The AICPA Moves to Converge and Clarify All of Its Auditing Standards

By CCH Staff

By now, most accountants have a working knowledge of the FASB Accounting Standards Codification™ (Codification). Although the Codification was not intended to change generally accepted accounting principles (GAAP) in the United States, it did affect the way accountants research and reference U.S. GAAP. Because GAAP did not change, many CPAs believed that significant planning for the Codification was unnecessary. We believe that most practicing CPAs were surprised at the complexity of the Codification released in July 2009 and have struggled with understanding and using it.

In all probability, few public accountants, specifically auditors, know a great deal about the Auditing Standards Board’s (ASB’s) Clarity Project or its practical effect on their audit practices. Like the Codification, the goal of the Clarity Project is not necessarily to change authoritative standards, rather to make them easier to read, understand, and apply. We hope the recent and ongoing experience of transitioning to the Codification will help CPAs prepare for the adjustment to their practices that the Clarity Project will require.

Background of the Clarity Project

In 2004, the ASB undertook its two-pronged Clarity Project. First, the Clarity Project is intended to make existing U.S. auditing standards easier to understand and apply. Second, the Clarity Project is designed to converge U.S. generally accepted auditing standards (GAAS) with International Standards on Auditing (ISAs) issued by the International Auditing and Assurance Standards Board (IAASB). The Clarity Project mirrors, to a large degree, an IAASB project that was completed in March 2009. In its convergence efforts, the ASB is using ISAs as the base for its clarified standards.

As with the Financial Accounting Standards Board (FASB) project that resulted in the Codification, the Clarity Project will result in a complete body of authoritative guidance for auditors of nonpublic companies. All AU sections of currently effective Statements on Auditing Standards (SASs) in AICPA Professional Standards are being evaluated and reissued in the clarified format (see the “Reorganization of Standards” section below).

Convergence

In accomplishing convergence with international standards, the ASB is also attempting to avoid conflict with Public Company Accounting Oversight Board (PCAOB) standards to the extent possible. However, the ASB has publicly recognized that some conflict between its newly clarified standards and those of both the IAASB and the PCAOB is unavoidable because of legal, regulatory, and other considerations.

For example, ISA 240 (Redrafted), The Auditor’s Responsibilities Relating to Fraud in an Audit of Financial Statements, defines fraud as “. . . an intentional act by one or more individuals among management, those charged with governance, employees, or third parties, involving the use of deception to obtain an unjust or illegal advantage [emphasis added].” The proposed redrafted SAS, however, retains the concept of fraud in SAS No. 99, Consideration of Fraud in a Financial Statement Audit, as an act “. . . that results in a material misstatement in financial statements that are the subject of an audit [emphasis added].”

The ASB believes that absolute convergence with international standards in this case “. . . could inappropriately expose auditors to additional liability in the [United States], . . . .” The ASB states in the exposure draft of the proposed SAS that the divergence between the definitions of fraud in the two standards will not create significant differences between the application of ISA 240 (Redrafted) and that of the redrafted SAS.

Reorganization of standards

The ASB will issue many of the clarified standards in a single SAS that will be codified in AU section format. This process is
the same as the one used when SAS No. 1, *Codification of Auditing Standards and Procedures*, was issued in 1972. SAS No. 1 contained all of the then-existing standards codified in AU section format within the SAS. As a result of the Clarity Project, existing AU sections will be modified and guidance may be combined and moved into new sections. Once completed, the single clarified SAS will be issued using the next available number, such as “SAS No. 12X.”

In some cases, individual AU sections are being clarified “one for one” into individual clarified standards. In other cases, some AU sections are grouped together and clarified into one or more standards. As a result, topics currently associated with certain AU section numbers might be re-titled and assigned different AU section numbers in “SAS No. 12X.” The AICPA staff has published “Ex tant AU Sections Mapped to Clarity SASs,” which compares existing AU sections to their related ISAs.

In addition, as the clarified standards are issued, the AICPA staff publishes supplementary materials. These materials include a comparison of the new clarified standards to international standards, as well as information on the disposition of affected AU sections.

### Fundamentals of Clarity standards

As mentioned above, one of the primary objectives of the Clarity Project is to make auditing standards easier to understand. In addition, the project is designed to eliminate redundancies and clearly differentiate practical guidance from the requirements of the standards. To help accomplish these objectives, the ASB is employing certain conventions in drafting new and redrafting existing standards. These conventions call for the inclusion of the following sections:

- statement of objective;
- definitions, where relevant;
- requirements; and
- application and other explanatory material, with paragraphs using an “A” prefix.

The explanatory material in the “A” prefix paragraphs is cross-referenced to the corresponding paragraphs in the requirements section. The auditor is responsible for considering the entire text of each standard in applying its requirements.

The general, field work, and reporting standards—the 10 general standards—are being eliminated by the Clarity Project. However, the statement of an objective is fundamental to the clarified standards and, in a more principles-based approach, serves to link the individual standards to the conceptual framework that formed the basis for those 10 standards. The general, field work, and reporting standards will still serve, to some degree, to provide structure to the auditing standards codification.

In addition, the drafting conventions call for the use of certain formatting techniques, such as bulleted lists, to enhance readability. Finally, special considerations that are relevant to the audits of both smaller, less complex entities and governmental entities are included where appropriate.

### Changes to existing standards

CPA firms that have structured their audit methodologies following the guidance issued by the IAASB and the best practices of the ASB should be better prepared when the clarified standards take effect. However, these firms will need to revise their existing guidance or work programs when referring to authoritative literature (see the “Planning for Implementation” section below).

As with the FASB Codification, the Clarity Project is not expected to significantly change existing audit guidance. However, based on the clarified standards that have been exposed for public comment, finalized, or issued by the ASB, specific examples of revisions to existing authoritative guidance include:

- conceptual and practical use of the term “applicable financial reporting framework” rather than “generally accepted accounting principles”;
- changes to wording of auditor’s reports, including the use of paragraph headings and expansion of the description of management’s responsibilities;
- explicit requirements for auditors related to the detection of illegal acts; and
- additional requirements related to opening balances in initial audit engagements.

As noted earlier in the “Reorganization of Standards” section, some existing AU sections will be merged and others will be split into different sections.
Effective date
The effective date of the clarified standards is scheduled for audits of financial statements for periods ending on or after December 15, 2012; however, auditors are not precluded from considering the guidance in clarified standards as long as the auditor continues to comply with existing standards. The ASB maintains its belief that having a single effective date will ease the transition to, and the implementation of, its clarified standards.

The scheduled effective date for the clarified standards should allow CPA firms to close out their December 31, 2011, audits using the “old standards.” The firms could then begin preparing for their December 31, 2012, audits using the new standards.

Planning for implementation
The ASB has indicated that its release of the finalized standards as they are approved serves to allow auditors more time for updating of, and training in, firm methodologies. Although substantive revisions to authoritative guidance are not substantial, auditors will need to modify their work programs—including both general and specific procedures—for changes in specific guidance as well as changes in references to authoritative standards.

Even though the standards will not be effective until 2012 calendar-year audits, auditors should familiarize themselves with the redrafted standards as they are finalized. CPA firms should begin the process of reviewing audit programs and references to related AU sections. In addition, firms should consider providing their audit departments with ongoing training on the clarified standards.

Peer reviews and documentation
CPA firms generally have unique methodologies for performing confirmations, testing controls, and other audit procedures. Such methodologies should refer to the SASs issued by the ASB or the appropriate AU sections. To help avoid unwelcome findings in peer reviews once the Clarity Project changes are effective, firms should ensure that any references to the authoritative literature match those in the redrafted clarified standards.

In addition, firms should carefully review each standard once finalized to ensure they have considered any nuances in the new literature that may require changes to audit procedures and training in accordance with the firms’ quality-control documents. Firms may also need to consider restructuring or revising their standard engagement letters.

Conclusion
The ASB’s Clarity Project is moving rapidly toward its conclusion. Even though the effective date of most of the clarified standards has been postponed, CPAs should still monitor the new standards as they are finalized and prepare for any changes in their audit practices that the new standards will require.

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Understand the potential of team members, you will be surprised at the talent you find.

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