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Appendix 3 – Conforming Amendments to PCAOB Auditing Standards

June 12, 2007

AUDITING AND RELATED PROFESSIONAL PRACTICE STANDARDS

Conforming Amendments to PCAOB Auditing Standards

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Appendix 3

Conforming Amendments to PCAOB Auditing Standards

AU sec. 230, "Due Professional Care in the Performance of Work"

Statement on Auditing Standards ("SAS") No. 1, "Codification of Auditing Standards and Procedures," section 230, "Due Professional Care in the Performance of Work" (AU sec. 230, "Due Professional Care in the Performance of Work"), as amended, is amended as follows –

- a. Paragraph .10 is replaced with –

The exercise of due professional care allows the auditor to obtain *reasonable assurance* about whether the financial statements are free of material misstatement, whether caused by error or fraud, or whether any material weaknesses exist as of the date of management's assessment. Absolute assurance is not attainable because of the nature of audit evidence and the characteristics of fraud. Although not absolute assurance, reasonable assurance is a high level of assurance. Therefore, an audit conducted in accordance with the standards of the Public Company Accounting Oversight Board (United States) may not detect a material weakness in internal control over financial reporting or a material misstatement to the financial statements.

- b. The term "financial statements" within the first sentence of paragraph .13 is replaced with the term "financial statements or internal control over financial reporting."

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- c. The second sentence of paragraph .13 is replaced with –

Therefore, the subsequent discovery that either a material misstatement, whether from error or fraud, exists in the financial statements or a material weakness in internal control over financial reporting exists does not, in and of itself, evidence (a) failure to obtain reasonable assurance, (b) inadequate planning, performance, or judgment, (c) the absence of due professional care, or (d) a failure to comply with the standards of the Public Company Accounting Oversight Board (United States).

AU sec. 310, "Appointment of the Independent Auditor"

SAS No. 1, "Codification of Auditing Standards and Procedures," section 310, "Appointment of the Independent Auditor" (AU sec. 310, "Appointment of the Independent Auditor"), as amended, is amended as follows –

- a. The third bullet point of paragraph .06 is replaced with –

Management is responsible for establishing and maintaining effective internal control over financial reporting. If, in an integrated audit of financial statements and internal control over financial reporting, the auditor concludes that he or she cannot express an opinion on internal control over financial reporting because there has been a limitation on the scope of the audit, he or she should communicate, in writing, to management and the audit committee that the audit of internal control over financial reporting cannot be satisfactorily completed.

- b. The eighth bullet point of paragraph .06 is amended as follows –

Under Integrated audit of financial statements and internal control over financial reporting, the last sub-bullet point is replaced with the following –

To the board of directors – any conclusion that the audit committee's oversight of the company's external financial reporting and internal control over financial reporting is ineffective.

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Under Audit of financial statements, the last sub-bullet is replaced with the following –

To the board of directors – if the auditor becomes aware that the oversight of the company's external financial reporting and internal control over financial reporting by the audit committee is ineffective, that conclusion.

AU sec. 311, "Planning and Supervision"

SAS No. 22, "Planning and Supervision" (AU sec. 311, "Planning and Supervision"), as amended, is amended as follows –

Within the note to paragraph 1, the reference to paragraph 39 of PCAOB Auditing Standard No. 2 is replaced with a reference to paragraph 9 of PCAOB Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*.

AU sec. 312, "Audit Risk and Materiality in Conducting an Audit"

SAS No. 47, "Audit Risk and Materiality in Conducting an Audit" (AU sec. 312, "Audit Risk and Materiality in Conducting an Audit"), as amended, is amended as follows –

- a. Within the note to paragraph 3, the reference to paragraphs 22-23 of PCAOB Auditing Standard No. 2 is replaced with a reference to paragraph 20 of PCAOB Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*.
- b. Within the note to paragraph 7, the reference to paragraphs 24-26 of PCAOB Auditing Standard No. 2 is replaced with a reference to paragraphs 14-15 of PCAOB Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*.

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- c. The note to paragraph 12 is replaced with –

Note: When performing an integrated audit of financial statements and internal control over financial reporting, refer to paragraphs 9 and 20 of PCAOB Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*, regarding planning considerations and materiality, respectively.

- d. Within the note to paragraph 18, the reference to Appendix B, *Additional Performance Requirements and Directions; Extent-of-Testing Examples* of PCAOB Auditing Standard No. 2 is replaced with a reference to paragraphs B10-B16 of Appendix B, *Special Topics*, of PCAOB Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*.
- e. Within the note to paragraph 30, the reference to paragraphs 147-149 of PCAOB Auditing Standard No. 2 is replaced with a reference to paragraphs 6-8 and paragraphs B1-B5 of Appendix B, *Special Topics*, of PCAOB Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*.

AU sec. 313, "Substantive Tests Prior to the Balance-Sheet Date"

SAS No. 45, "Omnibus Statement on Auditing Standards – 1983" (AU sec. 313, "Substantive Tests Prior to the Balance-Sheet Date"), is amended as follows –

Within the note to paragraph 1, the reference to paragraphs 98-103 of PCAOB Auditing Standard No. 2 is replaced with a reference to paragraphs 52-53 of PCAOB Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*.

AU sec. 315, "Communications Between Predecessor and Successor Auditors"

SAS No. 84, "Communications Between Predecessor and Successor Auditors" (AU sec. 315, "Communications Between Predecessor and Successor Auditors"), as amended, is amended as follows –

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The last sentence of paragraph 16 is replaced with –

Furthermore, the predecessor auditor is not a specialist as defined in AU sec. 336, *Using the Work of a Specialist*, nor does the predecessor auditor's work constitute the work of others as described in AU sec. 322, *The Auditor's Consideration of the Internal Audit Function in an Audit of Financial Statements*, or paragraphs 16-19 of PCAOB Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*.

AU sec. 316, "Consideration of Fraud in a Financial Statement Audit"

SAS No. 99, "Consideration of Fraud in a Financial Statement Audit" (AU sec. 316, "Consideration of Fraud in a Financial Statement Audit"), is amended as follows –

Within the note to paragraph 1, the reference to paragraphs 24-26 of PCAOB Auditing Standard No. 2 is replaced with a reference to paragraphs 14-15 of PCAOB Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*.

AU sec. 319, "Consideration of Internal Control in a Financial Statement Audit"

SAS No. 55, "Consideration of Internal Control in a Financial Statement Audit" (AU sec. 319, "Consideration of Internal Control in a Financial Statement Audit"), as amended, is amended as follows –

- a. The note to paragraph 2 is replaced with –

Note: Refer to paragraph A9 of Appendix A, *Definitions*, of PCAOB Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements* for the definition of a relevant assertion and paragraphs 28-33 of PCAOB Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements* for discussion of identifying relevant assertions.

- b. Within the note to paragraph 9, the reference to Appendix B, *Additional Performance Requirements and Directions; Extent of Testing Examples*, of PCAOB Auditing Standard No. 2 is replaced with a reference to

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paragraphs B10-B16 of Appendix B, *Special Topics*, of PCAOB Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*.

- c. The last sentence of paragraph 33 is deleted.
- d. The note to paragraph 65 is deleted.
- e. The note to paragraph 83 is deleted.
- f. Within the note to paragraph 97, the reference to paragraphs 104-105 of PCAOB Auditing Standard No. 2 is replaced with a reference to paragraph 54 of PCAOB Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*.
- g. The appendix at paragraph 110 is deleted.

AU sec. 322, "The Auditor's Consideration of the Internal Audit Function in an Audit of Financial Statements"

SAS No. 65, "The Auditor's Consideration of the Internal Audit Function in an Audit of Financial Statements" (AU sec. 322, "The Auditor's Consideration of the Internal Audit Function in an Audit of Financial Statements"), is amended as follows –

- a. Within the note to paragraph 1, the reference to paragraphs 108-126 of PCAOB Auditing Standard No. 2 is replaced with a reference to paragraphs 16-19 of PCAOB Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*.
- b. The note to paragraph 20 is deleted.
- c. Within the note to paragraph 22, the reference to paragraph 122 of PCAOB Auditing Standard No. 2 is replaced with a reference to paragraphs 18-19 of PCAOB Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*.

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AU sec. 324, "Service Organizations"

SAS No. 70, "Service Organizations" (AU sec. 324, "Service Organizations"), as amended, is amended as follows –

Within the note to paragraph 1, the reference to Appendix B, *Additional Performance Requirements and Directions; Extent-of-Testing Examples*, of PCAOB Auditing Standard No. 2 is replaced with a reference to paragraphs B17-B27 of Appendix B, *Special Topics*, of PCAOB Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*.

AU sec. 325, "Communications About Control Deficiencies in an Audit of Financial Statements"^{1/}

AU sec. 325, "Communications About Control Deficiencies in an Audit of Financial Statements" is amended as follows –

- a. The first bullet point before paragraph 1 is amended as follows –

The reference to paragraphs 207-214 of PCAOB Auditing Standard No. 2 is replaced with a reference to paragraphs 78-84 of PCAOB Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*.

^{1/} When the Board adopted Auditing Standard No. 2, it superseded SAS No. 60 in the context of an integrated audit of financial statements and internal control over financial reporting by paragraphs 207-214 of Auditing Standard No. 2. See PCAOB Release No. 2004-008, *Conforming Amendments to PCAOB Interim Standards Resulting From the Adoption of PCAOB Auditing Standard No. 2, "An Audit of Internal Control Over Financial Reporting Performed in Conjunction with An Audit of Financial Statements"* (Sept. 15, 2004). As a result of superseding Auditing Standard No. 2, paragraphs 78-84 of Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*, now supersede SAS No. 60 in the context of an integrated audit.

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- b. The first bullet point in paragraph 1 is replaced with –

A deficiency in design exists when (a) a control necessary to meet the control objective is missing or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met.

- c. Paragraph 2 is replaced with –

A significant deficiency is a deficiency, or a combination of deficiencies, in internal control over financial reporting, that is less severe than a material weakness yet important enough to merit attention by those responsible for oversight of the company's financial reporting.

- d. The notes to paragraph 2 are deleted.

- e. Paragraph 3 is replaced with –

A material weakness is a deficiency, or a combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the company's annual or interim financial statements will not be prevented or detected on a timely basis.

Note: There is a reasonable possibility of an event when the likelihood of the event is either "reasonably possible" or "probable," as those terms are used in paragraph 3 of Financial Accounting Standards Board Statement No. 5, *Accounting for Contingencies*.

Note: In evaluating whether a deficiency exists and whether deficiencies, either individually or in combination with other deficiencies, are material weaknesses, the auditor should follow the direction in paragraphs 62-70 of PCAOB Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*.

- f. Paragraph 5 is replaced with –

If oversight of the company's external financial reporting and internal control over financial reporting by the company's audit committee is

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ineffective, that circumstance should be regarded as an indicator that a material weakness in internal control over financial reporting exists. Although there is not an explicit requirement to evaluate the effectiveness of the audit committee's oversight in an audit of only the financial statements, if the auditor becomes aware that the oversight of the company's external financial reporting and internal control over financial reporting by the company's audit committee is ineffective, the auditor must communicate that information in writing to the board of directors.

- g. The last sentence of paragraph 9 is replaced with –

In an audit of financial statements only, auditing interpretation 1 to AU sec. 325, "Reporting on the Existence of Material Weaknesses," continues to apply except that the term "reportable condition" means "significant deficiency" as defined in paragraph 2 of this standard.

AU sec. 9325, "Communication of Internal Control Related Matters Noted in an Audit: Auditing Interpretations of Section 325"

AU sec. 9325, "Communication of Internal Control Related Matters Noted in an Audit: Auditing Interpretations of Section 325" is amended as follows –

The note prior to paragraph 1 is replaced with –

Note: In an audit of financial statements only, auditing interpretation 1 to AU sec. 325, "Reporting on the Existence of Material Weaknesses," continues to apply except that the term "reportable condition" means "significant deficiency" as defined in paragraph 2 of this standard. Within the example report within paragraph 4 of the interpretation, the third sentence is replaced with the definition of a material weakness in paragraph A7 of Appendix A, *Definitions*, of PCAOB Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*.

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AU sec. 328, "Auditing Fair Value Measurements and Disclosures"

SAS No. 101, "Auditing Fair Value Measurements and Disclosures" (AU sec. 328, "Auditing Fair Value Measurements and Disclosures"), is amended as follows –

The first sentence of paragraph 41 is replaced with –

Events and transactions that occur after the balance-sheet date but before the date of the auditor's report (for example, a sale of an investment shortly after the balance-sheet date), may provide audit evidence regarding management's fair value measurements as of the balance-sheet date ^{7/}

^{7/} The auditor's consideration of a subsequent event or transaction, as contemplated in this paragraph, is a substantive test and thus differs from the review of subsequent events performed pursuant to section 560, *Subsequent Events*.

AU sec. 332, "Auditing Derivative Instruments, Hedging Activities, and Investments in Securities"

SAS No. 92, "Auditing Derivative Instruments, Hedging Activities, and Investments in Securities" (AU sec. 332, "Auditing Derivative Instruments, Hedging Activities, and Investments in Securities"), is amended as follows –

The note to paragraph 11 is replaced with –

Note: When performing an integrated audit of financial statements and internal control over financial reporting, paragraph 39 of PCAOB Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*, states "[t]he auditor should test those controls that are important to the auditor's conclusion about whether the company's controls sufficiently address the assessed risk of misstatement to each relevant assertion." Therefore, in an integrated audit of financial statements and internal control over financial reporting, if there are relevant assertions related to the company's investment in derivatives and securities, the auditor's understanding of controls should include controls over derivatives and securities transactions from their initiation to their inclusion in the financial statements and should

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encompass controls placed in operation by the entity and service organizations whose services are part of the entity's information system.

AU sec. 333, "Management Representations"

SAS No. 85, "Management Representations" (AU sec. 333, "Management Representations"), as amended, is amended as follows –

- a. Within the note to paragraph 5, the reference to paragraphs 142-144 of PCAOB Auditing Standard No. 2 is replaced with a reference to paragraphs 75-77 of PCAOB Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*.

- b. The second sentence of paragraph 9 is replaced with –

Because the auditor is concerned with events occurring through the date of his or her report that may require adjustment to or disclosure in the financial statements, the representations should be made as of the date of the auditor's report.

AU sec. 9337, "Inquiry of a Client's Lawyer Concerning Litigation, Claims, and Assessments: Auditing Interpretations of Section 337"

AU sec. 9337, "Inquiry of a Client's Lawyer Concerning Litigation, Claims, and Assessments: Auditing Interpretations of Section 337" is amended as follows –

- a. The last sentence of paragraph 4 is replaced with –

What is the relationship between the effective date of the lawyer's response and the date of the auditor's report?

- b. Paragraph 5 is replaced with –

Interpretation – Section 560.10 through .12 indicates that the auditor is concerned with events, which may require adjustment to, or disclosure in, the financial statements, occurring through the date of his or her report. Therefore, the latest date of the period covered by the lawyer's response (the "effective date") should be as close to the date of the auditor's report

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as is practicable in the circumstances. Consequently, specifying the effective date of the lawyer's response to reasonably approximate the expected date of the auditor's report will in most instances obviate the need for an updated response from the lawyer.

AU sec. 341, "The Auditor's Consideration of an Entity's Ability to Continue as a Going Concern"

SAS No. 59, "The Auditor's Consideration of an Entity's Ability to Continue as a Going Concern" (AU sec. 341, "The Auditor's Consideration of an Entity's Ability to Continue as a Going Concern"), as amended, is amended as follows –

The second sentence of paragraph 2 is replaced with –

The auditor's evaluation is based on his or her knowledge of relevant conditions and events that exist at or have occurred prior to the date of the auditor's report.

AU sec. 342, "Auditing Accounting Estimates"

SAS No. 57, "Auditing Accounting Estimates" (AU sec. 342, "Auditing Accounting Estimates"), is amended as follows –

a. Subparagraph c. of paragraph 10 is replaced with –

c. Review subsequent events or transactions occurring prior to the date of the auditor's report.

b. Paragraph 13 is replaced with –

Review subsequent events or transactions. Events or transactions sometimes occur subsequent to the date of the balance sheet, but prior to the date of the auditor's report, that are important in identifying and evaluating the reasonableness of accounting estimates or key factors or assumptions used in the preparation of the estimate. In such circumstances, an evaluation of the estimate or of a key factor or assumption may be minimized or unnecessary as the event or transaction can be used by the auditor in evaluating their reasonableness.

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AU sec. 380, "Communication With Audit Committees"

SAS No. 61, "Communication With Audit Committees" (AU sec. 380, "Communication With Audit Committees"), as amended, is amended as follows –

Within footnote 1 to paragraph 1, the reference to PCAOB Auditing Standard No. 2 is replaced with a reference to PCAOB Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*.

AU sec. 508, "Reports on Audited Financial Statements"

SAS No. 58, "Reports on Audited Financial Statements" (AU sec. 508, "Reports on Audited Financial Statements"), as amended, is amended as follows –

Within the note to paragraph 1, the reference to paragraphs 162-199 of PCAOB Auditing Standard No. 2 is replaced with a reference to paragraphs 85-98 of PCAOB Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements* and Appendix C, *Special Reporting Situations*, of PCAOB Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*. The sentence that reads "In addition, see Appendix A, *Illustrative Reports on Internal Control Over Financial Reporting*, of PCAOB Auditing Standard No. 2, which includes an illustrative combined audit report and examples of separate reports," is replaced with, "In addition, see paragraphs 86-88 of PCAOB Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements* which includes an illustrative combined audit report."

AU sec. 530, "Dating of the Independent Auditor's Report"

SAS No. 1, "Codification of Auditing Standards and Procedures," section 530, "Dating of the Independent Auditor's Report" (AU sec. 530, "Dating of the Independent Auditor's Report"), as amended, is amended as follows –

- a. Paragraph .01 is replaced with –

The auditor should date the audit report no earlier than the date on which the auditor has obtained sufficient competent evidence to support the

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auditor's opinion. Paragraph .05 describes the procedure to be followed when a subsequent event occurring after the report date is disclosed in the financial statements.

Note: When performing an integrated audit of financial statements and internal control over financial reporting, the auditor's reports on the company's financial statements and on internal control over financial reporting should be dated the same date.

Note: If the auditor concludes that a scope limitation will prevent the auditor from obtaining the reasonable assurance necessary to express an opinion on the financial statements, then the auditor's report date is the date that the auditor has obtained sufficient competent evidence to support the representations in the auditor's report.

- b. Paragraph .05 is replaced with –

The independent auditor has two methods for dating the report when a subsequent event disclosed in the financial statements occurs after the auditor has obtained sufficient competent evidence on which to base his or her opinion, but before the issuance of the related financial statements. The auditor may use "dual dating," for example, "February 16, 20__, except for Note __, as to which the date is March 1, 20__," or may date the report as of the later date. In the former instance, the responsibility for events occurring subsequent to the original report date is limited to the specific event referred to in the note (or otherwise disclosed). In the latter instance, the independent auditor's responsibility for subsequent events extends to the later report date and, accordingly, the procedures outlined in section 560.12 generally should be extended to that date.

- c. Within the heading before paragraph .03, the reference to "completion of field work" is replaced with "the date of the independent auditor's report."

AU sec. 543, "Part of Audit Performed by Other Independent Auditors"

SAS No. 1, "Codification of Auditing Standards and Procedures," section 543, "Part of Audit Performed by Other Independent Auditors" (AU sec. 543, "Part of Audit Performed by Other Independent Auditors"), as amended, is amended as follows –

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Within the note to paragraph .01, the reference to paragraphs 182-185 of PCAOB Auditing Standard No. 2 is replaced with a reference to paragraphs C8-C11 of Appendix C, *Special Reporting Situations*, of PCAOB Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*.

AU sec. 560, "Subsequent Events"

SAS No. 1, "Codification of Auditing Standards and Procedures," section 560, "Subsequent Events" (AU sec. 560, "Subsequent Events"), as amended, is amended as follows –

- a. Within the note to paragraph .01, the reference to paragraphs 186-189 of PCAOB Auditing Standard No. 2 is replaced with a reference to paragraphs 93-97 of PCAOB Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*.
- b. The second sentence of paragraph .12 is replaced with –

These procedures should be performed at or near the date of the auditor's report.

AU sec. 561, "Subsequent Discovery of Facts Existing at the Date of the Auditor's Report"

SAS No. 1, "Codification of Auditing Standards and Procedures," section 561, "Subsequent Discovery of Facts Existing at the Date of the Auditor's Report" (AU sec. 561, "Subsequent Discovery of Facts Existing at the Date of the Auditor's Report"), as amended, is amended as follows –

Within the note to paragraph .01, the reference to paragraph 197 of PCAOB Auditing Standard No. 2 is replaced with a reference to paragraph 98 of PCAOB Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*.

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AU sec. 711, "Filings Under Federal Securities Statutes"

SAS No. 37, "Filings Under Federal Securities Statutes" (AU sec. 711, "Filings Under Federal Securities Statutes"), is amended as follows –

- a. Within the note to paragraph 2, the reference to paragraphs 198-199 of PCAOB Auditing Standard No. 2 is replaced with a reference to paragraphs C16-C17 of Appendix C, *Special Reporting Situations*, of PCAOB Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*.

- b. The third sentence of paragraph 10 is replaced with –

The likelihood that the auditor will discover subsequent events necessarily decreases following the date of the auditor's report, and, as a practical matter, after that time the independent auditor may rely, for the most part, on inquiries of responsible officials and employees.

AU sec. 722, "Interim Financial Information"

SAS No. 100, "Interim Financial Information" (AU sec. 722, "Interim Financial Information"), is amended as follows –

- a. The following is inserted after the first sentence of paragraph 3 –

The SEC also requires management, with the participation of the principal executive and financial officers (the certifying officers) to make certain quarterly and annual certifications with respect to the company's internal control over financial reporting.^{2/}

^{2/} See Section 302 of the Sarbanes-Oxley Act of 2002, and Securities Exchange Act Rule 13a-14(a) or 15d-14(a), (17 C.F.R. § 240.13a-14a or 17 C.F.R. § 240.15d-14a), whichever applies.

- b. The note to paragraph 3 is deleted.

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- c. The following is added to the end of paragraph 7 –

Likewise, the auditor's responsibility as it relates to management's quarterly certifications on internal control over financial reporting is different from the auditor's responsibility as it relates to management's annual assessment of internal control over financial reporting. The auditor should perform limited procedures quarterly to provide a basis for determining whether he or she has become aware of any material modifications that, in the auditor's judgment, should be made to the disclosures about changes in internal control over financial reporting in order for the certifications to be accurate and to comply with the requirements of Section 302 of the Act.

Note: The auditor's responsibilities for evaluating management's certification disclosures about internal control over financial reporting take effect beginning with the first quarter after the company's first annual assessment of internal control over financial reporting as described in Item 308(a)(3) of Regulations S-B and S-K.

- d. The following lettered section is added to the end of paragraph 18 –

- g. Evaluating management's quarterly certifications about internal control over financial reporting by performing the following procedures –

- Inquiring of management about significant changes in the design or operation of internal control over financial reporting as it relates to the preparation of annual as well as interim financial information that could have occurred subsequent to the preceding annual audit or prior review of interim financial information;
- Evaluating the implications of misstatements identified by the auditor as part of the auditor's other interim review procedures as they relate to effective internal control over financial reporting; and

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- Determining, through a combination of observation and inquiry, whether any change in internal control over financial reporting has materially affected, or is reasonably likely to materially affect, the company's internal control over financial reporting.

e. Paragraph 29 is replaced with –

As a result of conducting a review of interim financial information, the accountant may become aware of matters that cause him or her to believe that –

- a. material modification should be made to the interim financial information for it to conform with generally accepted accounting principles;
- b. modification to the disclosures about changes in internal control over financial reporting is necessary for the certifications to be accurate and to comply with the requirements of Section 302 of the Act and Securities Exchange Act Rule 13a-14(a) or 15d-14(a), whichever applies; and
- c. the entity filed the Form 10-Q or Form 10-QSB before the completion of the review.

In such circumstances, the accountant should communicate the matter(s) to the appropriate level of management as soon as practicable.

f. Paragraph 32 is replaced with –

If the auditor becomes aware of information indicating that fraud or an illegal act has or may have occurred, the auditor must also determine his or her responsibilities under AU sec. 316, *Consideration of Fraud in a Financial Statement Audit*, AU sec. 317, *Illegal Acts by Clients*, and Section 10A of the Securities Exchange Act of 1934.^{1/}

^{1/} See 15 U.S.C. § 78j-1

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- g. Within paragraph 33, the third sentence is replaced with –

A significant deficiency is a deficiency, or a combination of deficiencies, in internal control over financial reporting, that is less severe than a material weakness yet important enough to merit attention by those responsible for oversight of the company's financial reporting.

Auditing Standard No. 3, *Audit Documentation*

Auditing Standard No. 3, *Audit Documentation* is amended as follows –

Within footnote 2 to paragraph 6, the reference to paragraphs 68-70 of Auditing Standard No. 2 is replaced with a reference to paragraphs 28-33 of Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*.

Auditing Standard No. 4, *Reporting on Whether a Previously Reported Material Weakness Continues to Exist*

Auditing Standard No. 4, *Reporting on Whether a Previously Reported Material Weakness Continues to Exist* is amended as follows –

- a. Within note 1 to paragraph 1, the reference to Auditing Standard No. 2 is replaced with a reference to Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*.
- b. Within paragraph 2, the two references to Auditing Standard No. 2 are replaced with references to Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*.
- c. Within the note to paragraph 2, the reference to Auditing Standard No. 2 is replaced with a reference to Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*.
- d. Within paragraph 4, the reference to Auditing Standard No. 2 is replaced with a reference to Auditing Standard No. 5, *An Audit of Internal Control*

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Over Financial Reporting That Is Integrated with An Audit of Financial Statements.

- e. Paragraph 9 is replaced with –

The terms *internal control over financial reporting*, *deficiency*, *significant deficiency*, and *material weakness* have the same meanings as the definitions of those terms in Appendix A, *Definitions*, of Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*.

- f. The first sentence of paragraph 10 is replaced with –

Paragraph 5 of Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*, states “[t]he auditor should use the same suitable, recognized control framework to perform his or her audit of internal control over financial reporting as management uses for its annual evaluation of the effectiveness of the company's internal control over financial reporting.”

- g. Within the note to paragraph 10, the reference to Auditing Standard No. 2 in the first sentence is replaced with a reference to Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*, and the last sentence is amended as follows –

More information about the COSO framework is included within the COSO report.

- h. Paragraph 11 is replaced with –

The terms *relevant assertion* and *control objective* have the same meaning as the definitions of those terms in Appendix A, *Definitions*, of Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*.

- i. Paragraph 13 is replaced with –

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In an audit of internal control over financial reporting, the auditor should test the design effectiveness of controls by determining whether the company's controls, if they are operated as prescribed by persons possessing the necessary authority and competence to perform the control effectively, satisfy the company's control objectives and can effectively prevent or detect errors or fraud that could result in material misstatements in the financial statements.^{2/}

^{2/} See paragraph 42 of Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*.

- j. Within the note to paragraph 17, the reference to Auditing Standard No. 2 is replaced with a reference to Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*.
- k. Within note 2 to paragraph 18, the reference to Auditing Standard No. 2 is replaced with a reference to Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*.
- l. Within paragraph 21, the last sentence is deleted.
- m. Within paragraph 23, the reference to paragraphs 22 and 23 of Auditing Standard No. 2 is replaced with a reference to paragraph 20 of Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*. Additionally, the second sentence is deleted.
- n. Within paragraph 24, the reference to paragraph 39 of Auditing Standard No. 2 is replaced with a reference to paragraph 9 of Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*.
- o. Within paragraph 25, the reference to Auditing Standard No. 2 is replaced with a reference to Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*.

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- p. Within the note to paragraph 25, the two references to Auditing Standard No. 2 are replaced with references to Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*.
- q. Within subparagraph a. of paragraph 26, the reference to paragraphs 47 through 51 of Auditing Standard No. 2 is replaced with a reference to paragraphs 22-27 of Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*.
- r. Subparagraph b. of paragraph 26 is replaced with –

Perform the procedures described in paragraphs 34-38 of Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*, for those transactions that are directly affected by controls specifically identified by management as addressing the material weakness.
- s. The note to subparagraph b. of paragraph 26 is deleted.
- t. Within paragraph 27, the reference to Auditing Standard No. 2 is replaced with a reference to Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*.
- u. The note to paragraph 28 is deleted.
- v. Within paragraph 31, the reference to paragraphs 88 through 91 of Auditing Standard No. 2 is replaced with a reference to paragraphs 42-43 of Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*.
- w. Paragraph 32 is replaced with –

Consistent with the direction in paragraphs 44-45 of Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*, the auditor should test the operating effectiveness of a specified control by determining whether the

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specified control operated as designed and whether the person performing the control possesses the necessary authority and qualifications to perform the control effectively. In determining the nature, timing, and extent of tests of controls, the auditor should apply paragraphs 50-54 of Auditing Standard No. 5.

- x. Paragraph 33 is replaced with –

The auditor should perform tests of the specified controls over a period of time that is adequate to determine whether, as of the date specified in management's assertion, the controls necessary for achieving the stated control objective are operating effectively. The timing of the auditor's tests should vary with the risk associated with the control being tested. For example, a transaction-based, daily reconciliation generally would permit the auditor to obtain sufficient evidence as to its operating effectiveness in a shorter period of time than a pervasive, entity-level control, such as any of those described in paragraphs 22-24 of Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*. Additionally, the auditor typically will be able to obtain sufficient evidence as to the operating effectiveness of controls over the company's period-end financial reporting process only by testing those controls in connection with a period-end.

- y. Within paragraph 35, the reference to paragraphs B1 through B13 of Appendix B of Auditing Standard No. 2 is replaced with a reference to paragraphs B10-B16 of Appendix B, *Special Topics*, of Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*.
- z. Within paragraph 36, the reference to paragraphs 109 through 115 and 117 through 125 of Auditing Standard No. 2 is replaced with a reference to paragraphs 16-19 of Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*.
- aa. The second sentence of paragraph 37 is replaced with –

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Therefore, if the auditor has been engaged to report on more than one material weakness or on more than one stated control objective, the auditor must evaluate whether he or she has obtained sufficient evidence that the control objectives related to each of the material weaknesses identified in management's assertion are achieved.

- bb. The first two sentences of paragraph 38 are replaced with –

Paragraphs 18-19 of Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*, should be applied in the context of the engagement to report on whether a previously reported material weakness continues to exist.

- cc. The note to paragraph 38 is deleted.

- dd. The note to paragraph 39 is deleted.

- ee. Paragraph 42 is replaced with –

Management may conclude that a previously reported material weakness no longer exists because its severity has been sufficiently reduced such that it is no longer a material weakness.

- ff. Subparagraph f. of paragraph 44 is replaced with –

Describing any fraud resulting in a material misstatement to the company's financial statements and any other fraud that does not result in a misstatement in the company's financial statements but involves senior management or management or other employees who have a significant role in the company's internal control over financial reporting and that has occurred or come to management's attention since the date of management's most recent annual assessment of internal control over financial reporting.

- gg. Within the note to subparagraph b. of paragraph 51, the reference to Auditing Standard No. 2 is replaced with a reference to Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*.

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- hh. Within the note to subparagraph l. of paragraph 51, the reference to Auditing Standard No. 2 is replaced with a reference to Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*.
- ii. Within the note to the second bullet point of subparagraph o. of paragraph 51, the reference to Auditing Standard No. 2 is replaced with a reference to Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*.
- jj. Within paragraph 52, the reference to Auditing Standard No. 2 is replaced with a reference to Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements*.
- kk. Within paragraph 63, the reference to paragraphs 202 through 206 of Auditing Standard No. 2 is replaced with a reference to paragraphs 7 and 29-32 of AU sec. 722, *Interim Financial Information*.
- ll. Within paragraph 64, the reference to paragraphs 202 through 206 of Auditing Standard No. 2 is replaced with a reference to paragraphs 7 and 29-32 of AU sec. 722, *Interim Financial Information*.