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Find the financial statement that fits your business' needs

By EVELYN A. WILLIAMS, October 12, 2015

"The company needs an audit."

This statement often is heard from small-business owners when asked to provide financial statements. An audit, though, is not always what is required.

A discussion regarding the purpose of the financial statements will clarify the situation, then a Certified Public Accountant can explain to the business owner the alternative levels of service that provide unaudited financial statements. These types of engagements are compilations, reviews and a new service called preparations.

With a clear understanding of the purpose of the financial statements, the correct decision on the level of service can be made appropriately without wasting resources.

Audits provide the highest level of independent CPA financial statement service. The purpose of an audit is to provide financial statements with an opinion by the auditor on whether the financial statements are prepared in accordance with the proper financial-reporting framework.

This is accomplished by independently verifying the company's financial reports through confirmation, observation, inquiries of management and assessment of the company's internal controls.

In addition to these procedures, the auditor also is required to obtain reasonable assurance that financial statements are not materially misstated because of fraud and to communicate deficiencies or weaknesses found in the company's internal controls. This assessment of fraud risk and internal controls is what differentiates the audit, as they are not required in review or compilation engagements.

Review engagements include procedures that enable the accountant to provide limited assurance on the financial statements. A review consists of an assessment of the company's books and records through the performance of management inquiries, analytical procedures (such as the comparison to prior books and records) and calculation of certain financial tests and ratios.

These procedures, by their very nature, are intended to give reasonable assurance to financial statement users, rather than the detailed verification and additional testing required by an audit.

As is the case with audits, a CPA must be independent to provide a reviewed financial statement. Reviews are frequently requested by banks or insurance companies issuing performance bonds that want a higher degree of service/verification than a compilation but not the full extent and cost of an audit.

The lowest level of attest service that a CPA can provide for a company's financial statements is a compilation.

The main objective is to assist management in presenting financial statements that include a compilation report stating the financials were compiled by a CPA. The CPA simply pulls together the books and records of a client without the performance of any substantive procedures, independent verification or confirmation of any of the amounts reported.

Thus, a compilation is solely the representation of a company's management, as no verification of account balances on the balance sheet or the profit and loss statements is required. The CPA does not need to be independent to issue this type of report, but must disclose the lack of independence.

Also, management has the option to exclude from compiled financial statements the statement of cash flow and all related footnotes.

For years ending after Dec. 15, 2015, there is a new nonattest service called a preparation, which allows a CPA to prepare financial statements without issuing an accompanying audit, review or compilation report.

The CPA is not required to make a determination regarding independence, and the statements will only require that each page says "no assurance is provided."

These can be used for internal purposes or presented to third parties. Since this is a new service, it is too early to determine the acceptability of these types of nonattest statements by third-party users.

Although this is a general overview, it is important for business owners to understand these options when deciding on the level of involvement needed by their CPA in the financial reporting process.

A greater understanding of the alternatives should help business owners make appropriate and cost-effective choices.

Evelyn A. Williams, Certified Public Accountant, is a shareholder with Buckno Lisicky & Company in Allentown and a member of the Pennsylvania Institute of Certified Public Accountants, serving on several committees. She can be reached at ewilliams@blco-cpa.com.