



***Statement on
Auditing Standards***
Issued by the Auditing Standards Board

August 2022
148

AMENDMENT TO AU-C SECTION 935

***(Amends Statement on Auditing Standards [SAS] No. 117, Compliance Audits, as amended
[AICPA, Professional Standards, AU-C sec. 935])***

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Statement on Auditing Standards No. 148, *Amendment to AU-C Section 935*

Executive Summary

Background

AU-C section 935, *Compliance Audits*,¹ addresses the application of generally accepted auditing standards (GAAS) to a compliance audit. AU-C sections 200–900 address audits of financial statements as well as other kinds of engagements. Generally, these AU-C sections can be adapted to the objectives of a compliance audit. However, certain AU-C sections, or portions thereof, are not applicable to a compliance audit because (a) they are not relevant to a compliance audit environment; (b) the procedures and guidance would not contribute to meeting the objectives of a compliance audit; or (c) the subject matter is specifically covered in AU-C section 935. These AU-C sections, or specified requirements thereof, are identified in the appendix to AU-C section 935, “AU-C Sections That Are Not Applicable to Compliance Audits” (the appendix).

SAS No. 148 amends AU-C section 935 to update the appendix and conform AU-C section 935 to reflect the issuance of the following SASs:

- SAS No. 142, *Audit Evidence* (AU-C section 500)
- SAS No. 145, *Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement* (AU-C section 315)

The Auditing Standards Board (ASB) has determined that no amendment is necessary to AU-C section 935 to reflect the issuance of the following SASs:

- SAS No. 143, *Auditing Accounting Estimates and Related Disclosures* (AU-C section 540)
- SAS No. 144, *Amendments to AU-C Sections 501, 540, and 620 Related to the Use of Specialists and the Use of Pricing Information Obtained From External Information Sources*

SAS No. 143 is codified in AU-C section 540, which is listed in the appendix as not applicable in its entirety to a compliance audit. SAS No. 144 amends only certain application material that is not relevant to AU-C section 935.

Explanation of Changes

Revisions Arising From SAS No. 142

SAS No. 142 superseded SAS No. 122, *Statements on Auditing Standards: Clarification and Recodification*, section 500, *Audit Evidence* (AU-C sec. 500A), and amended various AU-C sections, including AU-C section 501, *Audit Evidence — Specific Considerations for Selected Items*. The amendments in SAS No. 142 moved what had been paragraph .08 of AU-C section 500A, relating to using the work of a management’s specialist, to become paragraph .27 of AU-C section 501, without any substantive changes to that paragraph. This paragraph was applicable to compliance audits when it was in AU-C section 500A, and that applicability didn’t change when it was relocated. Accordingly, the appendix is revised to reflect the continued applicability of this paragraph in a compliance audit. No other paragraph in AU-C section 501 applies to a compliance audit.

Revisions Arising From SAS No. 145

¹ All AU-C sections can be found in AICPA *Professional Standards*.

- Paragraphs .12c, .26–.30, and .33c of AU-C section 315A are not applicable to a compliance audit. The appendix was updated to include comparable paragraphs (19b, 20, 32–34, 36, and 42d) of SAS No. 145 as not applicable to a compliance audit.
- Paragraphs 27a of SAS No. 145, which relates to controls over significant risks, and paragraph 40, which relates to classes of transactions, account balances, and disclosures that are not significant but are material, were added to the appendix as not applicable in a compliance audit. Historically, the concept of significant risks has not been applicable to a compliance audit. Likewise, the concept of classes of transactions, account balances, and disclosures that are material is not applicable to a compliance audit.
- Paragraphs 26 and 27b–30 of SAS No. 145, which address requirements related to the control activities component, apply to a compliance audit. In particular, paragraph 27b–d addresses certain controls that the auditor is required to identify. A new requirement was added to AU-C section 935 to address the auditor’s responsibility in adapting and applying paragraphs 27b–30 of SAS No. 145 in a compliance audit. This new requirement also includes controls over compliance that are required to be tested for operating effectiveness by a governmental audit requirement (paragraph .20 of extant AU-C section 935). Thus, the new requirement combines the auditor’s responsibilities under SAS No. 145 and AU-C section 935. Paragraphs 28–29 of SAS No. 145 include additional requirements related to control activities related to risks arising from the use of IT that also apply to a compliance audit.
- For ease of use and clarity of the requirements related to identifying and assessing risks of material noncompliance, paragraphs 35 and 37–38 of SAS No. 145, adapted as necessary, were added as requirements directly in AU-C section 935 and, consequentially, included in the appendix as not applicable when applying SAS No. 145 to a compliance audit. Application material was added to AU-C section 935 that references the 22 relevant application material paragraphs for paragraphs 35 and 37–38 in SAS No. 145.
- Extant AU-C section 935 excludes, within the appendix, the documentation requirement related to the identified and assessed risks at the financial statement level and assertion level (paragraph .33c of AU-C section 315A). The ASB believes that this requirement, adapted as necessary, is applicable to a compliance audit and, therefore, a new requirement was added to AU-C section 935 based on paragraph 42d of SAS No. 145, which, consistent with other revisions, excludes significant risks. Accordingly, paragraph 42d of SAS No. 145 has been included in the appendix (and thereby is not applicable in a compliance audit).

Other Revisions

- There is an inconsistency in extant AU-C section 935 whereby the requirements in AU-C section 315 with respect to significant risks were scoped out of a compliance audit, but the requirements in AU-C section 330 with respect to significant risks were not. This inconsistency has been removed by adding paragraphs .15 and .22 of AU-C section 330 to the appendix.
- Paragraph .18 of AU-C section 330 was also added to the appendix because performing substantive procedures for each relevant assertion of each significant class of transactions, account balance, and disclosure is not applicable in a compliance audit.
- Certain other editorial revisions were made for clarity or consistency with other AU-C sections.

Effective Date

The amendment relating to AU-C section 501 in the appendix, “AU-C Sections That Are Not Applicable to Compliance Audits,” is effective for compliance audits for fiscal periods ending on or after December 15, 2022, consistent with the effective date of SAS No. 142. All other amendments are effective for compliance audits for fiscal periods ending on or after December 15, 2023, consistent with the effective date of SAS No. 145.

The effective date of the amendment to the appendix with regard to AU-C section 501 is aligned with the effective date of SAS No. 142 because, as explained previously, this amendment arises from SAS No. 142. This amendment is not intended to change current practice because there were no changes to the underlying requirement; only its placement within GAAS changed. All other amendments in SAS No. 148 arise from SAS No. 145 and, accordingly, their effective date is aligned with the effective date of SAS No. 145.

Early implementation of SAS No. 148 is permitted. Because SAS No. 148 amends AU-C section 935 to reflect the issuance of SAS No. 142 and SAS No. 145, early implementation of SAS No. 148 is expected to occur in conjunction with early implementation of SAS No. 142 or SAS No. 145, as applicable, for compliance audits.

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Note: Statements on Auditing Standards are issued by the Auditing Standards Board, the senior technical body of the AICPA designated to issue pronouncements on auditing matters. The “Compliance With Standards Rule” (ET sec. 1.310.001)² of the AICPA Code of Professional Conduct requires compliance with these standards in an audit of a nonissuer.

² All ET sections can be found in AICPA *Professional Standards*.

STATEMENT ON AUDITING STANDARDS

AMENDMENT TO AU-C SECTION 935

(***Boldface italics*** denotes new language. Deleted text is shown in ~~strikethrough~~.)

Amendment to AU-C Section 935, *Compliance Audits*

1. The amendment relating to AU-C section 501 in the appendix, “AU-C Sections That Are Not Applicable to Compliance Audits,” is effective for compliance audits for fiscal periods ending on or after December 15, 2022. All other amendments are effective for compliance audits for fiscal periods ending on or after December 15, 2023.

[No amendment to paragraph .01.]

.02 This section addresses the application of GAAS to a compliance audit. Compliance audits ~~usually are~~ ***may be*** performed in conjunction with a financial statement ~~an~~ ***audit of a complete set of financial statements, an audit of a single financial statement, or an audit of a specific element, account, or item of a financial statement.*** This section does not apply to the financial statement ~~an~~ ***audit of a complete set of financial statements, an audit of a single financial statement, or an audit of a specific element, account, or item of a financial statement, even when such audit is performed in conjunction with a compliance audit*** component of such engagements. ~~Although certain~~ ***Certain*** AU-C sections are not applicable to a compliance audit, as identified in the appendix, “AU-C Sections That Are Not Applicable to Compliance Audits.,” ~~all AU-C sections other than this section are applicable to the audit of financial statements performed in conjunction with a compliance audit.~~

[No amendment to paragraph .03–.11.]

Requirements

Adapting and Applying the AU-C Sections to a Compliance Audit (Ref: [par. .A5](#) and [.A4042](#))

.12 When performing a compliance audit, the auditor, ~~using~~ ***exercising*** professional judgment, should adapt and apply the AU-C sections to the objectives of a compliance audit, except for the AU-C sections listed in the [appendix](#).

[No amendment to paragraphs .13–.14.]

Performing Risk Assessment Procedures (Ref: [par. .A12–.A1517](#))

.15 For each of the government programs and applicable compliance requirements selected for testing, the auditor should perform risk assessment procedures to obtain a sufficient understanding of the applicable compliance requirements and the entity’s internal control over compliance with the applicable compliance requirements.^{fn 1}

^{fn 1} Paragraphs ~~.03–.12b and .12d–.25.11–.19a, .19c, .21–.26, and .27b–.31~~ of section 315A, *Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement*.

.16 *In adapting and applying the requirements of section 315 to identify controls that address risks of material noncompliance,*^{fn2} *the auditor should perform risk assessment procedures, beyond inquiry, to evaluate whether the following controls that address risks of material noncompliance are effectively designed and determine whether those controls have been implemented:*

- a. *Controls over journal entries and other adjustments as required by section 240, Consideration of Fraud in a Financial Statement Audit*
- b. *Controls for which the auditor plans to test operating effectiveness in determining the nature, timing, and extent of substantive procedures, which include*
 - i. *controls that address risks for which substantive procedures alone do not provide sufficient appropriate audit evidence, and*
 - ii. *controls that are required to be tested for operating effectiveness by the governmental audit requirement as required by paragraph 24 of this section*
- c. *Other controls that, based on the auditor’s professional judgment, the auditor considers appropriate to enable the auditor to identify and assess risks of material noncompliance and design further audit procedures.*

^{fn2} Paragraphs ~~.27b–d and .30~~ of section 315.

[Subsequent footnotes are renumbered. No amendment to paragraph .16, which is renumbered as paragraph .17.]

Identifying and Assessing the Risks of Material Noncompliance (Ref: [par. .A16A17–.A18A19](#))

.1718 The auditor should identify and assess the risks of material noncompliance whether due to fraud or error for each applicable compliance requirement and should consider whether any of those risks are pervasive to the entity’s compliance because they may affect the entity’s compliance with many compliance requirements.

Assessing Inherent Risk

.19 For identified risks of material noncompliance for each applicable compliance requirement, the auditor should assess inherent risk by assessing the likelihood and magnitude of noncompliance. In doing so, the auditor should take into account how, and the degree to which, inherent risk factors affect the susceptibility of compliance requirements to noncompliance.

.20 The auditor should determine whether substantive procedures alone cannot provide sufficient appropriate audit evidence for any of the risks of material noncompliance.

Assessing Control Risk

.21 For identified risks of material noncompliance for each applicable compliance requirement, the auditor should assess control risk based on the auditor's understanding of controls and the auditor's plan to test the operating effectiveness of controls. If the auditor does not plan to test the operating effectiveness of controls, the auditor should assess control risk at the maximum level such that the assessment of the risk of material noncompliance is the same as the assessment of inherent risk.

Performing Further Audit Procedures in Response to Assessed Risks

[No amendment to former paragraphs .18–.19, which are renumbered as paragraphs .22–.23.]

.2024 The auditor should design and perform further audit procedures in response to the assessed risks of material noncompliance. These procedures should include performing tests of controls over compliance if

- a.*** • the auditor's risk assessment includes an expectation of the operating effectiveness of controls over compliance related to the applicable compliance requirements;
- b.*** • substantive procedures alone ~~do not~~**cannot** provide sufficient appropriate audit evidence; or
- c.*** • such tests of controls over compliance are required by the governmental audit requirement.

If any of the conditions in this paragraph are met, the auditor should test the operating effectiveness of controls over each applicable compliance requirement to which the conditions apply in each compliance audit. (Ref: [par. .A2426–.A2527](#))

[No amendment to former paragraphs .21–.39, which are renumbered as paragraphs .25–.43.]

Documentation (Ref: [par. .A4042](#))

.4044 The auditor should document

- a.*** the risk assessment procedures performed, including those related to ~~gaining~~ **obtaining** an understanding of internal control over compliance-, **and** ^{fn 1213}

- b. *the identified and assessed risks of material noncompliance, including risks for which substantive procedures alone cannot provide sufficient appropriate audit evidence, and the rationale for the significant judgments made.*

^{fn 1213} Paragraph ~~.33a–b~~ and ~~.33d.42a–c~~ of section 315A.

[No amendment to former paragraphs .41–.44, which are renumbered as paragraphs .45–.48.]

Application and Other Explanatory Material

[No amendment to paragraphs .A1–.A11.]

Performing Risk Assessment Procedures (Ref: [par. .15–.1617](#))

- .A12** Obtaining an understanding of the government program, the applicable compliance requirements, and the entity’s internal control over compliance establishes a frame of reference within which the auditor plans the compliance audit and exercises professional judgment about *identifying and* assessing risks of material noncompliance and responding to those risks throughout the compliance audit. *The auditor is also responsible for evaluating the audit evidence obtained from the risk assessment procedures and, as applicable, revising the identification or assessment of risks of material noncompliance.* ^{fn15}

^{fn15} Paragraphs .39 and .41 of section 315.

[Subsequent footnotes are renumbered. No amendment to paragraph .A13.]

- .A14** ~~Performing risk assessment procedures to obtain an understanding of the entity’s internal control over compliance includes an evaluation of the design of controls and whether the controls have been implemented. For purposes of GAAS, the system of i~~Internal control consists of the following five interrelated components: the control environment, the entity’s risk assessment *process*, information and communication systems, control activities, and *the entity’s process to monitoring the system of internal control, the information system and communication, and control activities.* Section 315A, *Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement*, contains a detailed discussion of these components. ^{fn 1517}

^{fn 1517} Paragraphs ~~.15–.25.21–.26, .27b–.31,~~ and appendix CB, “*Understanding the Entity’s System of Internal Control–Components*,” of section 315A.

- .A15** *Evaluating whether controls that address risks of material noncompliance are effectively designed, and determining whether those controls have been implemented involves considering whether the identified controls, individually or in combination, are capable of effectively preventing, or detecting and correcting, material noncompliance as well as establishing that the control exists and that the entity is using it.* ^{fn18}

^{fn 18} Paragraph .A105 of section 315.

.A16 Section 315 includes additional requirements related to control activities related to risks arising from the use of IT that also apply to a compliance audit. ^{fn19}

^{fn 19} Paragraphs .28–.29 of section 315.

[Subsequent footnotes are renumbered. No amendment to former paragraph .A15, which is renumbered as paragraph .A17.]

Identifying and Assessing the Risks of Material Noncompliance (Ref: [par. .4718](#))

.A1618Inherent risk ~~Ffactors the auditor may consider~~ ***and other considerations*** in identifying and assessing the risks of material noncompliance ~~are as follows~~ ***may include the following:***

- ***Criteria for identifying and assessing risks of material noncompliance identified by the governmental audit requirement as well as related communications from oversight organizations or regulators***
- The complexity of the applicable compliance requirements
- The susceptibility of the applicable compliance requirements to noncompliance
- The length of time the entity has been subject to the applicable compliance requirements
- The auditor’s observations about how the entity has complied with the applicable compliance requirements in prior years
- The potential effect on the entity of noncompliance with the applicable compliance requirements
- The degree of judgment involved in adhering to the compliance requirements
- The auditor’s assessment of the risks of material misstatement in the financial statement audit

.A1719The auditor may find it helpful to consider the relevant application material in section 315, adapted as necessary for a compliance audit, when ~~In identifying and assessing the risks of material noncompliance, the auditor may evaluate inherent risk of noncompliance and control risk of noncompliance individually or in combination. ^{fn 20}~~

^{fn 20} Paragraphs .A235, .A237–.A244, and .A252–.A263 of section 315.

[Subsequent footnotes are renumbered. No amendment to former paragraphs .A18–.A22, which are renumbered as paragraphs .A20–.A24.]

Performing Further Audit Procedures in Response to Assessed Risks

...

~~.A23~~²⁵The use of **substantive** analytical procedures to ~~gather substantive~~**obtain** evidence **in responding to assessed risks of material noncompliance** is generally less effective in a compliance audit than it is in a financial statement audit. However, substantive analytical procedures may contribute some evidence when performed in addition to tests of transactions and other auditing procedures necessary to provide the auditor with sufficient appropriate audit evidence. (Ref: [par. .4923](#))

[No amendment to former paragraphs .A24–.A42, which are renumbered as paragraphs .A26–.A44.]

Appendix — AU-C Sections That Are Not Applicable to Compliance Audits

~~.A43~~⁴⁵The following AU-C sections and individually enumerated requirement paragraphs of specific AU-C sections are not applicable to a compliance audit performed under this section either because (a) they are not relevant to a compliance audit environment, (b) the procedures and guidance would not contribute to meeting the objectives of a compliance audit, or (c) the subject matter is specifically covered in this section. Where the table in this appendix specifies individual requirement paragraphs rather than an entire AU-C section, the application and other explanatory material paragraphs related to such requirement paragraphs also do not apply. However, an auditor may apply these AU-C sections and paragraphs if the auditor believes doing so will provide appropriate audit evidence in the specific circumstances to support the auditor’s opinion on compliance.

<i>AU-C Section</i>	<i>Paragraphs Not Applicable to Compliance Audits</i>
210, <i>Terms of Engagement</i>	Paragraphs .06a and .08a
240, <i>Consideration of Fraud in a Financial Statement Audit</i>	Paragraphs .26 and .32b
250, <i>Consideration of Laws and Regulations in an Audit of Financial Statements</i>	All
315A, <i>Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement</i>	Paragraphs .19b, .20, .27a, .32–.38, .40, and .42d–.42e, .26–.30, and .33e
330, <i>Performing Audit Procedures in Response to Assessed Risks and Evaluating the Audit Evidence Obtained</i>	Paragraphs .13–.14 ¹⁵ , .18 ¹⁹ – .21 ²² , .26, and .31–.32
501, <i>Audit Evidence — Specific Considerations for Selected Items</i>	All except paragraph .27*
505, <i>External Confirmations</i>	All
510, <i>Opening Balances — Initial Audit Engagements, Including Reaudit Engagements</i>	Paragraphs .06, .08–.13, and .15–.17
540A, <i>Auditing Accounting Estimates and Related Disclosures</i>	All
550, <i>Related Parties</i>	All
560, <i>Subsequent Events and Subsequently Discovered Facts</i>	Paragraphs .09–.11 and .19–.20
570, <i>The Auditor’s Consideration of an Entity’s Ability to Continue as a Going Concern</i>	All

<i>AU-C Section</i>	<i>Paragraphs Not Applicable to Compliance Audits</i>
600, <i>Special Considerations — Audits of Group Financial Statements (Including the Work of Component Auditors)</i>	Paragraphs .26, .39, .41c, .41d, .55, and .56c
700, <i>Forming an Opinion and Reporting on Financial Statements</i>	Paragraphs .13–.17, .21–.44, and .45–.61
701, <i>Communicating Key Audit Matters in the Independent Auditor’s Report</i>	All
703, <i>Forming an Opinion and Reporting on Financial Statements of Employee Benefit Plans Subject to ERISA</i>	All
705, <i>Modifications to the Opinion in the Independent Auditor’s Report</i>	Paragraphs .18–.20
706, <i>Emphasis-of-Matter Paragraphs and Other-Matter Paragraphs in the Independent Auditor’s Report</i>	Paragraphs .06–.07
708, <i>Consistency of Financial Statements</i>	All
720B, <i>Other Information Included in Annual Reports</i>	All
725, <i>Supplementary Information in Relation to the Financial Statements as a Whole</i>	All
730, <i>Required Supplementary Information</i>	All
800, <i>Special Considerations — Audits of Financial Statements Prepared in Accordance With Special Purpose Frameworks</i>	All
805, <i>Special Considerations — Audits of Single Financial Statements and Specific Elements, Accounts, or Items of a Financial Statement</i>	All
806, <i>Reporting on Compliance With Aspects of Contractual Agreements or Regulatory Requirements in Connection With Audited Financial Statements</i>	All
810, <i>Engagements to Report on Summary Financial Statements</i>	All
910 , <i>Financial Statements Prepared in Accordance With a Financial Reporting Framework Generally Accepted in Another Country</i>	All
915 , <i>Reports on Application of Requirements of an Applicable Financial Reporting Framework</i>	All
920 , <i>Letters for Underwriters and Certain Other Requesting Parties</i>	All
925 , <i>Filings With the U.S. Securities and Exchange Commission Under the Securities Act of 1933</i>	All
930 , <i>Interim Financial Information</i>	All
940 , <i>An Audit of Internal Control Over Financial Reporting That Is Integrated With an Audit of Financial Statements</i>	All
945 , <i>Auditor Involvement With Exempt Offering Documents</i>	All
* SAS No. 142, <i>Audit Evidence</i> , amended section 501, <i>Audit Evidence — Specific Considerations for Selected Items</i> , to add paragraph .27 to section 501. That amendment is effective for audits of financial statements for periods ending on or after December 15, 2022. Consequently, the amendment relating to AU-C section 501 in this appendix becomes effective for compliance audits for fiscal periods ending on or after December 15, 2022, to align with the effective date of SAS No. 142. All other revisions to this appendix become effective for compliance audits for fiscal periods ending on or after December 15, 2023.	

Exhibit — Illustrative Combined Report on Compliance With Applicable Requirements and Internal Control Over Compliance — (*Unmodified Opinion on Compliance, No Material Weaknesses or Significant Deficiencies in Internal Control Over Compliance Identified*)

.A4446

[The amendment is contained in the second paragraph of the “Report on Internal Control Over Compliance” section of the illustrative independent auditor’s report.]

...

Independent Auditor’s Report

...

Report on Internal Control Over Compliance

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance on a timely basis. A *material weakness* in internal control over compliance is a deficiency, or combination of deficiencies in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. A *significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the section above and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies in internal control over compliance. Given these limitations, during our audit we did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above. However, material weaknesses or significant deficiencies in internal control over compliance may exist that ~~have were~~ not been identified.

Our audit was not designed for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, no such opinion is expressed.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing

based on the *[insert the name of the governmental audit requirement or program-specific audit guide]*. Accordingly, this report is not suitable for any other purpose.

[Signature of the auditor's firm]

[City and state where the auditor's report is issued]

[Date of the auditor's report]