

**August 2010**

**ALERT: New Accounting Standards to Replace SAS 70 Standard**

There are 2 new accounting standards that are replacing the SAS 70 standard. Statement on Standards for Attestation Engagements (SSAE) No. 16, Reporting on Controls at a Service Organization, has been finalized by the Auditing Standards Board of the American Institute of Certified Public Accountants (AICPA). SSAE 16 effectively replaces SAS 70 by superseding the guidance for service auditors in AU section 324 of the AICPA Professional Standards. SSAE 16 was formally issued in April 2010 with an effective date of June 15, 2011. SSAE 16 was drafted with the intention and purpose of updating the US service organization reporting standard so that it mirrors and complies with the new international service organization reporting standard – ISAE 3402 <[http://sas70.com/sas70\\_ISAE3402.html](http://sas70.com/sas70_ISAE3402.html)>.

SAS 70 was developed as an auditor-to-auditor communication, a way for the service auditor to share audit workpapers with the user auditor, who then could rely on this work in planning and executing the financial statement audit. However, the regulatory landscape has seen significant changes, and governments, regulators, boards of directors and financial statement users are placing ever-increasing emphasis on internal control over financial reporting. These stakeholders, as well as the user auditors, now need a report from and by the service organization describing its internal control. This, in turn, significantly increases the importance of management’s description of its system. The independent service auditor’s opinion remains critical, but its role is as a provider of assurance, not the entity responsible for the communication.

Under the New Standards, service organizations have five primary responsibilities:

1. Prepare and present a complete and accurate description of the system
2. Specify the control objectives of the system and state those control objectives in the description of the system
3. Identify the risks that threaten the achievement of the control objectives (although these risks are not included in the service organization report)
4. Design, implement and maintain controls to provide reasonable assurance that the control objectives will be achieved
5. Provide a written assertion to accompany the description as to the completeness and accuracy of the information provided and state the criteria used as a basis for making the assertion.

Under SAS 70, a service organization provides a “description of controls.” Under SSAE 16, a

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service organization provides a “description of its system” as designed and implemented. While the term “system” has many different definitions, a common and useful definition is “the procedures, people, software, data and infrastructure organized to achieve a specific objective.” The new standards require a broader management description as the service organization’s description of its system includes:

- Description of the services provided, including classes of transactions processed. For service organizations that process transactions for user entities, a description of the classes of transactions processed should provide the information necessary to identify a user entity’s significant accounts to which the transactions are posted.
- Description of the procedures by which services are provided, including transaction initiation, authorization, recording, processing and correction. The description of the system should provide an understanding of the flow of transactions or activities from start to finish, as well as the processes by which information errors are corrected.
- Description of the capturing of significant events and conditions other than transactions, such as information technology general controls.
- Description of the process used to prepare reports or information provided to user entities. A description of the process used to prepare reports and provide information relates the other controls in the report to the transactions reflected in the financial statements and the information that user entity management relies on to run the business.
- Description of aspects of the service organization’s control environment, risk assessment process, information and communications systems, control activities and monitoring controls.

Under SSAE 16, other responsibilities of the service organization include providing a written assertion in the report. The assertion is a separate component of the report, typically on the service organization’s letterhead and signed by a member of management. The assertion communicates:

- Service organization management’s responsibility for the description of the system
- Achievement of the evaluation criteria of the description of the system
- Identifying risks that threaten the achievement of the control objectives. SSAE 16 requires the service organization to support its assertion by:
  - Identifying the risks that threaten the achievement of the control objectives
  - Determining whether the controls would, if operating as described, provide reasonable assurance that those risks would not prevent the control objectives from being achieved (these risks do not need to be described)

The AICPA is expected to release guidance on SSAE 16 in early 2011. Based on our current understanding, we do not believe that significant changes to typical SAS 70 reporting and no significant additional testing will be required. The biggest change will be the inclusion of your written assertion in the report.

For guidance on how to proceed, please contact Sue Peirce: [speirce@applegrowth.com](mailto:speirce@applegrowth.com) or 330-867-7350, or visit our website: [www.applegrowth.com](http://www.applegrowth.com).