information of this type.

32. The following guidelines should be observed by accountants in commenting on such tables and information:

- (a) No more than negative assurance should be given, except in most unusual circumstances.
- (b) The basis for negative assurance should be stated. This may be done by using one of the phrases or an appropriate combination of the phrases shown in the following:
 - (i) For the period covered by the examination by using a phrase such as, "during the course of our examination . . ."
 - (ii) For the unaudited or comfort period, by using a phrase such as, "As a result of the limited procedures described in this letter . . ."
 - (iii) When specific additional procedures are requested by the underwriters, or are otherwise appropriate, such procedures should be described in the letter. An appropriate form of recitation might be as follows: ". . . made inquiries of of-

officials responsible for financial and accounting matters as to whether the accounting information set forth in the Registration Statement and Prospectus under the captions '.....' and '.....' requires any material adjustment for a fair presentation."

- (c) Terms used in the standard short-form opinion should be avoided.
- (d) Phrases such as "correctly stated," "adequately presented," "adequately disclosed," and the like should be avoided in referring to the information.
- (e) The information covered should be identified by specific reference to captions, tables, or page numbers; broad designations such as "all financial data appearing in the Registration Statement and Prospectus" should be avoided.
- (f) Any implication of responsibility for legal interpretations should be avoided by appropriate disclaimer of opinion. The question as to what constitutes appropriate information for compliance with the requirements of a pertinent item of the registration statement form is, for example, a matter of legal interpretation generally outside the competence of the accountant.

33. Financial information of the type contemplated in the foregoing may relate to either the period covered by audited financial statements included in the registration statement or a later period not so covered. One way to express the negative assurance with respect to such financial information for an audited period is as follows:

During the course of our aforementioned examination of the financial statements for the year ended December 31, 1964, nothing came to our attention which caused us to believe that the accounting information set forth in the Registration Statement and Prospectus under the caption "Remuneration of Directors and Officers" required any material adjustment for a fair presentation.

34. One way to express the negative assurance as to information with respect to an unaudited period is as follows:

The limited procedures described in this letter did not bring anything to our attention which caused us to believe that the accounting information set forth in the Registration Statement and Prospectus under the caption "Capitalization" requires any material adjustment for a fair presentation.

35. An illustration of a way to express negative assurance concerning financial information, which may be construed as being subject to legal interpretation, is as follows:

During the course of our examination . . . (see above, but expand period to three years, if appropriate) . . . and as a result of the limited procedures described in this letter, nothing came to our attention which caused us to believe that the accounting information set forth in the Registration Statement and Prospectus under the caption "Recent Sales of Unregistered Securities" requires any material adjustment for a fair presentation, to the extent such accounting information is reflected in the accounting records, and excluding any questions of legal interpretation.

36. There follow some examples of letters for underwriters, introduced in each instance by a description of some of the circumstances to which the form is applicable. It is assumed that the letters are addressed to the Registrant.

Example A

This letter, sometimes called a "compliance" letter, applies when the underwriting agreement provides for nothing more than a statement as to compliance of audited financial statements with SEC requirements.

Dear Sirs:

This letter is written at your request pursuant to Section 8 of an agreement of April 18, 1965 between Blank Company and The Underwriters, Inc.

We have examined the balance sheet of Blank Company as of December 31, 1964, the related statement of income for the five years then ended, and the related statement of earned surplus for the three years then ended, and our opinion with respect to the foregoing is included in a Registration Statement (No. 2-00000) filed by the Company under the Securities Act of 1933.

In our opinion, the above-mentioned financial statements examined by us and included in the Registration Statement and the related Prospectus, as amended at the time such Registration Statement became effective, comply as to form in all material respects with the applicable accounting requirements of the Securities Act of 1933 and of the published rules and regulations of the Securities and Exchange Commission thereunder with respect to Registration Statements on Form S-1.

Example B

This letter is based on a situation in which the registration statement includes an audited consolidated balance sheet as of December 31, 1964, statements of consolidated income and surplus for the three years then ended, and a summary of consolidated earnings for the five years then ended. No unaudited financial statements are included in the registration statement but the capitalization table is as of a date later than the balance sheet. The underwriting agreement makes no reference to schedules but requires an opinion as to compliance, a representation as to independence, and negative assurance relating to the absence of material adverse changes in financial position or results of operations and changes in capitalization; the underwriters have agreed, in advance, that the corresponding period of the previous year might be used for purposes of comparison with the results of operations for the current interim period.

Dear Sirs:

This letter is written at your request to enable Blank Company to comply with Section 10 of its agreement of April 17, 1965, with The Underwriters, Inc.

We have made an examination of the consolidated financial statements of Blank Company (the "Company") and its sub-

sidiaries as of December 31, 1964, and for the three years then ended, and of the related summary of consolidated earnings for the five years ended December 31, 1964, and our opinion with respect to the foregoing is included in the registration statement (No. 2-00000) filed by the Company under the Securities Act of 1933 (the "Act"). Such registration statement and the related prospectus, as amended at the time such registration statement became effective, are herein referred to respectively as the "Registration Statement" and the "Prospectus."

We are independent public accountants as required by the Act and the applicable published rules and regulations thereunder.

In our opinion, the financial statements and summary of earnings examined by us and included in the Prospectus comply as to form in all material respects with the applicable accounting requirements of the Act and of the published rules and regulations thereunder with respect to Registration Statements on Form S-1.

We have not made an examination of any financial statements of the Company or any of its subsidiaries as of any date or for any period subsequent to December 31, 1964, and, therefore, we are unable to and do not express any opinion on any such financial statements. However, we have, at the Company's request, carried out procedures and made inquiries with respect to the period from December 31, 1964 to May 25, 1965 as follows:

- (1) read the interim unaudited consolidated financial statements of the Company and its subsidiaries covering the period from January 1, 1965 to April 30, 1965, officials of the Company having advised us that no such financial statements as of any date or for any period subsequent to April 30, 1965 were available;
- (2) read the 1965 minutes of the meetings of the stockholders, the Board of Directors, and the executive and finance committees of the Company and its subsidiaries as set forth in the minute books at May 25, 1965, officials of the Company having advised us that the minutes of all such meetings through that date were set forth therein; and

- (3) made inquiries of certain officials of the Company and its subsidiaries who have responsibility for financial and accounting matters as to whether since March 31, 1965 there had been any change in the consolidated capital stock or long-term debt of the companies from that shown as of March 31, 1965 under the caption "Capitalization" in the Prospectus, and as to whether since December 31, 1964 there has been any material adverse change in the consolidated financial position or consolidated results of operations.

The foregoing procedures and inquiries do not constitute an examination made in accordance with generally accepted auditing standards; also they would not necessarily reveal material adverse changes in the financial position or results of operations or inconsistencies in the application of generally accepted accounting principles.

We may state, however, that the foregoing procedures and inquiries did not cause us to believe that during the period from March 31, 1965 to May 25, 1965 there was any change in the capital stock or funded debt of the Company on a consolidated basis from that shown or contemplated under the caption "Capitalization" in the Prospectus or that during the period from January 1, 1965 to May 25, 1965 there was any material adverse change in the consolidated financial position of the Company and its subsidiaries from that set forth by the consolidated balance sheet as of December 31, 1964 included in the Prospectus or any material adverse change in the consolidated results of their operations as compared with the corresponding period in the preceding year, except in all instances as set forth in or contemplated by the Registration Statement and Prospectus or as occasioned by the declaration or payment of dividends.

The terms "financial position" and "results of operations" are used in this letter in their conventional accounting sense; accordingly, they relate to the financial statements of the business as a whole and have the same meaning when used in this letter as in our opinion contained in the Registration Statement and Prospectus.

This letter is solely for the information of the Company and

the Underwriters and is not to be referred to in whole or in part in the Registration Statement or Prospectus or quoted by excerpt or reference outside the underwriting group in connection with the registration under the Act or the sale of securities, except for any reference to it in an underwriting agreement or in any list of closing documents.

Example C

This letter relates to a situation similar to that for Example B except that the prospectus includes unaudited statements as follows: Balance sheet as of March 31, 1965, statement of surplus for the three months then ended, and a summary of earnings (called a statement of income) for the three-month periods ended March 31, 1964 and 1965; and Part II of the registration statement includes unaudited schedules for the three months ended March 31, 1965. The underwriting agreement, which does include a reference to schedules, requires a representation as to independence, an opinion as to compliance, and negative assurance from the auditors with respect to the unaudited figures and material adverse changes in financial position and results of operations. This letter illustrates, among other things, the terminology employed where the accountants' opinion contains a "subject to" qualification.

Dear Sirs:

We have made an examination of the balance sheet of Blank Company (the "Company") as of December 31, 1964, the related statement of income for the five years then ended, and the related statement of earned surplus, and schedules, for the three years then ended, and our opinions (qualified as set forth therein) with respect to the foregoing are included in the registration statement (No. 2-00000) filed by the Company under the Securities Act of 1933 (the "Act"). Such registration statement and the related prospectus, as amended at the time such registration statement became effective, are herein referred to respectively as the "Registration Statement" and the "Prospectus."

We are independent public accountants as required by the

Act and the applicable published rules and regulations thereunder.

In our opinion, the financial statements and schedules examined by us and included or incorporated by reference in the Prospectus or elsewhere in the Registration Statement comply as to form in all material respects with the applicable accounting requirements of the Act and the published rules and regulations thereunder, with respect to Registration Statements on Form S-1.

We have not made an examination of any financial statements of the Company as of any date or for any period subsequent to December 31, 1964; and although we have made an examination for the year ended December 31, 1964, the purpose (and therefore the scope) of such examination was to enable us to express our opinion as to the financial statements as of December 31, 1964 and for the year then ended but not as to the financial statements for any interim period within such year. Therefore, we are unable to and do not express any opinion on the unaudited balance sheet as of March 31, 1965, interim statement of surplus for the three months then ended, and interim statements of income for the three-month periods ended March 31, 1965 and 1964 and related schedules contained in the Prospectus or included elsewhere in the Registration Statement or on the financial position or results of operations as of any date or for any period subsequent to December 31, 1964.

However, we have at the Company's request carried out procedures and made inquiries:

with respect to the three-month periods ended March 31, 1964 and 1965, as follows:

- (1) read the unaudited statements of income for these periods included in the Prospectus;
- (2) read the unaudited balance sheet as of March 31, 1965, and unaudited statement of surplus for the three months then ended included in the Prospectus and the related unaudited schedules included elsewhere in the Registration Statement;

- (3) read the 1965 minutes of the meetings of the stockholders, the Board of Directors, and the executive and finance committees of the Company as set forth in the minute books at June 25, 1965 (having previously read the 1964 minutes as a part of our examination of the financial statements for that year), officials of the Company having advised us that the minutes of all such meetings through that date were set forth therein; and
- (4) made inquiries of certain officials of the Company who have responsibility for financial and accounting matters as to whether the unaudited financial statements and schedules referred to above are fair presentations of the financial information they purport to show and have been prepared on a basis substantially consistent with the audited financial statements and schedules included in the Prospectus or elsewhere in the Registration Statement; and

with respect to the period from March 31, 1965 to June 25, 1965, as follows:

- (5) read the interim unaudited financial statements of the Company for the months of April and May 1965, officials of the Company having advised us that no such financial statements as of any date or for any period subsequent to May 31, 1965 were available;
- (6) read the 1965 minutes of meetings as set forth in (3) above; and
- (7) made inquiries of certain officials of the Company who have responsibility for financial and accounting matters, as to whether since March 31, 1965 there had been any change in the capital stock or funded debt of the Company or any material adverse change in its financial position or results of operations.

The foregoing procedures and inquiries do not constitute an examination made in accordance with generally accepted auditing standards; also they would not necessarily reveal material adverse changes in the financial position or results of operations

or inconsistencies in the application of generally accepted accounting principles.

We may state, however, that the foregoing procedures and inquiries did not cause us to believe that:

- (a) the unaudited financial statements and schedules, described above, included in the Prospectus or elsewhere in the Registration Statement are not fair presentations of the information they purport to show (but the subject matter of the qualification expressed in our opinion included in the Registration Statement and Prospectus is pertinent also to the unaudited financial statements), have not been prepared on a basis substantially consistent with the audited financial statements and schedules included therein, or fail to comply as to form in any material respect with the applicable accounting requirements of the Act and the published rules and regulations thereunder with respect to Registration Statements on Form S-1, or
- (b) during the period from March 31, 1965 to June 25, 1965 there was any change in the capital stock or funded debt of the Company, or any material adverse change in the financial position or results of operations, in each case from that set forth by the latest financial statements in the Prospectus, except in all instances as set forth in or contemplated by the Registration Statement and Prospectus or as occasioned by the declaration or payment of dividends.

The terms "financial position" and "results of operations" are used in this letter in their conventional accounting sense; accordingly, they relate to the financial statements of the business as a whole and have the same meaning when used in this letter as in our opinion contained in the Registration Statement and Prospectus.

This letter is solely for the information of the Company and the Underwriters and is not to be referred to in whole or in part in the Registration Statement or Prospectus or quoted by excerpt or reference outside the underwriting group in connection with the registration under the Act or the sale of securities,

except for any reference to it in an underwriting agreement or in any list of closing documents.

The statement entitled "Letters for Underwriters" was adopted unanimously by the twenty-one members of the committee.

NOTES

Unless otherwise indicated, Statements on Auditing Procedure present the considered opinion of the twenty-one members of the committee on auditing procedure, reached on a formal vote after examination of the subject matter by the committee and the technical services division. Except where formal adoption by the Council or the membership of the Institute has been asked and secured, the authority of the statements rests upon the general acceptability of the opinions so reached.

The committee on auditing procedure is the senior technical committee of the Institute designated to express opinions on auditing matters. While it is recognized that general rules may be subject to exception, the burden of justifying departures from the committee's recommendations must be assumed by those who adopt other practices.

COMMITTEE ON AUDITING PROCEDURE (1964-65)

ALBERT J. BOWS, JR., *Chairman*
 MARLIN P. ALT
 R. KIRK BATZER
 MILTON M. BROEKER
 FRANK H. EISEMAN
 HAROLD S. GELB
 OSCAR S. GELLEIN
 DAVID O. GILLETTE
 J. SPENCER GOULD
 WILLIAM J. HAJJAR
 NEWMAN T. HALVORSON

JAMES W. HENDRIX
 JACK D. KINGSOLVER
 ROBERT K. MAUTZ
 IRVING RICHARDSON
 JOSEPH L. ROTH
 L. I. SWINDELL
 JAMES W. THOKEY
 RALPH E. WALTERS
 IVAN M. WEST
 HOWARD G. WOMSLEY