Financial forecasts and projections; Statement on standards for accountants' services on prospective financial information, Oct. 1985

American Institute of Certified Public Accountants. Auditing Standards Board
Financial Forecasts and Projections

SUMMARY

This Statement provides that an accountant who either (1) submits to his clients or others prospective financial statements that he has assembled or assisted in assembling or (2) reports on prospective financial statements should either compile, examine, or apply agreed-upon procedures to the prospective financial statements, in accordance with this Statement, if those statements are, or reasonably might be, expected to be used by another (third) party.

Specifically, the Statement —

• Defines a “financial forecast” and a “financial projection.”
• Establishes procedures and reporting standards for a compilation service on prospective financial statements.
• Establishes procedures and reporting standards for an examination service on prospective financial statements. This service was described as a review in the 1980 AICPA guide, Guide for a Review of a Financial Forecast. This Statement renames the service and extends it to financial projections.
• Establishes standards for services to apply agreed-upon procedures to prospective financial statements.
Prohibits an accountant from compiling, examining, or applying agreed-upon procedures to prospective financial statements that omit a summary of significant assumptions. It also prohibits an accountant from consenting to the use of his name in conjunction with a financial projection if the projection is to be used by persons not negotiating directly with the responsible party unless the projection is used to supplement a forecast.

The Statement does not apply to services on "partial presentations" of prospective financial information, that is, presentations that do not meet the minimum presentation guidelines detailed in Appendix A of this Statement. In addition, this Statement does not apply to an accountant's services involving prospective financial statements that are restricted to internal use, those used solely in connection with litigation support services, or current year budgets presented with interim period financial statements.

STATEMENT

1. This Statement sets forth standards and provides guidance to accountants concerning performance and reporting for engagements to examine (paragraphs 27 through 48), compile (paragraphs 10 through 26), or apply agreed-upon procedures to (paragraphs 49 through 57) prospective financial statements.¹ This Statement is not applicable to presentations that do not meet the minimum presentation guidelines in Appendix A of this Statement. Such partial presentations are not deemed to be "prospective financial statements."

2. Whenever an accountant (a) submits, to his client or others, prospective financial statements that he has assembled, or assisted in assembling, that are, or reasonably might be, expected to be used by another (third) party ² or (b) reports on prospective financial statements that are, or reasonably might be, expected to be used by another (third) party, he should perform one of the engagements described in the preceding paragraph. In deciding whether the prospective financial statements are, or reasonably might be, expected to be used by a

¹The accountant should refer to rule 201(e) of the AICPA Code of Professional Ethics and the related interpretation 201-2, because this rule and interpretation are applicable to all engagements a member performs involving prospective financial information, including those engagements that are not covered by the provisions of this Statement.
²However, paragraph 58 permits an exception to this for certain types of budgets.
third party, the accountant may rely on either the written or oral representation of the responsible party, unless information comes to his attention that contradicts the responsible party’s representation. If such third party use of the prospective financial statements is not reasonably expected, the provisions of this Statement are not applicable unless the accountant has been engaged to examine, compile, or apply agreed-upon procedures to the prospective financial statements.

3. This Statement does not provide standards or procedures for engagements involving prospective financial statements used solely in connection with litigation support services, although it provides helpful guidance for many aspects of such engagements and may be referred to as useful guidance in such engagements. Litigation support services are engagements involving pending or potential formal legal proceedings before a “trier of fact” in connection with the resolution of a dispute between two or more parties, for example, in circumstances where an accountant acts as an expert witness. This exception is provided because, among other things, the accountant’s work in such proceedings is ordinarily subject to detailed analysis and challenge by each party to the dispute. This exception does not apply, however, if the prospective financial statements are for use by third parties who, under the rules of the proceedings, do not have the opportunity for such analysis and challenge. For example, creditors may not have such opportunities when prospective financial statements are submitted to them to secure their agreement to a plan of reorganization.

4. In reporting on prospective financial statements the accountant may be called on to assist the responsible party in identifying assumptions, gathering information, or assembling the statements.3 The responsible party is nonetheless responsible for the preparation and presentation of the prospective financial statements because the prospective financial statements are dependent on the actions, plans, and assumptions of the responsible party, and only it can take responsibility for the assumptions. Accordingly, the accountant’s engagement

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3Some of these services may not be appropriate if the accountant is to be named as the person reporting on an examination in a filing with the Securities and Exchange Commission (SEC). SEC Release Nos. 33-5992 and 34-15305, “Disclosure of Projections of Future Economic Performance,” state that for prospective financial statements filed with the commission, “a person should not be named as an outside reviewer if he actively assisted in the preparation of the projection.”
should not be characterized in his report or in the document containing his report as including “preparation” of the prospective financial statements. An accountant may be engaged to prepare a financial analysis of a potential project where the engagement includes obtaining the information, making appropriate assumptions, and assembling the presentation. Such an analysis is not, and should not be characterized as, a forecast or projection and would not be appropriate for general use. However, if the responsible party reviewed and adopted the assumptions and presentation, or based its assumptions and presentation on the analysis, the accountant could perform one of the engagements described in this Statement and issue a report appropriate for general use.

5. The concept of materiality affects the application of this Statement to prospective financial statements as materiality affects the application of generally accepted auditing standards to historical financial statements. Materiality is a concept that is judged in light of the expected range of reasonableness of the information; therefore, users should not expect prospective information (information about events that have not yet occurred) to be as precise as historical information.

Definitions

6. For the purposes of this Statement the following definitions apply.

Prospective financial statements. Either financial forecasts or financial projections including the summaries of significant assumptions and accounting policies. Although prospective financial statements may cover a period that has partially expired, statements for periods that have completely expired are not considered to be prospective financial statements. Pro forma financial statements4 and partial presentations5 are not considered to be prospective financial statements.

4 "Pro forma" financial presentations are designed to demonstrate the effect of a future or hypothetical transaction by showing how it might have affected the historical financial statements if it had been consummated during the period covered by those statements. Although the transactions in question are prospective, this Statement does not apply to such presentations because they are essentially historical financial statements and do not purport to be prospective financial statements.

5 Partial presentations are presentations that do not meet the minimum presentation guidelines in Appendix A of this Statement.
Financial forecast. Prospective financial statements that present, to the best of the responsible party’s knowledge and belief, an entity’s expected financial position, results of operations, and changes in financial position. A financial forecast is based on the responsible party’s assumptions reflecting conditions it expects to exist and the course of action it expects to take. A financial forecast may be expressed in specific monetary amounts as a single point estimate of forecasted results or as a range, where the responsible party selects key assumptions to form a range within which it reasonably expects, to the best of its knowledge and belief, the item or items subject to the assumptions to actually fall. When a forecast contains a range, the range is not selected in a biased or misleading manner, for example, a range in which one end is significantly less expected than the other. Minimum presentation guidelines for prospective financial statements are set forth in Appendix A of this Statement.

Financial projection. Prospective financial statements that present, to the best of the responsible party’s knowledge and belief, given one or more hypothetical assumptions, an entity’s expected financial position, results of operations, and changes in financial position. A financial projection is sometimes prepared to present one or more hypothetical courses of action for evaluation, as in response to a question such as “What would happen if . . . ?” A financial projection is based on the responsible party’s assumptions reflecting conditions it expects would exist and the course of action it expects would be taken, given one or more hypothetical assumptions. A projection, like a forecast, may contain a range. Minimum presentation guidelines for prospective financial statements are set forth in Appendix A of this Statement.

Entity. Any unit, existing or to be formed, for which financial statements could be prepared in accordance with generally accepted accounting principles or another comprehensive basis of accounting. For example, an entity can be an individual, partnership, corporation, trust, estate, association, or governmental unit.

Hypothetical assumption. An assumption used in a financial projection to present a condition or course of action that is not necessarily expected to occur, but is consistent with the purpose of the projection.

*Statement on Auditing Standards (SAS) No. 14, Special Reports, discusses comprehensive bases of accounting other than generally accepted accounting principles.*
**Responsible party.** The person or persons who are responsible for the assumptions underlying the prospective financial statements. The responsible party usually is management, but it can be persons outside of the entity who do not currently have the authority to direct operations (for example, a party considering acquiring the entity).

**Assembly.** The manual or computer processing of mathematical or other clerical functions related to the presentation of the prospective financial statements. Assembly does not refer to the mere reproduction and collation of such statements or to the responsible party’s use of the accountant’s computer processing hardware or software.

**Key factors.** The significant matters on which an entity’s future results are expected to depend. Such factors are basic to the entity’s operations and thus encompass matters that affect, among other things, the entity’s sales, production, service, and financing activities. Key factors serve as a foundation for prospective financial statements and are the bases for the assumptions.

## Uses of Prospective Financial Statements

7. Prospective financial statements are for either “general use” or “limited use.” “General use” of prospective financial statements refers to use of the statements by persons with whom the responsible party is not negotiating directly, for example, in an offering statement of an entity’s debt or equity interests. Because recipients of prospective financial statements distributed for general use are unable to ask the responsible party directly about the presentation, the presentation most useful to them is one that portrays, to the best of the responsible party’s knowledge and belief, the expected results. Thus, only a financial forecast is appropriate for general use.

8. “Limited use” of prospective financial statements refers to use of prospective financial statements by the responsible party alone or by the responsible party and third parties with whom the responsible party is negotiating directly. Examples include use in negotiations for a bank loan, submission to a regulatory agency, and use solely within the entity. Third-party recipients of prospective financial statements intended for limited use can ask questions of the responsible party and negotiate terms directly with it. Any type of prospective financial statements that would be useful in the circumstances would normally
be appropriate for limited use. Thus, the presentation may be a financial forecast or a financial projection.

9. Because a financial projection is not appropriate for general use, an accountant should not consent to the use of his name in conjunction with a financial projection that he believes will be distributed to those who will not be negotiating directly with the responsible party, for example, in an offering statement of an entity’s debt or equity interests, unless the projection is used to supplement a financial forecast.

Compilation of Prospective Financial Statements

10. A compilation of prospective financial statements is a professional service that involves —

a. Assembling, to the extent necessary, the prospective financial statements based on the responsible party's assumptions.

b. Performing the required compilation procedures,7 including reading the prospective financial statements with their summaries of significant assumptions and accounting policies, and considering whether they appear to be (i) presented in conformity with AICPA presentation guidelines8 and (ii) not obviously inappropriate.

c. Issuing a compilation report.

11. A compilation is not intended to provide assurance on the prospective financial statements or the assumptions underlying such statements. Because of the limited nature of the accountant's procedures, a compilation does not provide assurance that the accountant will become aware of significant matters that might be disclosed by more extensive procedures, for example, those performed in an examination of prospective financial statements.

12. The summary of significant assumptions is essential to the reader's understanding of prospective financial statements. Accordingly, the accountant should not compile prospective financial statements

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7 See Appendix B, paragraph 5, for the required procedures.

8 AICPA presentation guidelines are detailed in the AICPA Guide for Prospective Financial Statements.
that exclude disclosure of the summary of significant assumptions. Also, the accountant should not compile a financial projection that excludes (a) an identification of the hypothetical assumptions or (b) a description of the limitations on the usefulness of the presentation.

13. The following standards apply to a compilation of prospective financial statements and to the resulting report:

a. The compilation should be performed by a person or persons having adequate technical training and proficiency to compile prospective financial statements.

b. Due professional care should be exercised in the performance of the compilation and the preparation of the report.

c. The work should be adequately planned, and assistants, if any, should be properly supervised.

d. Applicable compilation procedures should be performed as a basis for reporting on the compiled prospective financial statements. (See Appendix B for the procedures to be performed.)

e. The report based on the accountant’s compilation of prospective financial statements should conform to the applicable guidance in paragraphs 16 through 26 of this Statement.

14. The accountant should consider, after applying the procedures specified in Appendix B, whether representations or other information he has received appear to be obviously inappropriate, incomplete, or otherwise misleading, and if so, the accountant should attempt to obtain additional or revised information. If he does not receive such information, the accountant should ordinarily withdraw from the compilation engagement.9 (Note that the omission of disclosures, other than those relating to significant assumptions, would not require the accountant to withdraw, see paragraph 24.)

**Working Papers**

15. Although it is not possible to specify the form or content of the working papers that an accountant should prepare in connection with a compilation of prospective financial statements because of the differ-

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9 The accountant need not withdraw from the engagement if the effect of such information on the prospective financial statement does not appear to be material.
ent circumstances of individual engagements, the accountant’s working papers ordinarily should indicate that —

a. The work was adequately planned and supervised.

b. The required compilation procedures were performed as a basis for the compilation report.

**Reports on Compiled Prospective Financial Statements**

16. The accountant’s standard report on a compilation of prospective financial statements should include —

a. An identification of the prospective financial statements presented by the responsible party.

b. A statement that the accountant has compiled the prospective financial statements in accordance with standards established by the American Institute of Certified Public Accountants.

c. A statement that a compilation is limited in scope and does not enable the accountant to express an opinion or any other form of assurance on the prospective financial statements or the assumptions.

d. A caveat that the prospective results may not be achieved.

e. A statement that the accountant assumes no responsibility to update the report for events and circumstances occurring after the date of the report.

17. The following is the form of the accountant’s standard report on the compilation of a forecast that does not contain a range.\(^{10}\)

We have compiled the accompanying forecasted balance sheet, statements of income, retained earnings, and changes in financial position of XYZ Company as of December 31, 19XX, and for the year then ending, in accordance with standards established by the American Institute of Certified Public Accountants.\(^ {11}\)

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\(^{10}\) The forms of reports provided in this Statement are appropriate whether the presentation is based on generally accepted accounting principles or on another comprehensive basis of accounting.

\(^{11}\) When the presentation is summarized as discussed in Appendix A of this Statement, this sentence might read “We have compiled the accompanying summarized forecast of XYZ Company as of December 31, 19XX, and for the year then ending, in accordance with standards established by the American Institute of Certified Public Accountants.”
A compilation is limited to presenting in the form of a forecast information that is the representation of management and does not include evaluation of the support for the assumptions underlying the forecast. We have not examined the forecast and, accordingly, do not express an opinion or any other form of assurance on the accompanying statements or assumptions. Furthermore, there will usually be differences between the forecasted and actual results, because events and circumstances frequently do not occur as expected, and those differences may be material. We have no responsibility to update this report for events and circumstances occurring after the date of this report.

18. When the presentation is a projection, the accountant's report should include a separate paragraph that describes the limitations on the usefulness of the presentation. The following is the form of the accountant's standard report on a compilation of a projection that does not contain a range.

We have compiled the accompanying projected balance sheet, statements of income, retained earnings, and changes in financial position of XYZ Company as of December 31, 19XX, and for the year then ending, in accordance with standards established by the American Institute of Certified Public Accountants.13

The accompanying projection and this report were prepared for [state special purpose, for example, "the DEF National Bank for the purpose of negotiating a loan to expand XYZ Company's plant,"] and should not be used for any other purpose.

A compilation is limited to presenting in the form of a projection information that is the representation of management and does not include evaluation of the support for the assumptions underlying the projection. We have not examined the projection and, accordingly, do not express an opinion or any other form of assurance on the accompanying statements or assumptions. Furthermore, even if [describe hypothetical assumption, for example, "the loan is granted and the plant is expanded."], there will usually be differences between the projected and

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13When the responsible party is other than management, the references to management in the standard reports provided in this Statement should be changed to refer to the party who assumes responsibility for the assumptions.

19When the presentation is summarized as discussed in Appendix A of this Statement, this sentence might read "We have compiled the accompanying summarized projection of XYZ Company as of December 31, 19XX, and for the year then ending, in accordance with standards established by the American Institute of Certified Public Accountants."
actual results, because events and circumstances frequently do not occur as expected, and those differences may be material. We have no responsibility to update this report for events and circumstances occurring after the date of this report.

19. When the prospective financial statements contain a range, the accountant's standard report should also include a separate paragraph that states that the responsible party has elected to portray the expected results of one or more assumptions as a range. The following is an example of the separate paragraph to be added to the accountant's report when he compiles prospective financial statements, in this case a forecast, that contain a range.

As described in the summary of significant assumptions, management of XYZ Company has elected to portray forecasted (describe financial statement element or elements for which the expected results of one or more assumptions fall within a range, and identify the assumptions expected to fall within a range, for example, "revenue at the amounts of $X,XXX and $Y,YYY, which is predicated upon occupancy rates of XX percent and YY percent of available apartments," rather than as a single point estimate. Accordingly, the accompanying forecast presents forecasted financial position, results of operations, and changes in financial position (describe one or more assumptions expected to fall within a range, for example, "at such occupancy rates.") However, there is no assurance that the actual results will fall within the range of (describe one or more assumptions expected to fall within a range, for example, "occupancy rates") presented.

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

21. An accountant may compile prospective financial statements for an entity with respect to which he is not independent. In such circumstances, the accountant should specifically disclose his lack of independence; however, the reason for the lack of independence should not be described. When the accountant is not independent, he may give the standard compilation report but should include the following sentence after the last paragraph.

We are not independent with respect to XYZ Company.

14 In making a judgment about whether he is independent, the accountant should be guided by the AICPA Code of Professional Ethics. Also, see the auditing interpretation "Applicability of Guidance on Reporting When Not Independent" (AICPA, Professional Standards, vol. 1., AU sec. 9504.19-.22).
22. Prospective financial statements may be included in a document that also contains historical financial statements and the accountant's report thereon. In addition, the historical financial statements that appear in the document may be summarized and presented with the prospective financial statements for comparative purposes. An example of the reference to the accountant's report on the historical financial statements when he examined, reviewed, or compiled those statements is presented below.

(concluding sentence of last paragraph)

The historical financial statements for the year ended December 31, 19XX, (from which the historical data are derived) and our report thereon are set forth on pages xx-xx of this document.

23. In some circumstances, an accountant may wish to expand his report to emphasize a matter regarding the prospective financial statements. Such information may be presented in a separate paragraph of the accountant's report. However, the accountant should exercise care that emphasizing such a matter does not give the impression that he is expressing assurance or expanding the degree of responsibility he is taking with respect to such information. For example, the accountant should not include statements in his compilation report about the mathematical accuracy of the statements or their conformity with presentation guidelines.

**Modifications of the Standard Compilation Report**

24. An entity may request an accountant to compile prospective financial statements that contain presentation deficiencies or omit dis-
closures other than those relating to significant assumptions. The accountant may compile such prospective financial statements provided the deficiency or omission is clearly indicated in his report and is not, to his knowledge, undertaken with the intention of misleading those who might reasonably be expected to use such statements.

25. Notwithstanding the above, if the compiled prospective financial statements are presented on a comprehensive basis of accounting other than generally accepted accounting principles and do not include disclosure of the basis of accounting used, the basis should be disclosed in the accountant's report.

26. The following is an example of a paragraph that should be added to a report on compiled prospective financial statements, in this case a financial forecast, in which the summary of significant accounting policies has been omitted.

Management has elected to omit the summary of significant accounting policies required by the guidelines for presentation of a forecast established by the American Institute of Certified Public Accountants. If the omitted disclosures were included in the forecast, they might influence the user's conclusions about the Company's financial position, results of operations, and changes in financial position for the forecast period. Accordingly, this forecast is not designed for those who are not informed about such matters.

**Examination of Prospective Financial Statements**

27. An examination of prospective financial statements is a professional service that involves —

a. Evaluating the preparation of the prospective financial statements.

b. Evaluating the support underlying the assumptions.

c. Evaluating the presentation of the prospective financial statements for conformity with AICPA presentation guidelines.¹⁸

d. Issuing an examination report.

¹⁸AICPA presentation guidelines are detailed in the AICPA Guide for Prospective Financial Statements.
28. As a result of his examination, the accountant has a basis for reporting on whether, in his opinion —
   a. The prospective financial statements are presented in conformity with AICPA guidelines.
   b. The assumptions provide a reasonable basis for the responsible party's forecast, or whether the assumptions provide a reasonable basis for the responsible party's projection given the hypothetical assumptions.

29. The accountant should be independent; have adequate technical training and proficiency to examine prospective financial statements; adequately plan the engagement and supervise the work of assistants, if any; and obtain sufficient evidence to provide a reasonable basis for his examination report. (See Appendix C of this Statement for standards concerning such technical training and proficiency, planning the examination engagement, and the types of procedures an accountant should perform to obtain sufficient evidence for his examination report.)

Working Papers

30. The accountant's working papers in connection with his examination of prospective financial statements should be appropriate to the circumstances and the accountant's needs on the engagement to which they apply. Although the quantity, type, and content of working papers vary with the circumstances, they ordinarily should indicate that —
   a. The work was adequately planned and supervised.
   b. The process by which the entity develops its prospective financial statements was considered in determining the scope of the examination.
   c. Sufficient evidence was obtained to provide a reasonable basis for the accountant's report.

Reports on Examined Prospective Financial Statements

31. The accountant's standard report on an examination of prospective financial statements should include —
   a. An identification of the prospective financial statements presented.
   b. A statement that the examination of the prospective financial
statements was made in accordance with AICPA standards and a brief description of the nature of such an examination.

c. The accountant's opinion that the prospective financial statements are presented in conformity with AICPA presentation guidelines19 and that the underlying assumptions provide a reasonable basis for the forecast or a reasonable basis for the projection given the hypothetical assumptions.

d. A caveat that the prospective results may not be achieved.

e. A statement that the accountant assumes no responsibility to update the report for events and circumstances occurring after the date of the report.

32. The following is the form of the accountant's standard report on an examination of a forecast that does not contain a range.

We have examined the accompanying forecasted balance sheet, statements of income, retained earnings, and changes in financial position of XYZ Company as of December 31, 19XX, and for the year then ending.20 Our examination was made in accordance with standards for an examination of a forecast established by the American Institute of Certified Public Accountants and, accordingly, included such procedures as we considered necessary to evaluate both the assumptions used by management and the preparation and presentation of the forecast.

In our opinion, the accompanying forecast is presented in conformity with guidelines for presentation of a forecast established by the American Institute of Certified Public Accountants, and the underlying assumptions provide a reasonable basis for management's forecast. However, there will usually be differences between the forecasted and actual results, because events and circumstances frequently do not occur as expected, and those differences may be material. We have no responsibility to update this report for events and circumstances occurring after the date of this report.

33. When an accountant examines a projection, his opinion regarding the assumptions should be conditioned on the hypothetical assumptions.

19 The accountant’s report need not comment on the consistency of the application of accounting principles as long as the presentation of any change in accounting principles is in conformity with AICPA presentation guidelines as detailed in the AICPA Guide for Prospective Financial Statements.

20 When the presentation is summarized as discussed in Appendix A of this Statement, this sentence might read “We have examined the accompanying summarized forecast of XYZ Company as of December 31, 19XX, and for the year then ending.”
assumptions; that is, he should express an opinion on whether the assumptions provide a reasonable basis for the projection given the hypothetical assumptions. Also, his report should include a separate paragraph that describes the limitations on the usefulness of the presentation. The following is the form of the accountant's standard report on an examination of a projection that does not contain a range.

We have examined the accompanying projected balance sheet, statements of income, retained earnings, and changes in financial position of XYZ Company as of December 31, 19XX, and for the year then ending.21 Our examination was made in accordance with standards for an examination of a projection established by the American Institute of Certified Public Accountants and, accordingly, included such procedures as we considered necessary to evaluate both the assumptions used by management and the preparation and presentation of the projection.

The accompanying projection and this report were prepared for [state special purpose, for example, "the DEF National Bank for the purpose of negotiating a loan to expand XYZ Company's plant,"] and should not be used for any other purpose.

In our opinion, the accompanying projection is presented in conformity with guidelines for presentation of a projection established by the American Institute of Certified Public Accountants, and the underlying assumptions provide a reasonable basis for management's projection [describe the hypothetical assumption, for example, "assuming the granting of the requested loan for the purpose of expanding XYZ Company's plant as described in the summary of significant assumptions."] However, even if [describe hypothetical assumption, for example, "the loan is granted and the plant is expanded,"] there will usually be differences between the projected and actual results, because events and circumstances frequently do not occur as expected, and those differences may be material. We have no responsibility to update this report for events and circumstances occurring after the date of this report.

34. When the prospective financial statements contain a range, the accountant's standard report should also include a separate paragraph that states that the responsible party has elected to portray the expected results of one or more assumptions as a range. The following is an example of the separate paragraph to be added to the accountant's report when he examines prospective financial statements, in this case a forecast, that contain a range.

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21When the presentation is summarized as discussed in Appendix A of this Statement, this sentence might read "We have examined the accompanying summarized projection of XYZ Company as of December 31, 19XX, and for the year then ending."
As described in the summary of significant assumptions, management of XYZ Company has elected to portray forecasted ([describe financial statement element or elements for which the expected results of one or more assumptions fall within a range, and identify assumptions expected to fall within a range, for example, “revenue at the amounts of $X,XXX and $Y,YYY, which is predicated upon occupancy rates of XX percent and YY percent of available apartments,”] rather than as a single point estimate. Accordingly, the accompanying forecast presents forecasted financial position, results of operations and changes in financial position ([describe one or more assumptions expected to fall within a range, for example, “at such occupancy rates.”]) However, there is no assurance that the actual results will fall within the range of ([describe one or more assumptions expected to fall within a range, for example, “occupancy rates”]) presented.

35. The date of completion of the accountant’s examination procedures should be used as the date of the report.

**Modifications to the Accountant’s Opinion**

36. The following circumstances result in the following types of modified accountant’s report involving the accountant’s opinion:

a. If, in the accountant’s opinion, the prospective financial statements depart from AICPA presentation guidelines, he should issue a qualified opinion (see paragraph 37) or an adverse opinion (see paragraph 39). However, if the presentation departs from the presentation guidelines because it fails to disclose assumptions that appear to be significant the accountant should issue an adverse opinion (see paragraphs 39 and 40).

b. If the accountant believes that one or more significant assumptions do not provide a reasonable basis for the forecast, or a reasonable basis for the projection given the hypothetical assumptions, he should issue an adverse opinion (see paragraph 39).

c. If the accountant’s examination is affected by conditions that preclude application of one or more procedures he considers necessary in the circumstances, he should disclaim an opinion and describe the scope limitation in his report (see paragraph 41).

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22 However, the accountant may issue the standard examination report on a financial forecast filed with the SEC that meets the presentation requirements of article XI of Regulation S-X.
37. **Qualified Opinion.** In a qualified opinion, the accountant should state, in a separate paragraph, all of his substantive reasons for modifying his opinion and describe the departure from AICPA presentation guidelines. His opinion should include the words "except" or "exception" as the qualifying language and should refer to the separate explanatory paragraph. The following is an example of an examination report on a forecast that is at variance with AICPA guidelines for presentation of a financial forecast.

We have examined the accompanying forecasted balance sheet, statements of income, retained earnings, and changes in financial position of XYZ Company as of December 31, 19XX, and for the year then ending. Our examination was made in accordance with standards for an examination of a forecast established by the American Institute of Certified Public Accountants and, accordingly, included such procedures as we considered necessary to evaluate both the assumptions used by management and the preparation and presentation of the forecast.

The forecast does not disclose reasons for the significant variation in the relationship between income tax expense and pretax accounting income as required by generally accepted accounting principles.

In our opinion, except for the omission of the disclosure of the reasons for the significant variation in the relationship between income tax expense and pretax accounting income as discussed in the preceding paragraph, the accompanying forecast is presented in conformity with guidelines for presentation of a forecast established by the American Institute of Certified Public Accountants and the underlying assumptions provide a reasonable basis for management’s forecast. However, there will usually be differences between the forecasted and actual results, because events and circumstances frequently do not occur as expected, and those differences may be material. We have no responsibility to update this report for events and circumstances occurring after the date of this report.

38. Because of the nature, sensitivity, and interrelationship of prospective information, a reader would find an accountant’s report qualified for a measurement departure, the reasonableness of the underlying assumptions, or a scope limitation difficult to interpret. Accordingly, the accountant should not express his opinion about these

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23An example of a measurement departure is the failure to capitalize a capital lease in a forecast where the historical financial statements for the prospective period are expected to be presented in conformity with generally accepted accounting principles.
items with language such as "except for . . ." or "subject to the effects of . . . ." Rather, when a measurement departure, an unreasonable assumption, or a limitation on the scope of the accountant's examination has led him to conclude that he cannot issue an unqualified opinion, he should issue the appropriate type of modified opinion described in paragraphs 39 through 42.

39. **Adverse Opinion.** In an adverse opinion the accountant should state, in a separate paragraph, all of his substantive reasons for his adverse opinion. His opinion should state that the presentation is not in conformity with presentation guidelines and should refer to the explanatory paragraph. When applicable, his opinion paragraph should also state that, in the accountant's opinion, the assumptions do not provide a reasonable basis for the prospective financial statements. An example of an adverse opinion on an examination of prospective financial statements is set forth below. In this case, a financial forecast was examined and the accountant's opinion was that a significant assumption was unreasonable. The example should be revised as appropriate for a different type of presentation or if the adverse opinion is issued because the statements do not conform to the presentation guidelines.

We have examined the accompanying forecasted balance sheet, statements of income, retained earnings, and changes in financial position of XYZ Company as of December 31, 19XX, and for the year then ending. Our examination was made in accordance with standards for an examination of a financial forecast established by the American Institute of Certified Public Accountants and, accordingly, included such procedures as we considered necessary to evaluate both the assumptions used by management and the preparation and presentation of the forecast.

As discussed under the caption "Sales" in the summary of significant forecast assumptions, the forecasted sales include, among other things, revenue from the Company's federal defense contracts continuing at the current level. The Company's present federal defense contracts will expire in March 19XX. No new contracts have been signed and no negotiations are under way for new federal defense contracts. Furthermore, the federal government has entered into contracts with another company to supply the items being manufactured under the Company's present contracts.

In our opinion, the accompanying forecast is not presented in conformity with guidelines for presentation of a financial forecast established by the American Institute of Certified Public Accountants because management's assumptions, as discussed in the preceding paragraph, do not
provide a reasonable basis for management's forecast. We have no responsibility to update this report for events or circumstances occurring after the date of this report.

40. If the presentation, including the summary of significant assumptions, fails to disclose assumptions that, at the time, appear to be significant, the accountant should describe the assumptions in his report and issue an adverse opinion. The accountant should not examine a presentation that omits all disclosures of assumptions. Also, the accountant should not examine a financial projection that omits (a) an identification of the hypothetical assumptions or (b) a description of the limitations on the usefulness of the presentation.

41. Disclaimer of Opinion. In a disclaimer of opinion the accountant's report should indicate, in a separate paragraph, the respects in which the examination did not comply with standards for an examination. The accountant should state that the scope of the examination was not sufficient to enable him to express an opinion with respect to the presentation or the underlying assumptions, and his disclaimer of opinion should include a direct reference to the explanatory paragraph. The following is an example of a report on an examination of prospective financial statements, in this case a financial forecast, for which a significant assumption could not be evaluated.

We have examined the accompanying forecasted balance sheet, statements of income, retained earnings, and changes in financial position of XYZ Company as of December 31, 19XX, and for the year then ending. Except as explained in the following paragraph, our examination was made in accordance with standards for an examination of a financial forecast established by the American Institute of Certified Public Accountants and, accordingly, included such procedures as we considered necessary to evaluate both the assumptions used by management and the preparation and presentation of the forecast.

As discussed under the caption "Income From Investee" in the summary of significant forecast assumptions, the forecast includes income from an equity investee constituting 23 percent of forecasted net income, which is management's estimate of the Company's share of the investee's income to be accrued for 19XX. The investee has not prepared a forecast for the year ending December 31, 19XX, and we were therefore unable to obtain suitable support for this assumption.

Because, as described in the preceding paragraph, we are unable to evaluate management's assumption regarding income from an equity investee and other assumptions that depend thereon, we express no opinion with respect to the presentation of or the assumptions underly-
ing the accompanying forecast. We have no responsibility to update this report for events and circumstances occurring after the date of this report.

42. When there is a scope limitation and the accountant also believes there are material departures from the presentation guidelines, those departures should be described in the accountant's report.

Other Modifications to the Standard Examination Report

43. The circumstances described below, although not necessarily resulting in modifications to the accountant's opinion, would result in the following types of modifications to the standard examination report.

44. *Emphasis of a Matter.* In some circumstances, the accountant may wish to emphasize a matter regarding the prospective financial statements but nevertheless intends to issue an unqualified opinion. The accountant may present other information and comments he wishes to include, such as explanatory comments or other informative material, in a separate paragraph of his report.

45. *Evaluation Based in Part on a Report of Another Accountant.* When more than one accountant is involved in the examination, the guidance provided for that situation in connection with examinations of historical financial statements is generally applicable. When the principal accountant decides to refer to the report of another accountant as a basis, in part, for his own opinion, he should disclose that fact in stating the scope of the examination and should refer to the report of the other accountant in expressing his opinion. Such a reference indicates the division of responsibility for the performance of the examination.

46. *Comparative Historical Financial Information.* Prospective financial statements may be included in a document that also contains historical financial statements and an accountant's report thereon. The accountant's responsibility with respect to those historical financial statements upon which he is not engaged to perform a professional service is described in SAS No. 26, *Association With Financial Statements*, in the case of public entities, and SSARS No. 1, *Compilation and Review of Financial Statements*, paragraphs 5 through 7, in the case of nonpublic entities.
ment may be summarized and presented with the prospective financial statements for comparative purposes.\textsuperscript{25} An example of the reference to the accountant's report on the historical financial statements when he examined, reviewed, or compiled those statements is presented in paragraph 22.

47. \textit{Reporting When the Examination Is Part of a Larger Engagement}. When the accountant's examination of prospective financial statements is part of a larger engagement, for example, a financial feasibility study or business acquisition study, it is appropriate to expand the report on the examination of the prospective financial statements to describe the entire engagement.

48. The following is a report that might be issued when an accountant chooses to expand his report on a financial feasibility study.\textsuperscript{26}

\begin{itemize}
  \item \textbf{a.} The Board of Directors
  Example Hospital
  Example, Texas
  
  \item \textbf{b.} We have prepared a financial feasibility study of Example Hospital's plans to expand and renovate its facilities. The study was undertaken to evaluate the ability of Example Hospital (the Hospital) to meet the Hospital's operating expenses, working capital needs, and other financial requirements, including the debt service requirements associated with the proposed $25,000,000 \textit{[legal title of bonds]} issue, at an assumed average annual interest rate of 10.0 percent during the five years ending December 31, 19X6.
\end{itemize}

\textsuperscript{25}SAS No. 42, \textit{Reporting on Condensed Financial Statements and Selected Financial Data}, discusses the accountant's report for summarized financial statements derived from audited financial statements that are not included in the same document.

\textsuperscript{26}Although the entity referred to in the report is a hospital, the form of report is also applicable to other entities such as hotels or stadiums. Also, although the illustrated report format and language should not be departed from in any significant way, the language used should be tailored to fit the circumstances that are unique to a particular engagement (for example, the description of the proposed capital improvement program, paragraph c; the proposed financing of the program, paragraphs b and d; the specific procedures applied by the accountant, paragraph e; and any explanatory comments included in emphasis-of-a-matter paragraphs, paragraph i, which deals with general matter; and paragraph j, which deals with specific matters).
c. The proposed capital improvements program (the Program) consists of a new two-level addition, which is to provide fifty additional medical-surgical beds, increasing the complement to 275 beds. In addition, various administrative and support service areas in the present facilities are to be remodeled. The Hospital administration anticipates that construction is to begin June 30, 19X2, and to be completed by December 31, 19X3.

d. The estimated total cost of the Program is approximately $30,000,000. It is assumed that the $25,000,000 of revenue bonds that the Example Hospital Finance Authority proposes to issue would be the primary source of funds for the Program. The responsibility for payment of debt service on the bonds is solely that of the Hospital. Other necessary funds to finance the Program are assumed to be provided from the Hospital's funds, from a local fund drive, and from interest earned on funds held by the bond trustee during the construction period.

e. Our procedures included analysis of—
   • Program history, objectives, timing and financing.
   • The future demand for the Hospital's services, including consideration of—
     Economic and demographic characteristics of the Hospital's defined service area.
     Locations, capacities, and competitive information pertaining to other existing and planned area hospitals.
     Physician support for the Hospital and its programs.
     Historical utilization levels.
   • Planning agency applications and approvals.
   • Construction and equipment costs, debt service requirements, and estimated financing costs.
   • Staffing patterns and other operating considerations.
   • Third-party reimbursement policy and history.
   • Revenue/expense/volume relationships.

f. We also participated in gathering other information, assisted management in identifying and formulating its assumptions, and assembled the accompanying financial forecast based on those assumptions.

g. The accompanying financial forecast for the annual periods ending December 31, 19X2, through 19X6, is based on assumptions that
were provided by or reviewed with and approved by management. The financial forecast includes —

- Balance sheets.
- Statements of revenues and expenses.
- Statements of changes in financial position.
- Statements of changes in fund balance.

h. We have examined the financial forecast. Our examination was made in accordance with standards for an examination of a financial forecast established by the American Institute of Certified Public Accountants and, accordingly, included such procedures as we considered necessary to evaluate both the assumptions used by management and the preparation and presentation of the forecast.

i. Legislation and regulations at all levels of government have affected and may continue to affect revenues and expenses of hospitals. The financial forecast is based on legislation and regulations currently in effect. If future legislation or regulations related to hospital operations are enacted, such legislation or regulations could have a material effect on future operations.

j. The interest rate, principal payments, Program costs, and other financing assumptions are described in the section entitled "Summary of Significant Forecast Assumptions and Rationale." If actual interest rates, principal payments, and funding requirements are different from those assumed, the amount of the bond issue and debt service requirements would need to be adjusted accordingly from those indicated in the forecast. If such interest rates, principal payments, and funding requirements are lower than those assumed, such adjustments would not adversely affect the forecast.

k. Our conclusions are presented below.

- In our opinion, the accompanying financial forecast is presented in conformity with guidelines for presentation of a financial forecast established by the American Institute of Certified Public Accountants.

- In our opinion, the underlying assumptions provide a reasonable basis for management's forecast. However, there will usually be differences between the forecasted and actual results, because events and circumstances frequently do not occur as expected, and those differences may be material.

- The accompanying financial forecast indicates that sufficient funds could be generated to meet the Hospital's operating
expenses, working capital needs, and other financial requirements, including the debt service requirements associated with the proposed $25,000,000 bond issue, during the forecast periods. However, the achievement of any financial forecast is dependent on future events, the occurrence of which cannot be assured.

l. We have no responsibility to update this report for events and circumstances occurring after the date of this report.

Applying Agreed-Upon Procedures to Prospective Financial Statements

49. An accountant may accept an engagement to apply agreed-upon procedures to prospective financial statements provided that (a) the specified users involved have participated in establishing the nature and scope of the engagement and take responsibility for the adequacy of the procedures to be performed, (b) distribution of the report is to be restricted to the specified users involved, and (c) the prospective financial statements include a summary of significant assumptions.

50. The accountant who accepts an engagement to apply agreed-upon procedures to prospective financial statements should be independent; have adequate technical training and proficiency to apply agreed-upon procedures to prospective financial statements; adequately plan the engagement and supervise the work of assistants, if any; and obtain sufficient evidence to provide a reasonable basis for his report on the results of applying the agreed-upon procedures.

51. The accountant’s procedures generally may be as limited or extensive as the specified users desire as long as the specified users take responsibility for their adequacy. However, mere reading of prospective financial statements does not constitute a procedure sufficient to permit an accountant to report on the results of applying agreed-upon procedures to such statements.

52. To satisfy the requirement that the specified users involved participate in establishing the nature and scope of the engagement and take responsibility for the adequacy of the procedures to be performed, the accountant ordinarily should meet with the specified users involved to discuss the procedures to be followed. This discussion may
include describing, to the specified users, procedures that are frequently followed in similar types of engagements. Sometimes the accountant may not be able to discuss the procedures directly with all of the specified users who will receive the report. In such circumstances, the accountant may satisfy the requirement that the specified users involved take responsibility for the adequacy of the procedures by applying any one of the following or similar procedures:

a. Discussing the procedures to be applied with legal counsel or other appropriate designated representatives of the users involved, such as, a trustee, a receiver, or a creditors’ committee

b. Reviewing relevant correspondence from the specified users

c. Comparing the procedures to be applied to written requirements of a supervisory agency

d. Distributing a draft of the report or a copy of the client’s engagement letter to the specified users involved with a request for their comments before the report is issued

Working Papers

53. Although it is not possible to specify the form or content of the working papers that an accountant should prepare in connection with an engagement to apply agreed-upon procedures to prospective financial statements because of the different circumstances of individual engagements, the accountant’s working papers ordinarily should indicate that —

a. The work was adequately planned and supervised.

b. The agreed-upon procedures were performed as a basis for the report.

Reports on the Results of Applying Agreed-Upon Procedures

54. The accountant’s report on the results of applying agreed-upon procedures should —

a. Indicate the prospective financial statements covered by the accountant’s report.

b. Indicate that the report is limited in use, intended solely for the specified users, and should not be used by others.

c. Enumerate the procedures performed and refer to conformity with the arrangements made with the specified users.
d. If the agreed-upon procedures are less than those performed in an examination, state that the work performed was less in scope than an examination of prospective financial statements in accordance with AICPA standards and disclaim an opinion on whether the presentation of the prospective financial statements is in conformity with AICPA presentation guidelines and on whether the underlying assumptions provide a reasonable basis for the forecast, or a reasonable basis for the projection given the hypothetical assumptions.

e. State the accountant's findings.

f. Include a caveat that the prospective results may not be achieved.

g. State that the accountant assumes no responsibility to update the report for events and circumstances occurring after the date of the report.

55. Also, the accountant may wish to state in his report that he makes no representation about the sufficiency of the procedures for the specified users' purposes.

56. When the accountant reports on the results of applying agreed-upon procedures, he should not express any form of negative assurance on the prospective financial statements taken as a whole.

57. The following two exhibits illustrate reports that might be issued when the engagement is limited to applying agreed-upon procedures to the prospective financial statements.

**Exhibit 1**

**Board of Directors—XYZ Corporation**

**Board of Directors—ABC Company**

At your request, we have performed certain agreed-upon procedures, as enumerated below, with respect to the forecasted balance sheet, statements of income, retained earnings and changes in financial position of DEF Company, a subsidiary of ABC Company, as of December 31, 19XX, and for the year then ending. These procedures, which were specified by the Boards of Directors of XYZ Corporation and ABC Company, were performed solely to assist you in connection with the proposed sale of DEF Company to XYZ Corporation. It is understood that this report is solely for your information and should not be used by those who did not participate in determining the procedures.

a. With respect to forecasted rental income, we compared the assumptions about expected demand for rental of the housing units to demand for similar housing units at similar rental prices in the city area in which DEF Company's housing units are located.
b. We tested the forecast for mathematical accuracy.
Because the procedures described above do not constitute an examination of prospective financial statements in accordance with standards established by the American Institute of Certified Public Accountants, we do not express an opinion on whether the prospective financial statements are presented in conformity with AICPA presentation guidelines or on whether the underlying assumptions provide a reasonable basis for the presentation.

In connection with the procedures referred to above, no matters came to our attention that caused us to believe that rental income should be adjusted or that the forecast is mathematically inaccurate. Had we performed additional procedures or had we made an examination of the forecast in accordance with standards established by the American Institute of Certified Public Accountants, matters might have come to our attention that would have been reported to you. Furthermore, there will usually be differences between the forecasted and actual results, because events and circumstances frequently do not occur as expected, and those differences may be material. We have no responsibility to update this report for events and circumstances occurring after the date of this report.

Exhibit 2

ABC Trustee
XYZ Company
At your request, we performed the agreed-upon procedures enumerated below with respect to the forecasted balance sheet, statements of income, retained earnings and changes in financial position of XYZ Company as of December 31, 19XX, and for the year then ending. These procedures, which were specified by ABC Trustee and XYZ Company, were performed solely to assist you, and this report is solely for your information and should not be used by those who did not participate in determining the procedures.

a. We assisted the management of XYZ Company in assembling the prospective financial statements.

b. We read the prospective financial statements for compliance in regard to format with the presentation guidelines established by the American Institute of Certified Public Accountants for presentation of a forecast.

c. We tested the forecast for mathematical accuracy.

Because the procedures described above do not constitute an examination of prospective financial statements in accordance with standards established by the American Institute of Certified Public Accountants, we do not express an opinion on whether the prospective financial statements are presented in conformity with AICPA presentation guidelines or on whether the underlying assumptions provide a reasonable basis for the presentation.

In connection with the procedures referred to above, no matters came to
our attention that caused us to believe that the format of the forecast should be modified or that the forecast is mathematically inaccurate. Had we performed additional procedures or had we made an examination of the forecast in accordance with standards established by the American Institute of Certified Public Accountants, matters might have come to our attention that would have been reported to you. Furthermore, there will usually be differences between the forecasted and actual results, because events and circumstances frequently do not occur as expected, and those differences may be material. We have no responsibility to update this report for events and circumstances occurring after the date of this report.

Other Information

58. When an accountant’s compilation, review, or examination report on historical financial statements is included in an accountant-submitted document containing prospective financial statements, the accountant should either examine, compile, or apply agreed-upon procedures to the prospective financial statements and report accordingly, unless (a) the prospective financial statements are labeled as a “budget,” (b) the budget does not extend beyond the end of the current fiscal year, and (c) the budget is presented with interim historical financial statements for the current year. In such circumstances, the accountant need not examine, compile, or apply agreed-upon procedures to the budget; however, he should report on it and (a) indicate that he did not examine or compile the budget and (b) disclaim an opinion or any other form of assurance on the budget. In addition, the budgeted information may omit the summaries of significant assumptions and accounting policies required by the guidelines for presentation of prospective financial statements established by the American Institute of Certified Public Accountants, provided such omission is not, to the accountant’s knowledge, undertaken with the intention of misleading those who might reasonably be expected to use such budgeted information, and is disclosed in the accountant’s report. The following is the form of the standard paragraphs to be added to the accountant’s report in this circumstance when the summaries of significant assumptions and accounting policies have been omitted.

The accompanying budgeted balance sheet, statements of income, retained earnings, and changes in financial position of XYZ Company as of December 31, 19XX, and for the six months then ending, have not been compiled or examined by us, and, accordingly, we do not express an opinion or any other form of assurance on them.
Management has elected to omit the summaries of significant assumptions and accounting policies required under established guidelines for presentation of prospective financial statements. If the omitted summaries were included in the budgeted information, they might influence the user's conclusions about the company's budgeted information. Accordingly, this budgeted information is not designed for those who are not informed about such matters.

59. When the accountant's compilation, review, or examination report on historical financial statements is included in a client-prepared document containing prospective financial statements, the accountant should not consent to the use of his name in the document unless (a) he has examined, compiled, or applied agreed-upon procedures to the prospective financial statements and his report accompanies them, (b) the prospective financial statements are accompanied by an indication by the responsible party or the accountant that the accountant has not performed such a service on the prospective financial statements and that the accountant assumes no responsibility for them, or (c) another accountant has examined, compiled, or applied agreed-upon procedures to the prospective financial statements and his report is included in the document. In addition, if the accountant has examined the historical financial statements and they accompany prospective financial statements that he did not examine, compile, or apply agreed-upon procedures to in certain\(^\text{27}\) client-prepared documents, he should refer to SAS No. 8, *Other Information in Documents Containing Audited Financial Statements*.

60. The accountant whose report on prospective financial statements is included in a client-prepared document containing historical financial statements should not consent to the use of his name in the document unless (a) he has compiled, reviewed, or examined the historical financial statements and his report accompanies them, (b) the

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\(^{27}\) SAS No. 8 applies only to such prospective financial statements contained in (a) annual reports to holders of securities or beneficial interests, annual reports of organizations for charitable or philanthropic purposes distributed to the public, and annual reports filed with regulatory authorities under the Securities Exchange Act of 1934 or (b) other documents to which the auditor, at the client's request, devotes attention. SAS No. 8 does not apply when the historical financial statements and report appear in a registration statement filed under the Securities Act of 1933 (in which case, see SAS No. 37, *Filings Under Federal Securities Statutes*).
historical financial statements are accompanied by an indication by the responsible party or the accountant that the accountant has not performed such a service on the historical financial statements and that the accountant assumes no responsibility for them, or (c) another accountant has compiled, reviewed, or examined the historical financial statements and his report is included in the document.

61. An entity may publish various documents that contain information other than historical financial statements in addition to the compiled or examined prospective financial statements and the accountant's report thereon. The accountant's responsibility with respect to information in such a document does not extend beyond the financial information identified in the report, and he has no obligation to perform any procedures to corroborate other information contained in the document. However, the accountant should read the other information and consider whether such information, or the manner of its presentation, is materially inconsistent with the information, or manner of its presentation, appearing in the prospective financial statements.

62. If the accountant examines prospective financial statements included in a document containing inconsistent information, he might not be able to conclude that there is adequate support for each significant assumption. The accountant should consider whether the prospective financial statements, his report, or both require revision. Depending on the conclusion he reaches, the accountant should consider other actions that may be appropriate, such as issuing an adverse opinion, disclaiming an opinion because of a scope limitation, withholding the use of his report in the document, or withdrawing from the engagement.

63. If the accountant compiles the prospective financial statements included in the document containing inconsistent information, he should attempt to obtain additional or revised information. If he does not receive such information, the accountant should withhold the use of his report or withdraw from the compilation engagement.

64. If, while reading the other information appearing in the document containing the examined or compiled prospective financial statements, as described in the preceding paragraphs, the accountant becomes aware of information that he believes is a material misstatement of fact that is not an inconsistent statement, he should discuss the
matter with the responsible party. In connection with this discussion, the accountant should consider that he may not have the expertise to assess the validity of the statement made, that there may be no standards by which to assess its presentation, and that there may be valid differences of judgment or opinion. If the accountant concludes that he has a valid basis for concern, he should propose that the responsible party consult with some other party whose advice might be useful, such as the entity’s legal counsel.

65. If, after discussing the matter as described in paragraph 64, the accountant concludes that a material misstatement of fact remains, the action he takes will depend on his judgment in the particular circumstances. He should consider steps such as notifying the responsible party in writing of his views concerning the information and consulting his legal counsel about further appropriate action in the circumstances.

**Effective Date**

66. This Statement is effective for engagements in which the date of completion of the accountant’s services on prospective financial statements is September 30, 1986, or later. Earlier application is encouraged.
Appendix A

Minimum Presentation Guidelines

1. Prospective information presented in the format of historical financial statements facilitates comparisons with financial position, results of operations, and changes in financial position of prior periods, as well as those actually achieved for the prospective period. Accordingly, prospective financial statements preferably should be in the format of the historical financial statements that would be issued for the period(s) covered unless there is an agreement between the responsible party and potential users specifying another format. Prospective financial statements may take the form of complete basic financial statements or may be limited to the following minimum items (where such items would be presented for historical financial statements for the period).²

   a. Sales or gross revenues
   b. Gross profit or cost of sales
   c. Unusual or infrequently occurring items
   d. Provision for income taxes
   e. Discontinued operations or extraordinary items
   f. Income from continuing operations
   g. Net income
   h. Primary and fully diluted earnings per share
   i. Significant changes in financial position³
   j. A description of what management intends the prospective financial statements to present, a statement that the assumptions are based on

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Note: This appendix describes the minimum items that constitute a presentation of a financial forecast or a financial projection, as specified in the AICPA Guide for Prospective Financial Statements. Complete presentation guidelines for entities that choose to issue prospective financial statements, together with illustrative presentations, are included in the guide.

¹The details of each statement may be summarized or condensed so that only the major items in each are presented. The usual footnotes associated with historical financial statements need not be included as such. However, significant assumptions and accounting policies should be disclosed.

²Similar types of financial information should be presented for entities for which these terms do not describe operations. Further, similar items should be presented if a comprehensive basis of accounting other than generally accepted accounting principles is used to present the prospective financial statements. For example, if the cash basis were used, item a would be cash receipts.

³This item does not require a balance sheet or a statement of changes in financial position. Examples are included in the AICPA Guide for Prospective Financial Statements.
information about circumstances and conditions existing at the time the prospective information was prepared, and a caveat that the prospective results may not be achieved

k. Summary of significant assumptions

l. Summary of significant accounting policies

2. A presentation that omits one or more of the applicable minimum items a through i above is a partial presentation, which would not ordinarily be appropriate for general use. If an omitted applicable minimum item is derivable from the information presented, the presentation would not be deemed to be a partial presentation. A presentation that contains the applicable minimum items a through i above, but omits minimum items j through l above is not a partial presentation, and an engagement involving such a presentation is subject to the provisions of this Statement.

\footnote{The accountant who provides services with respect to a partial presentation should consider the reporting guidance in the AICPA Code of Professional Ethics, rule 201(e) and interpretation 201-2.}
Appendix B

Training and Proficiency, Planning and Procedures Applicable to Compilations

Training and Proficiency

1. The accountant should be familiar with the guidelines for the preparation and presentation of prospective financial statements. The guidelines are contained in the AICPA Guide for Prospective Financial Statements.

2. The accountant should possess or obtain a level of knowledge of the industry and the accounting principles and practices of the industry in which the entity operates, or will operate, that will enable him to compile prospective financial statements that are in appropriate form for an entity operating in that industry.

Planning the Compilation Engagement

3. To compile the prospective financial statements of an existing entity, the accountant should obtain a general knowledge of the nature of the entity’s business transactions and the key factors upon which its future financial results appear to depend. He should also obtain an understanding of the accounting principles and practices of the entity to determine if they are comparable to those used within the industry in which the entity operates.

4. To compile the prospective financial statements of a proposed entity, the accountant should obtain knowledge of the proposed operations and the key factors upon which its future results appear to depend and that have affected the performance of entities in the same industry.

Compilation Procedures

5. In performing a compilation of prospective financial statements the accountant should, where applicable —

a. Establish an understanding with the client, preferably in writing, regarding the services to be performed.

b. Inquire about the accounting principles used in the preparation of the prospective financial statements.

• For existing entities, compare the accounting principles used to those used in the preparation of previous historical financial statements and inquire whether such principles are the same as those expected to be
used in the historical financial statements covering the prospective period.

- For entities to be formed or entities formed that have not commenced operations, compare specialized industry accounting principles used, if any, to those typically used in the industry. Inquire about whether the accounting principles used for the prospective financial statements are those that are expected to be used when, or if, the entity commences operations.

c. Ask how the responsible party identifies the key factors and develops its assumptions.

d. List, or obtain a list of, the responsible party's significant assumptions providing the basis for the prospective financial statements and consider whether there are any obvious omissions in light of the key factors upon which the prospective results of the entity appear to depend.

e. Consider whether there appear to be any obvious internal inconsistencies in the assumptions.

f. Perform, or test the mathematical accuracy of, the computations that translate the assumptions into prospective financial statements.

g. Read the prospective financial statements, including the summary of significant assumptions, and consider whether —

- The statements, including the disclosures of assumptions and accounting policies, appear to be not presented in conformity with the AICPA presentation guidelines for prospective financial statements.¹

- The statements, including the summary of significant assumptions, appear to be not obviously inappropriate in relation to the accountant's knowledge of the entity and its industry and, for a —

  Financial forecast, the expected conditions and course of action in the prospective period.

  Financial projection, the purpose of the presentation.

h. If a significant part of the prospective period has expired, inquire about the results of operations or significant portions of the operations (such as sales volume), and significant changes in financial position, and consider their effect in relation to the prospective financial statements. If historical financial statements have been prepared for the expired portion of the period, the accountant should read such statements and consider those results in relation to the prospective financial statements.

i. Confirm his understanding of the statements (including assumptions) by obtaining written representations from the responsible party. Because the amounts reflected in the statements are not supported by historical

¹Presentation guidelines for entities that issue prospective financial statements are set forth and illustrated in the AICPA Guide for Prospective Financial Statements.
books and records but rather by assumptions, the accountant should obtain representations in which the responsible party indicates its responsibility for the assumptions. The representations should be signed by the responsible party at the highest level of authority who the accountant believes is responsible for and knowledgeable, directly or through others, about matters covered by the representations.

- **For a financial forecast**, the representations should include a statement that the financial forecast presents, to the best of the responsible party’s knowledge and belief, the expected financial position, results of operations, and changes in financial position for the forecast period and that the forecast reflects the responsible party’s judgment, based on present circumstances, of the expected conditions and its expected course of action. If the forecast contains a range, the representation should also include a statement that, to the best of the responsible party’s knowledge and belief, the item or items subject to the assumption are expected to actually fall within the range and that the range was not selected in a biased or misleading manner.

- **For a financial projection**, the representations should include a statement that the financial projection presents, to the best of the responsible party’s knowledge and belief, the expected financial position, results of operations, and changes in financial position for the projection period given the hypothetical assumptions, and that the projection reflects its judgment, based on present circumstances, of expected conditions and its expected course of action given the occurrence of the hypothetical events. The representations should also (i) identify the hypothetical assumptions and describe the limitations on the usefulness of the presentation, (ii) state that the assumptions are appropriate, (iii) indicate if the hypothetical assumptions are improbable, and (iv) if the projection contains a range, include a statement that, to the best of the responsible party’s knowledge and belief, given the hypothetical assumptions, the item or items subject to the assumption are expected to actually fall within the range and that the range was not selected in a biased or misleading manner.

j. Consider, after applying the above procedures, whether he has received representations or other information that appears to be obviously inappropriate, incomplete, or otherwise misleading and, if so, attempt to obtain additional or revised information. If he does not receive such information, the accountant should ordinarily withdraw from the compilation engagement.² (Note that the omission of disclosures, other than those relating to significant assumptions, would not require the accountant to withdraw; see paragraph 24 of this Statement.)

²The accountant need not withdraw from the engagement if the effect of such information on the prospective financial statements does not appear to be material.
Appendix C

Training and Proficiency, Planning and Procedures Applicable to Examinations

Training and Proficiency

1. The accountant should be familiar with the guidelines for the preparation and presentation of prospective financial statements. The guidelines are contained in the AICPA Guide for Prospective Financial Statements.

2. The accountant should possess or obtain a level of knowledge of the industry and the accounting principles and practices of the industry in which the entity operates, or will operate, that will enable him to examine prospective financial statements that are in appropriate form for an entity operating in that industry.

Planning an Examination Engagement

3. Planning the examination engagement involves developing an overall strategy for the expected scope and conduct of the engagement. To develop such a strategy, the accountant needs to have sufficient knowledge to enable him to adequately understand the events, transactions, and practices that, in his judgment, may have a significant effect on the prospective financial statements.

4. Factors to be considered by the accountant in planning the examination include (a) the accounting principles to be used and the type of presentation, (b) the anticipated level of attestation risk\(^1\) related to the prospective financial statements, (c) preliminary judgments about materiality levels, (d) items within the prospective financial statements that are likely to require revision or adjustment, (e) conditions that may require extension or modification of the accountant's examination procedures, (f) knowledge of the entity's business

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\(^1\)Attestation risk is the risk that the accountant may unknowingly fail to appropriately modify his examination report on prospective financial statements that are materially misstated, that is, that are not presented in conformity with AICPA presentation guidelines or have assumptions that do not provide a reasonable basis for management's forecast, or management's projection given the hypothetical assumptions. It consists of (a) the risk (consisting of inherent risk and control risk) that the prospective financial statements contain errors that could be material and (b) the risk (detection risk) that the accountant will not detect such errors.
and its industry, (g) the responsible party's experience in preparing prospective financial statements, (h) the length of the period covered by the prospective financial statements, and (i) the process by which the responsible party develops its prospective financial statements.

5. The accountant should obtain knowledge of the entity's business, accounting principles, and the key factors upon which its future financial results appear to depend. The accountant should focus on such areas as —
   a. The availability and cost of resources needed to operate. Principal items usually include raw materials, labor, short-term and long-term financing, and plant and equipment.
   b. The nature and condition of markets in which the entity sells its goods or services, including final consumer markets if the entity sells to intermediate markets.
   c. Factors specific to the industry, including competitive conditions, sensitivity to economic conditions, accounting policies, specific regulatory requirements, and technology.
   d. Patterns of past performance for the entity or comparable entities, including trends in revenue and costs, turnover of assets, uses and capacities of physical facilities, and management policies.

Examination Procedures

6. The accountant and the responsible party should reach an understanding regarding the services to be provided. Ordinarily, this understanding is confirmed in an engagement letter.

7. The accountant's objective in an examination of prospective financial statements is to accumulate sufficient evidence to limit attestation risk to a level that is, in his professional judgment, appropriate for the level of assurance that may be imparted by his examination report. In a report on an examination of prospective financial statements, he provides assurance only about whether the prospective financial statements are presented in conformity with AICPA presentation guidelines and whether the assumptions provide a reasonable basis for management's forecast, or a reasonable basis for management's projection given the hypothetical assumptions. He does not provide assurance about the achievability of the prospective results because events and circumstances frequently do not occur as expected and achievement of the prospective results is dependent on the actions, plans, and assumptions of the responsible party.

8. In his examination of prospective financial statements, the accountant should select from all available procedures—that is, procedures that assess inherent and control risk and restrict detection risk—any combination that
can limit attestation risk to such an appropriate level. The extent to which examination procedures will be performed should be based on the accountant’s consideration of (a) the nature and materiality of the information to the prospective financial statements taken as a whole; (b) the likelihood of misstatements; (c) knowledge obtained during current and previous engagements; (d) the responsible party’s competence with respect to prospective financial statements; (e) the extent to which the prospective financial statements are affected by the responsible party’s judgment, for example, its judgment in selecting the assumptions used to prepare the prospective financial statements; and (f) the adequacy of the responsible party’s underlying data.

9. The accountant should perform those procedures he considers necessary in the circumstances to report on whether the assumptions provide a reasonable basis for the —

   a. Financial forecast. The accountant can form an opinion that the assumptions provide a reasonable basis for the forecast if the responsible party represents that the presentation reflects, to the best of its knowledge and belief, its estimate of expected financial position, results of operations, and changes in financial position for the prospective period and the accountant concludes, based on his examination, (i) that the responsible party has explicitly identified all factors expected to materially affect the operations of the entity during the prospective period and has developed appropriate assumptions with respect to such factors and (ii) that the assumptions are suitably supported.

   b. Financial projection given the hypothetical assumptions. The accountant can form an opinion that the assumptions provide a reasonable basis for the financial projection given the hypothetical assumptions if the responsible party represents that the presentation reflects, to the best of its knowledge and belief, expected financial position, results of operations, and changes in financial position for the prospective period given the hypothetical assumptions and the accountant concludes, based on his examination, (i) that the responsible party has explicitly identified all factors expected to materially affect the operations of the entity during the prospective period and has developed appropriate assumptions with respect to such factors and (ii) that the assumptions are suitably supported.

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If the forecast contains a range, the representation should also include a statement that, to the best of the responsible party’s knowledge and belief, the item or items subject to the assumption are expected to actually fall within the range and that the range was not selected in a biased or misleading manner.

An attempt to list all assumptions is inherently not feasible. Frequently, basic assumptions that have enormous potential impact are considered to be implicit, such as conditions of peace and absence of natural disasters.

If the projection contains a range, the representation should also include a statement that, to the best of the responsible party’s knowledge and belief, given the hypothetical assumptions, the item or items subject to the assumption are expected to actually fall within the range and that the range was not selected in a biased or misleading manner.
tors that would materially affect the operations of the entity during the prospective period if the hypothetical assumptions were to materialize and has developed appropriate assumptions with respect to such factors and (ii) that the other assumptions are suitably supported given the hypothetical assumptions. However, as the number and significance of the hypothetical assumptions increase, the accountant may not be able to satisfy himself about the presentation as a whole by obtaining support for the remaining assumptions.

10. The accountant should evaluate the support for the assumptions.
   a. Financial forecast—The accountant can conclude that assumptions are suitably supported if the preponderance of information supports each significant assumption.
   b. Financial projection—In evaluating support for assumptions other than hypothetical assumptions, the accountant can conclude that they are suitably supported if the preponderance of information supports each significant assumption given the hypothetical assumptions. The accountant need not obtain support for the hypothetical assumptions, although he should consider whether they are consistent with the purpose of the presentation.

11. In evaluating the support for assumptions, the accountant should consider—
   a. Whether sufficient pertinent sources of information about the assumptions have been considered. Examples of external sources the accountant might consider are government publications, industry publications, economic forecasts, existing or proposed legislation, and reports of changing technology. Examples of internal sources are budgets, labor agreements, patents, royalty agreements and records, sales backlog records, debt agreements, and actions of the board of directors involving entity plans.
   b. Whether the assumptions are consistent with the sources from which they are derived.
   c. Whether the assumptions are consistent with each other.
   d. Whether the historical financial information and other data used in developing the assumptions are sufficiently reliable for that purpose. Reliability can be assessed by inquiry and analytical or other procedures, some of which may have been completed in past examinations or reviews of the historical financial statements. If historical financial statements have been prepared for an expired part of the prospective period, the accountant should consider the historical data in relation to the prospective results for the same period, where applicable. If the prospective financial statements incorporate such historical financial results and that period is
significant to the presentation, the accountant should make a review of the historical information in conformity with the applicable standards for a review.\(^5\)

e. Whether the historical financial information and other data used in developing the assumptions are comparable over the periods specified or whether the effects of any lack of comparability were considered in developing the assumptions.

f. Whether the logical arguments or theory, considered with the data supporting the assumptions, are reasonable.

12. In evaluating the preparation and presentation of the prospective financial statements, the accountant should perform procedures that will provide reasonable assurance that the —

a. Presentation reflects the identified assumptions.

b. Computations made to translate the assumptions into prospective amounts are mathematically accurate.

c. Assumptions are internally consistent.

d. Accounting principles used in the —

*Financial forecast* are consistent with the accounting principles expected to be used in the historical financial statements covering the prospective period and those used in the most recent historical financial statements, if any.

*Financial projection* are consistent with the accounting principles expected to be used in the prospective period and those used in the most recent historical financial statements, if any, or that they are consistent with the purpose of the presentation.\(^6\)

e. Presentation of the prospective financial statements follows the AICPA guidelines applicable for such statements\(^7\).

f. Assumptions have been adequately disclosed based on AICPA presentation guidelines for prospective financial statements.

\(^5\)If the entity is a public company, the accountant should perform the procedures in SAS No. 36, *Review of Interim Financial Information*, paragraphs 6 through 15. If the entity is nonpublic, the accountant should perform the procedures in SSARS No. 1, *Compilation and Review of Financial Statements*, paragraphs 24 through 31.

\(^6\)The accounting principles used in a financial projection need not be those expected to be used in the historical financial statements for the prospective period if use of different principles is consistent with the purpose of the presentation.

\(^7\)Presentation guidelines for entities that issue prospective financial statements are set forth and illustrated in the AICPA *Guide for Prospective Financial Statements*. 
13. The accountant should consider whether the prospective financial statements, including related disclosures, should be revised because of (a) mathematical errors, (b) unreasonable or internally inconsistent assumptions, (c) inappropriate or incomplete presentation, or (d) inadequate disclosure.

14. The accountant should obtain written representations from the responsible party acknowledging its responsibility for both the presentation and the underlying assumptions. The representations should be signed by the responsible party at the highest level of authority who the accountant believes is responsible for and knowledgeable, directly or through others in the organization, about the matters covered by the representations. Appendix B, paragraph 5i describes the specific representations to be obtained for a financial forecast and a financial projection.
QUALIFICATIONS

The Statement, entitled Financial Forecasts and Projections, was adopted by the assenting votes of the fifteen members of the board, of whom three, Messrs. Bixby, Glenn, and Harris, assented with qualification.

Mr. Glenn qualifies his assent because he believes that issuance of a statement is premature. He believes that it would be appropriate to issue the guidance in the form of a guide for a trial period before a statement is issued.

Mr. Harris qualifies his assent because he believes that the applicability of the statement should not be based on anticipation of the future use of prospective financial statements that the accountant has assembled or assisted in assembling. In Mr. Harris’s view, an accountant can provide a useful, cost-effective service assisting clients in preparing prospective financial statements without performing one of the engagements prescribed by the statement when those statements “reasonably might be expected to be used by another (third) party.”

Mr. Bixby qualifies his assent because he objects to the proscription in paragraph 9 of the accountant’s consent to the use of his name in conjunction with a financial projection that he believes will be distributed to those who will not be negotiating directly with the responsible party. Mr. Bixby believes this is unnecessarily restrictive. In his opinion, there may be circumstances in which a financial projection would be useful to a third party who has not had the opportunity to negotiate directly with the responsible party. Mr. Bixby believes that if the effects of the hypothetical assumption are adequately explained, the reader can draw his own conclusions from the presentation without participating in negotiations.
Note: This Statement is issued by the Auditing Standards Board under the authority granted it by Council of the Institute to interpret rule 201, General Standards, of the Institute's Code of Professional Ethics. Members should be prepared to justify departures from this Statement.