

Independence Disclosures in Compilation Reports

AICPA independence rules, including *Performance of nonattest services* (ET§101.05 of the AICPA Code of Professional Conduct), apply to compilation engagements unless a CPA firm discloses that it is not independent of the client. A compilation report should include such disclosure when the member or his or her firm lacks independence in fact or appearance, without stating the reason for the impairment (Statements on Standards for Accounting and Review Services (SSARS) No. 1, *Compilation and Review of Financial Statements* (AICPA, Professional Standards, vol. 2, AR §100.22). Some firms, in an attempt to be conservative, have adopted a practice of disclosing a lack of independence in all compilation reports. Since compilation services are commonly used by smaller, closely held businesses that may request bookkeeping or other assistance from their CPA firm, the practice allows firms to assist the client outside the constraints of the AICPA nonattest services rule. However, practitioners should also consider the following:

- The client may subsequently need an attest service, such as a review or audit of their financial statements, which would require compliance with interpretation 101-3 (and certain other independence standards) during the period covered by the financial statements. Various independence rules, including those related to nonattest services, employment, commissions and contingent fees, often apply *before* the professional engagement period begins (that is, before the CPA firm signs the attest services engagement letter or starts to perform attest services). Therefore, failure to meet any of these rules would preclude performance of the attest service for the period(s) to which the impairment relates.

- The disclosure that a firm lacks independence may impact the views of users of the compilation report. Though the number of respondents was relatively small, a 2005 survey by the AICPA

Accounting and Review Services Committee (ARSC) found that users of compilation reports (largely bankers) overwhelmingly indicated that they would like additional information about why a CPA firm's independence was impaired (see **AUDIT CONDUCT NEWS**, Fall 2006 (vol. 1, Article 4)). To help them better understand the needs of compilation report users, the ARSC plans to meet with representatives of the American Banking Association in the third quarter of 2007. Anecdotally, some have observed that some bankers and other users of compilation reports may be less concerned about additional services the accountant performed for their attest client than an accountant's direct financial interest in that client.

- A handful of state accountancy boards (e.g., Texas, Pennsylvania and Louisiana) have defined compilation engagements as attest services along with audits, reviews



and examination engagements. This is different from the AICPA standards and those of most other accountancy boards, which do not consider compilations to constitute the attest function. In Texas, for example, CPAs are required to follow (among other rules and regulations) the AICPA standards, including the SSARS and rule 101 (independence) of the Code. Thus, practitioners should ensure that they understand the impact of their state board regulations on their ability to provide certain nonattest services to clients who need compiled financial statements.

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