

Audit Communications: A Two Way Street

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Objectives

- Required elements of communication
 - Who?
 - What?
 - When?
- The new management letter

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SAS 114- Who are we talking to?

- *Those charged with governance* means the person(s) with responsibility for overseeing the strategic direction of the entity and obligations related to the accountability of the entity. This includes overseeing the financial reporting process.

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SAS 114- Who are we talking to?

- Those charged with governance can include:
 - Board of Directors
 - Audit Committee
 - Finance Committee
 - Management

SAS 114- Who are we talking to?

- *Management* means the person(s) responsible for achieving the objectives of the entity and who have the authority to establish policies and make decisions by which those objectives are to be pursued. Management is responsible for the financial statements, including designing, implementing, and maintaining effective internal control over financial reporting.

SAS 114- What are we talking about?

- Required communications by auditor:
 - The auditor's responsibilities under GAAS
 - Overview of the planned scope and timing of the audit
 - Significant findings from the audit

SAS 114- What are we talking about?

- Required communications by auditor:
 - Significant Findings:
 - Qualitative aspects of significant accounting practices (policies, estimates, disclosures)
 - Significant difficulties
 - Uncorrected misstatements
 - Disagreements with management
 - Other findings or issues

SAS 114- What are we talking about?

- Required communications by auditor:
 - Significant Findings:
 - Material, corrected misstatements
 - Management's written representation
 - Management's consultations with other accountants
 - Significant issues/matters

SAS 114- When are we talking?

Communication Process

- Should be a two way process
- Forms of communication:
 - Meeting or conversation
 - Presentation
 - Written report

SAS 114- When are we talking?

Communication Process

- Timing
 - Planning stages
 - During audit committee and/or board meetings
 - Anytime!
- Two meetings/discussions

Communications in Other Standards

- SAS No. 54, *Illegal Acts by Clients*- responsibility to communicate illegal acts that come to the auditor's attention
- SAS No. 74, *Compliance Auditing Considerations in Audits of Governmental Entities and Recipients of Governmental Financial Assistance*- the entity is subject to an audit requirement that may not be encompassed in the terms of the engagement, and that an audit in accordance with generally accepted auditing standards may not satisfy the relevant legal, regulatory, or contractual requirements

Communications in Other Standards

- SAS No. 99, *Consideration of Fraud in a Financial Statement Audit*
 - Inquiry of audit committee
 - Fraud involving senior management
 - Fraud resulting in a material misstatement
- SAS No. 115, *Communicating Internal Control Related Matters Identified in an Audit*- communication of control deficiencies in writing to management

SAS 115

- Provides guidance on evaluating the severity of deficiencies in internal control identified in an audit of financial statements.
- Defines the terms *deficiency in internal control*, *significant deficiency*, and *material weakness*.
- Requires the auditor to communicate, in writing, to management and those charged with governance, significant deficiencies and material weaknesses identified in an audit.

SAS 115- Definitions

- A *deficiency* in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis.

Design Deficiency

- A control necessary to meet the control objective is missing; or
- An existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met.

Operation Deficiency

- A properly designed control does not operate as designed; or
- The person performing the control does not possess the necessary authority or competence to perform the control effectively.

SAS 115- Definitions

- A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

SAS 115- Definitions

- A *material weakness* is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

Communication Under SAS 115

- Auditor's role related to internal control
- Definitions of control deficiency, significant deficiency, and material weakness
- Description of deficiencies and management's response
- Limitation of use paragraph

Correction of Deficiencies

- Your auditor is your friend
- Similar organizations
- Professional development and training

Resource Materials

- AICPA Audit Committee Effectiveness Center
- <http://www.aicpa.org/ForThePublic/AuditCommitteeEffectiveness>
- AICPA Audit Committee Toolkit- Not-For-Profit Entities

Resource Materials

- SAS No. 114, *The Auditor's Communication With Those Charged With Governance*
- SAS No. 115, *Communicating Internal Control Related Matters Identified in an Audit*



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