

# Types of Financial Statements

When CPAs prepare or assist in preparing financial statements, they are required under professional standards to issue a report on those financial statements. This report can be one of three types:

- \* Audit report
- \* Review report
- \* Compilation report

The type of report is determined by mutual agreement between the client and the CPA. This determination usually depends on many factors, such as the needs of the client, needs of creditors or investors, the size and complexity of the business, and other factors. Securities laws require all publicly held enterprises to provide annual audited financial statements, while privately held companies often opt for reviewed or compiled statements. Or, credit agreements with lenders may require audited statements, even for private companies. In addition, audited financial statements are often beneficial in a business disposition or acquisition.

Regardless of the level of service performed by the CPA, the financial statements are the primary responsibility of the reporting entity.

We are experienced in performing audits, reviews, and compilations for entities of all kinds and sizes. This experience can be placed at your disposal.

## A Comparison

**Compiled Financial Statements** represent the most basic level of service CPAs provide with respect to financial statements. In a compilation, the CPA must comply with certain basic requirements of professional standards, such as having a knowledge of the client's industry and applicable accounting principles, having a clear understanding with the client as to the services to be provided, and reading the financial statements to determine whether there are any obvious departures from generally accepted accounting principles (or, in some cases, another comprehensive basis of accounting used by the entity). It may be necessary for the CPA to perform "other accounting services" - such as creating your general ledger, or assisting you with adjusting entries for your books - before the financial statements can be prepared. Upon completion, a report on the financial statements is issued that states a compilation was performed in accordance with AICPA professional standards, but no assurance is expressed that the statements are in conformity with generally accepted accounting principles. This is known as the expression of "no assurance." Compiled financial statements are often prepared for privately held entities that do not need a higher level of assurance expressed by the CPA.

**Reviewed Statements** require that the CPA perform inquiry and analytical procedures in addition to the procedures described above for a compilation. Upon completion, a report is issued stating that a review has been performed in accordance with AICPA professional standards, that a review is less in scope than an audit, and that the CPA did not become aware of any material modifications that should be made in order for the statements to be in conformity with generally accepted accounting principles, or if applicable, another comprehensive basis of accounting. This is known as the expression of "limited assurance." Reviewed financial statements are often prepared for entities that have bank loans, outside investors, or trade creditors, but those third parties do not require audited statements.

**Audited Financial Statements** are the product of a CPA's highest level of assurance services. In an audit, the CPA performs all of the steps indicated above regarding compiled or reviewed statements, but also performs verification and substantiation procedures. These verification and substantiation procedures may include direct correspondence with creditors or debtors to verify details of amounts owed, physical inspection of inventories or investment securities, inspection of minutes and contracts, and other similar steps. Also, the CPA gains a knowledge and understanding of the entity's system of internal control. When the audit is completed, the CPA's standard audit report states that an audit was performed in accordance with generally accepted auditing standards, and expresses an opinion that the financial statements present fairly the entity's financial position and results of operations. This is known as the expression of "positive assurance."

### **Audit vs. Review**

There are significant differences between the objectives of an audit of financial statements in accordance with generally accepted auditing standards and the objectives of a review in accordance with statements on standards for accounting and review services. The objective of an audit is to provide a reasonable basis for expressing an opinion regarding the financial statements taken as a whole. A review does not provide a basis for the expression of such an opinion because a review does not contemplate obtaining an understanding of the internal control structure or assess control risk, tests of accounting records and of responses to inquiries by obtaining corroborating evidential matter through inspection, observation or confirmation, and certain other procedures ordinarily performed during an audit. A review may bring to the accountant's attention significant matters affecting the financial statements, but it does not provide assurance that the accountant will become aware of all significant matters that would be disclosed in an audit.

Below is a comparison of procedures to be performed within each level of service:

Procedures To Be Performed:	AUDIT	REVIEW	COMPILATION
A. Obtain and document a general understanding of the industry, the entity's business & accounting principles & practices used	Yes	Yes	Yes
B. Obtain & document understanding of the entities internal controls	Yes	Yes	No
C. Apply analytical procedures & inquiries to accumulate evidence	Yes	Yes	No
D. Analytical procedures applied to financial statements by developing expectations & comparing to recorded amounts, or ratios developed	Yes	Yes	No
E. Identify risk & assess risks, develop responses & perform audit procedures in response to identified risks	Yes	No	No
F. Perform inventory observations & document trace test counts	Yes	No	No
G. Confirm account balances with third parties, ie. bank balances, accounts receivable, notes receivable, long-term debt balances	Yes	No	No
H. Perform detailed testing of account balances & transactions & additional substantive testing to source documents	Yes	No	No
I. Confirm with legal counsel regarding contingencies	Yes	No	No
J. Provide accountants report with entity's financial statements:			
1. Level of assurance	Full	Limited	None
2. Independence required	Yes	Yes	No
3. Footnote disclosures required	Yes	Yes	No
K. Consideration given to information arising after report date	Yes	Yes	Yes
L. Obtain representation letter from management	Yes	Yes	No
M. Provide management comment letter to entity describing material weakness, significant deficiencies & other matters considered during audit	Yes	No	No

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If you would like more information or would like to discuss your needs, [contact us](#) for a free consultation.