

Compilation Engagements - Third Party Approval of Basis of Accounting

December 31, 2021



Overview of this Resource

Under CSRS 4200 requirements, management is required to obtain third party approval of the expected basis of accounting from those who are not in a position to obtain further information from the entity (e.g. minority shareholders). It is the practitioner's responsibility to obtain acknowledgment from management, where applicable, that third parties have provided their approval. Although the requirement is not onerous, there are a few practical issues when servicing smaller clients.

The first is that management generally is not in a position to execute this communication without our assistance. The specifics of discussing the appropriate basis of accounting and third party needs of financial information may not be an area of comfort for the client. In these cases, we will be assisting management through the provision of a template email to forward to third parties. Where there are concerns raised, we will advise management to involve us in the discussion.

However, we have also considered the level of evidence we would like to have in our file documentation that this approval has been adequately obtained, especially given the requirement that without this approval engagement acceptance may not appropriate. We can see situations arising where as part of our risk management strategies we would like to have formal documentation on file that the third party has agreed to the basis of accounting. Situations where we believe more formal communication could be desirable include:

- Buy/sell arrangements where the purchaser may not fully appreciate the future needs of users of the financial statements;
- Where there is conflicting information between managements acknowledgements and our understanding of the third party requirements;
- In order to dispel any concerns that management has not communicated with third parties; or
- When it appears necessary to obtain documentation that you have advised that an assurance engagement may be more appropriate.

We would like to reiterate that formal documentation supporting third party approval of the basis of accounting is not a requirement of the standard. The suggestions and guidance provided in this document are related to client assistance and practice management considerations. Note also that we recommend the client initiate the email communication. Direct communication with third parties is not required, nor recommended, under non-assurance engagements for risk management and potential liability.

About Us

Clearline Consulting provides practitioners and their staff with the tools, training and advice they need to succeed and build thriving accounting firms. From compliance and file monitoring to professional development courses, staff training and customized consulting solutions, our team exists to serve the needs of small to mid-sized public practice firms. Our collaborative, integrated approach means clients have access to and support from knowledgeable people who are in front of the ever-changing standards environment.

To assist you in the development of your firm's processes and file documentation requirements we have provide an extract of the requirements as provided in CSRS 4200: Compilation Engagements.

Related Requirements - Extracts from CSRS 4200

When the Compiled Financial Information Is Intended to Be Used by a Third Party

23. *When the compiled financial information is intended to be used by a third party, the practitioner may accept or continue the engagement if, according to management, the third party:*

- (a) Is in a position to request and obtain further information from the entity; or (Ref: Para. A16-A17)*
- (b) Has agreed with management the basis of accounting to be applied in the preparation of the compiled financial information. (Ref: Para. A18)*

If neither (a) nor (b) above are met, the practitioner shall not accept or continue the engagement, unless the basis of accounting to be applied in the preparation of the compiled financial information is a general purpose framework. (Ref: Para. A19)

A18. *A third party may have agreed with management the basis of accounting to be applied in the preparation of the compiled financial information, in writing or orally. The practitioner is not required to verify whether the third party has agreed to that basis of accounting. Management's acknowledgment that it has agreed with the third party the basis of accounting to be applied in the preparation of the compiled financial information is included in the engagement letter or other suitable form of written agreement, as required by paragraph 25(c)(ii).*

A21. *There may be circumstances where law, regulation or contractual provisions with a third party require the entity's financial information to be subject to an audit engagement or a review engagement. In the case of contractual provisions with a third party, management may have confirmed with the third party that it will accept compiled financial information. When management has not obtained such confirmation, the practitioner may consider recommending that management do so. The practitioner is not required to perform procedures to verify that the third party provided such confirmation. Management's acknowledgment for the matters in paragraph 25(e)(i)-(ii) is sufficient.*

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Draft Communication – Tailor to Firm Preferences

Dear Third Party,

In discussion with our accountant, [insert], we would like to bring to your attention a change in the accounting requirements for our compiled financial statements. The financial statements will include disclosure, providing information related to the basis of accounting.

The proposed basis of accounting is to apply the historical cost basis, reflecting cash transactions with the addition of the necessary accruals and/or estimates as noted below. This accounting treatment is expected to result in financial statements, that are consistent with those provided in prior years, with the addition of the following disclosure:

Basis of Accounting [to be tailored to client specifics]

The basis of accounting applied in the preparation of the financial information is on the historical cost basis, reflecting cash transactions with the addition of:

- *Accounts receivable less an allowance for doubtful accounts*
- *Inventory valued using the retail method*
- *Property, plant and equipment amortized on the same basis as for income tax*
- *Accounts payable and accrued liabilities*
- *Current income taxes payable as at the reporting date*

Should there be any necessary modifications identified throughout the engagement, management will approve these and the finalized basis of accounting will be disclosed in the financial statements.

For further information about this new standard as well as a copy of the new compilation engagement report, please review to the professional publication found here [CPA Canada Third Party Briefing](#).

Should the above noted basis of accounting, or the provision of a compilation engagement, no longer be sufficient for your purposes please let us know as soon as possible as we will need to discuss this with our external accountants and plan according.

Link to CPA Canada Third Party Briefing Document

<https://www.cpacanada.ca/en/business-and-accounting-resources/audit-and-assurance/standards-other-than-cas/publications/new-Compilation-standard-guidance-resources/third-party-briefing>