1991

Guide to the personal financial planning process and professional standards

American Association of Certified Public Accountants. Personal Financial Planning Division

Personal Financial Planning Division

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Guide to the Personal Financial Planning Process and Professional Standards

AICPA American Institute of Certified Public Accountants

NOTICE TO READERS

The purpose of this practice aid on the personal financial planning process is to define the process and describe its basic elements. It is designed to provide guidance on the responsibilities of CPAs who provide personal financial planning services. This practice aid also explains professional literature and standards that provide guidance for CPAs participating in the area of personal financial planning.

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We would like to acknowledge the work of the following subgroup members: D. Larry Fowler, Dirk L. Edwards, and Kevin F. Roach for preparing this practice aid.

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Guide to the Personal Financial Planning Process and Professional Standards

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IBSN 0-87051-095-9

PREFACE

The Personal Financial Planning Division has prepared the Personal Financial Planning Manual of nonauthoritative practice aids to assist certified public accountants in the efficient and competent delivery of personal financial planning services to their clients.

This practice aid is intended for practitioners who are developing comprehensive personal financial plans as well as those performing segmented planning and consultation engagements. This guide contains previously released material which was distributed as part of the January 1991 update to the PFP Manual.

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SCOPE OF THIS PRACTICE AID

This practice aid is composed of two parts. Part 1 provides information about the personal financial planning process by defining it and describing its basic elements. It is designed to provide guidance for CPAs who practice personal financial planning. Part 2 is an analysis of professional literature relevant to personal financial planning. It is intended to provide guidance on issues arising for CPAs engaged in personal financial planning. Part 2 refers to certain statements that change from time to time.

This practice aid considers only AICPA professional literature and standards. It does not address the federal or state registration requirements for investment advisers. The PFP Division's practice aid Issues Involving Registration Under the Investment Adviser's Act of 1940 provides information about the federal requirements. Whether a CPA is required to register depends on the facts and circumstances of each practice.

PART 1 - THE PERSONAL FINANCIAL PLANNING PROCESS

Part 1
The Personal Financial Planning Process

INTRODUCTION

This part of the practice aid is designed to define the personal financial planning process and to describe its basic elements. In accordance with that purpose, it describes the fundamental issues that CPAs confront most often and is designed to foster quality and consistency in the personal financial planning services provided by CPAs. It describes the objectives of each significant element of the personal financial planning process and explains the objectives by applying the concepts to particular practice situations. This is not intended to be a comprehensive discussion of the planning process.

This practice aid is applicable to segmented and comprehensive personal financial planning engagements and it describes the significant elements of the planning process. For practitioners who provide consultation services, some of the explanations in this practice aid may be helpful.

DEFINITIONS

Certain terms are defined as follows for the purposes of practice aids on personal financial planning.

Personal Financial Planning

Personal financial planning is the process of designing financial strategies and making planning decisions that are intended to implement short-term and long-term family and individual goals. CPAs can assist clients with this process by organizing data, performing analyses, providing suggestions and recommendations, assisting in decision making, and facilitating the implementation of planning decisions. CPAs can also help clients by monitoring their progress toward accomplishing their goals and by updating previous plans. Because financial planning is a process, the CPA may be involved in all or only some elements of this process. For instance, organizing data, performing analyses, providing suggestions or recommendations, and helping clients make decisions may constitute one engagement with a client, while facilitating the implementation of that same client's planning decisions may be dealt with in a separate engagement.

Comprehensive Planning Engagements

Comprehensive personal financial planning engagements address the client's overall financial situation and include, to the extent necessary, studying the client's financial position, projecting the client's cash flow, income tax planning, risk management, retirement planning, investment planning, goal planning, and estate planning. Comprehensive planning involves an analytical approach to these matters and recognizes their interrelationships, but it does not mean that every potential situation will be considered. The term *comprehensive* applies to the process but does not suggest that the CPA consider every possible alternative.

Segmented Planning Engagements

Segmented planning engagements involve analyses and recommendations that address one or more of the specific planning concerns of most importance to a particular client. The scope of a segmented planning engagement omits considerations of one or more planning areas included in a comprehensive planning engagement. A segmented planning engagement should involve qualifications to the recommendations because the effects of certain planning areas were not considered and analyses in certain planning areas were not performed. The extent of the limited-scope engagement is agreed upon by the CPA and the client. Both also should recognize that if the omitted analysis had been performed or other planning areas had been considered, different recommendations or decisions may have resulted.

Consultations

A personal financial planning consultation is an informal type of service that is based mostly on the CPA's knowledge about the client, the circumstances, the technical matters involved, and the mutual intent of the parties. Consultations generally involve written or oral advice or information given by a CPA in a short time frame. Information is usually received through discussion with the client. The CPA's responses and the understanding of the engagement are frequently communicated orally to the client. The CPA's response may be deemed to be adequate when existing personal knowledge is deemed to be adequate; otherwise it may be qualified, in which case limitations are stated. A qualified response often reflects cost, time, scope, and other limitations imposed by the client's specific circumstance. Consultations are usually provided along with other accounting services.

Ongoing Services

Consulting and segmented and comprehensive planning could result in ongoing services. Such ongoing relationships with the client may also involve other accounting services. Ongoing services may be delivered in a variety of ways; for example, updating financial statements, updating capital sufficiency analyses, preparing income tax projections, calculating estimated tax payments, reviewing existing insurance coverages, assessing changes in company benefits, and assessing estate planning needs resulting from changes in intentions, family circumstances, civil laws, tax laws, or level of wealth or income. Ongoing planning services may result in revisions to planning decisions when new information is available.

Engagement Objectives

Engagement objectives are an integral part of the engagement understanding with the client. They describe the CPA's preliminary understanding of the client's reasons for seeking personal financial planning services and the general nature of the recommendations or advice that the client expects to result from the planning process. Usually, engagement objectives reflect the client's interest in and concerns about the ability of individual and family goals.

Estimates

Estimates are approximate values that result from projections or other analyses. Estimates substitute for precise values where precision would not add material value to the planning process.

Assumptions

Assumptions are the most important determinant of forward-looking information. They represent conditions or events that are expected to exist and a course of action the responsible party expects to take. Assumptions used may be particularly sensitive, significant, or hypothetical. Assumptions have the same meaning as in the AICPA Guide for Prospective Financial Statements.

Hypothetical Assumptions. Hypothetical assumptions are used in financial projections to present conditions or courses of action that are not necessarily expected to occur but that are consistent with the purpose of the projection. Hypothetical assumptions have the same meaning as in the Guide for Prospective Financial Statements.

THE PERSONAL FINANCIAL PLANNING PROCESS

The client's goals and the scope of the engagement determine the CPA's role in the personal financial planning process. It is not necessary to cover every planning area in every engagement. Having an adequate understanding of the client's goals, financial resources, and attitudes allows the CPA to be an effective financial adviser.

Effective personal financial planning services should be flexible, allowing the CPA and the client to vary the methods used and the sequence of the planning process. The process includes such functions as defining engagement objectives, engagement planning, documenting the process, performing analyses, developing recommendations and assisting the client to make planning decisions, reporting recommendations and advice, helping the client effect financial planning decisions, monitoring the client's planning progress, and helping the client revise planning decisions.

This practice aid applies to segmented and comprehensive planning engagements, and elements of it may apply to consultations. The following guidance presents the CPA's objectives in carrying out each of these functions. Explanations that follow the objectives are designed to illustrate how these functions may be performed.

Defining Engagement Objectives

The personal financial planning process includes the development of objectives for the work to be performed in a specific engagement, the selection of an appropriate scope of services, and the comprehension of the client's individual and family goals. This element of the process enables the CPA to--

- Reach an understanding of whether the client can benefit from personal financial planning services and, if so, to determine with the client which level of service-- consultation, segmented planning, or comprehensive planning -- is appropriate to meet the client's needs.
- Reach an understanding with the client concerning the engagement objectives. The CPA may identify issues not originally considered by the client that require special attention and need to be brought into the process.
- Obtain a sufficient understanding of the client's individual and family goals and resources so that the CPA can satisfy the engagement objectives, properly plan the engagement, facilitate the analyses that will be used in developing recommendations, and help the client make decisions.
- Assist the client in prioritizing individual and family goals.

Explanations. A process of prescreening clients helps the CPA determine whether the client has a planning need and sufficient resources to benefit from the planning process. Such prescreening would also include a discussion of the expected cost of planning services and the anticipated benefits. Information gathered to evaluate client acceptance for an engagement might be more limited than the data necessary to perform the analysis. The amount of prescreening inquiries made or information gathered depends on the CPA's familiarity with the client's circumstances. The CPA, by making the appropriate inquiries, would attempt to develop an understanding of the client's needs, expectations, and desires. This may include understanding the client's family data, commitment to the planning process, amount of current cash flow and assets that are available to implement financial planning decisions, personal preferences, and relationships with other professionals.

It is important that the client understand the responsibilities of all interested parties, including the client, the CPA, and the client's other advisers. In addition, the client's involvement and cooperation in providing necessary data is essential to the success of an engagement. It is also important for the CPA and the client to reach an understanding of the financial planning issues to be considered, their relative priorities, and the significant planning assumptions to be made.

The scope of the personal financial planning engagement may vary. Segmented planning engagements may be limited to reviewing and analyzing one or more aspects of the client's financial goals, whereas comprehensive engagements should involve analysis of all of the client's significant financial goals.

The client should develop reasonable expectations for the planning engagement. These expectations influence the engagement objectives.

It is important that the CPA establish an understanding with the client regarding the services that are to be performed. The CPA can exercise professional judgment in determining the degree to which this understanding is documented. Typical documentation would be in the form of an engagement letter or in the form of file memos that document oral understandings.

This documentation may include a description of (1) the engagement objectives; (2) the level of services to be provided; (3) the roles and responsibilities of the CPA, the client, and other advisers in the personal financial planning process; (4) the fee arrangements; (5) the limitations and other constraints; and (6) whether the services are to be ongoing or of a limited term.

It is important for the CPA to help the client articulate and quantify individual and family goals. Goals have to be quantifiable. Helping the client to articulate his or her concerns and develop clear goals helps the CPA provide services tailored to meet the client's specific needs.

Professional judgment should be exercised to determine what information is relevant to an engagement. Necessary information includes an understanding of financial and nonfinancial aspects of the client's life such as the client's attitudes, risk tolerance, and financial situation. This knowledge of the client can be obtained through a long-term relationship with the client, through information gathering, or both.

During the planning process it is likely that the client's objectives and goals will become clearer to both the client and the CPA. Regular communication between the CPA and the client is helpful to enhance the CPA's understanding of the client. The engagement may need to be modified as this understanding grows. During the engagement, the CPA should evaluate whether the engagement objectives, as originally determined, continue to be appropriate.

The CPA may also encourage the client to redefine and reprioritize goals or objectives that have been identified.

Engagement Planning

The personal financial planning process includes the selection of specific procedures relevant to the personal financial planning engagement. This element of the process enables the CPA to--

- Develop procedures that provide a sufficient basis for the CPA's professional recommendations and assistance in helping the client make planning decisions.
- Focus on analyses and procedures that are intended to provide useful information for the planning process.

Explanations. The engagement's objectives and the CPA's understanding of the client form the basis for determining those procedures that are needed to develop recommendations and to help the client make planning decisions. CPAs select procedures that are appropriate for the individual client's circumstances. Procedures performed often reflect materiality and cost/benefit considerations.

The CPA meets with the client to understand the type, scope, and special concerns of the client. In planning the engagement, the CPA may coordinate with the client's attorney or other specialists who may be necessary for the engagement.

CPAs usually create a time budget to determine manpower and schedule requirements. The following factors are considered: engagement's size and complexity; personnel available; special expertise required; and qualification, experience, and training of personnel to be assigned.

Performing Analyses to Develop and Support Recommendations and Planning Decisions

Analyses of alternative strategies or data for achieving the client's goals are necessary to develop and support the recommendations and to assist the client in making each of the planning decisions. This element of the process enables the CPA to--

- Develop recommendations and assist the client in making planning decisions.
- Provide adequate support for the recommendations that are developed.

Explanations. In preparing analyses of the client's current financial situation and to help the client achieve stated objectives, the CPA may use estimates furnished by the client or the client's advisers, or the CPA may develop estimates. Estimates, by their nature, may not be precise. The level of precision can depend on such factors as the priority of a goal to which the analysis relates, the time frame in which the goal is to be achieved, or the sensitivity of the analysis to other variables. For example, in some cases it may be appropriate to use a flat tax rate in the analysis.

It is possible in a personal financial planning engagement to rely on estimates to provide an economically useful service within a reasonable time at a reasonable cost.

The CPA may either work with the client in developing assumptions or develop assumptions for the client's approval based on the CPA's understanding of the client and other factors. Hypothetical assumptions are generally useful when considering various alternatives for which expected courses of action are not completely defined. CPAs should communicate the assumptions used and ascertain that the client concurs with all significant assumptions.

The analyses frequently center around projections of cash flow and net worth and may include--

- Attempting to define the client's financial goals in measurable terms.
- Comparing the financial effects of different financial strategies.
- Projecting tax liabilities.
- Evaluating the present investment portfolio in terms of diversification, liquidity, risk, and yield.
- Evaluating casualty or disability insurance coverage requirements.
- Projecting liquidity requirements.
- Projecting income requirements during retirement.
- Projecting education costs.
- Calculating the client's current and projected financial positions.
- Projecting life insurance coverage requirements based on current expenditure patterns and dependent's financial needs.
- Projecting estate taxes.

Multiple-year projections may be appropriate for many of these analyses.

In the process of performing analyses it may be determined that the client's goals cannot be achieved. This may lead to a reassessment of the goals or related assumptions.

The CPA will identify action steps that can be taken by the client to help achieve his or her goals. These action steps are related to recommendations, which may be translated into action items. Recommendations also may include estimates of amounts that need to be saved, projections of amounts the client is capable of saving, and the need for the client to develop an investment strategy with a qualified investment adviser. For example, an analysis of retirement may lead to recommendations about starting a regular savings program and following a disciplined investment plan.

Documenting the Planning Process

Documentation is important in every phase of the planning process to demonstrate how the engagement was performed and how the CPA arrived at his or her recommendations and advice. This element of the process enables the CPA to develop workpapers that document the engagement objectives, the CPA's understanding of the client, and the basis of the CPA's recommendations and advice. Documentation does the following:

- Shows a systematic approach to the engagement
- Provides a record of a CPA's understanding of the client and the engagement
- Demonstrates due professional care
- Supports conclusions
- Provides a source for future reference

Explanations. Documentation of the CPA's understanding of the client may include one or more of the following:

- A signed engagement letter or file memo that sets forth the oral understanding with the client
- A completed data-gathering questionnaire
- A description of the client's goals
- Evidence of a review of client documents
- Copies of significant client documents such as wills and employee benefit statements

Documentation of the engagement

planning may include workpapers in addition to work program.

Documentation of the analyses performed may be composed of workpapers relating to analyses of earned income and expenses, net worth, tax position, and financial requirements and sources of income during retirement.

Documentation of recommendations, advice, and planning decisions may include a written communication that relates the analysis performed to the conclusions reached.

File memos also help to summarize significant client discussions and meetings regarding substantive issues and, in particular, differing views on planning decisions and on the implementation of decisions.

Reporting of Recommendations and Advice

The personal financial planning process includes the communication of recommendations and advice to the client. This element of the process enables the CPA to communicate recommendations and advice to the client in a way that clarifies both the anticipated effect and the limitations of the recommendations and advice.

Explanations. It is often helpful to discuss alternative strategies with a client so the client can evaluate the appropriateness of the recommendations. Alternative strategies are frequently an important factor that the client considers in making planning decisions.

To assist the client in making planning decisions, the CPA communicates significant information pertinent to his or her recommendations including applicable limitations and references to alternative recommendations that were considered by the CPA. For example, pertinent information may include information about cash flow that influenced the CPA's recommendations about saving for retirement. Limitations are often expressed in precautionary statements, such as the following:

- "The income and estate tax-planning recommendations are based on tax laws and regulations that are subject to change."
- "The advice contained in this report is based on your present financial condition, and the appropriateness of that advice may change as your personal and financial circumstances change or as the economic environment changes."

Professional judgment is used to determine whether recommendations and strategies can serve the client's needs. Recommendations may be communicated orally or in writing; however, all substantive communication usually should be documented in writing. Furthermore, it is usually advisable to follow up oral communication with a written communication to the client.

A written communication to the client may include a summary of the client's goals, a description of the CPA's work performed, and the scope of the engagement including qualifications on the recommendations, a clarification of the level of responsibility taken by the CPA for recommendations or advice, and a summary of actions suggested to implement planning decisions. The summary of actions suggested to implement planning decisions is often referred to as the action plan.

The remainder of part 1 presents elements of the process often provided as ongoing services.

Helping the Client Implement Financial Planning Decisions

If the client agrees that implementation is a part of the engagement, the CPA's role includes helping the client implement planning decisions as necessary. This element of the process enables the CPA to help the client take action to carry out the planning decisions.

Explanations. The CPA may be engaged to help the client implement the financial planning decisions. This agreement with the client should be documented in an engagement letter. This may be part of an initial financial planning engagement or it may constitute an additional engagement.

The CPA's role in implementation will vary depending on the engagement. The CPA may develop an action plan that includes a timetable, direct the process of carrying out the planning decisions, or actually perform some tasks that are included in the action plan, such as preparing tax returns.

This part of the process frequently involves other advisers. When other advisers are involved, the CPA may--

- Recommend the use of other specific advisers.
- Help a client identify competent advisers.
- Cooperate with and provide information to other advisers.
- Coordinate other advisers' participation in this process.

Often the presentation of recommended action plans to the client concludes the initial engagement and its fee arrangement.

Monitoring the Client's Progress in Achieving Goals

Monitoring helps to determine whether progress has been made with respect to achievement of the client's goals. The client may engage the CPA to perform certain monitoring services. Monitoring the client's progress toward achieving his or her goals and revising planning decisions are normally separate engagements that are undertaken by a separate specific agreement with the client. Thus, monitoring the process and revising planning decisions may be considered an additional service engagement, subject to another engagement letter, rather than part of the initial personal financial planning engagement. This element of the process enables the CPA to monitor a client's progress to determine whether the action steps have been completed and whether progress is being made with respect to the client's goals.

Explanations. Someone other than the CPA may be engaged to monitor the progress. The CPA may be engaged to review the client's progress or to determine if the recommendations are still appropriate to enable the client to meet his or her goals. This process may lead the client to revisions in planning decisions and identification of new financial planning needs that should be addressed. If the CPA is expected to communicate with the client when subsequent developments affect advice and recommendations previously provided, that expectation should be stated in the engagement understanding and documented in the engagement letter.

Updating Recommendations and Helping the Client Revise Planning Decisions

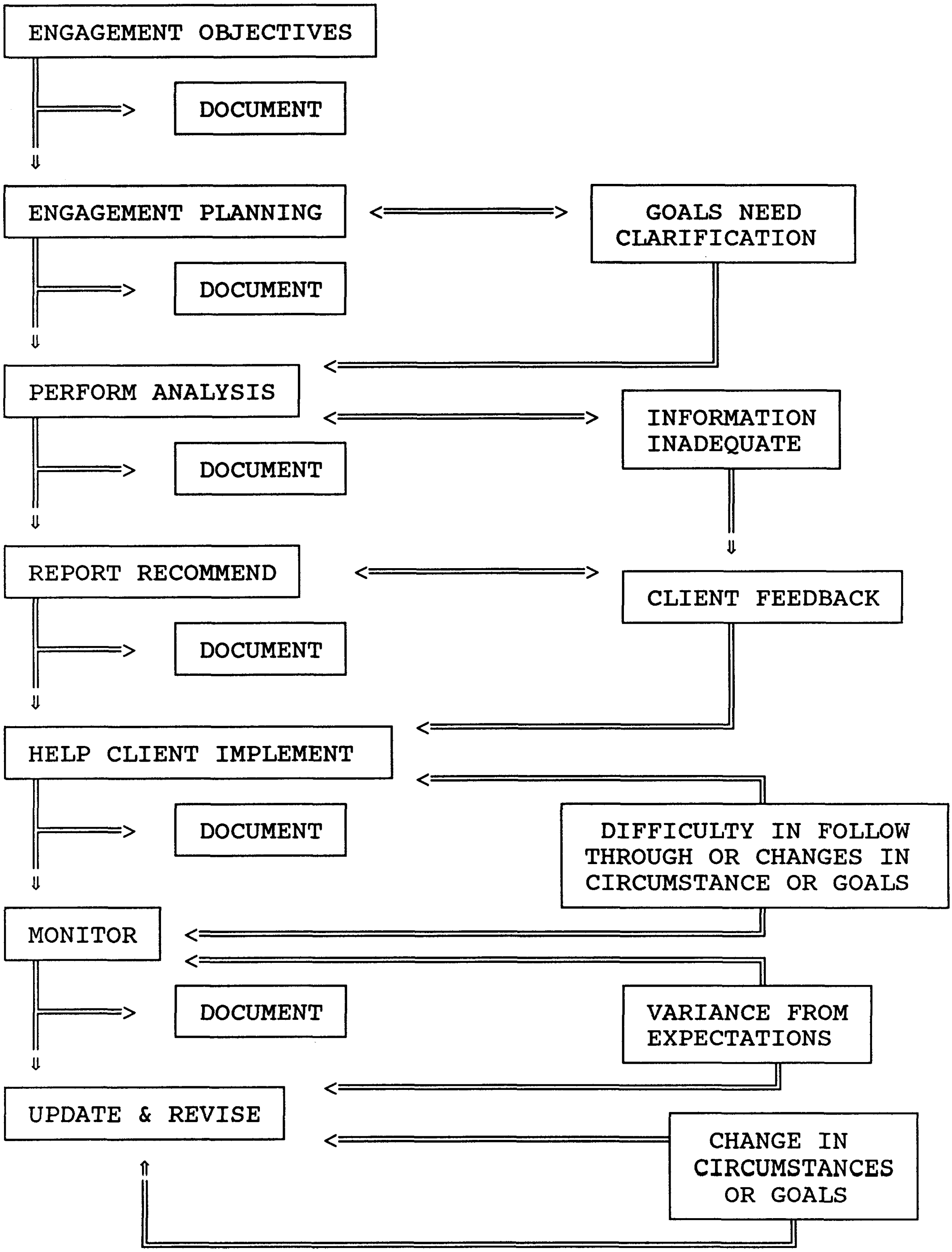
If it is agreed with the client that updating the recommendations is part of the engagement, the CPA's role may include helping the client revise planning decisions. This enables the CPA to update the client's financial planning decisions when circumstances change or when progress toward the goals differs from the projections.

Explanations. A CPA cannot be expected to update the recommendations and communicate with the client unless the CPA undertakes this obligation by specific agreement with the client.

During update meetings, the planning strategies may be modified. Updates may be scheduled with the client on a regular basis, depending on needs. Some areas are particularly critical for certain clients and may require frequent updates.

THE PROCESS -- A FLOWCHART

This flowchart is designed to assist CPAs in identifying the flow of the personal financial planning process.



PFP Process: QUESTIONS AND ANSWERS

What is PFP?

PFP is the process of designing financial strategies and making financial decisions that are intended to implement short-term and long-term family and individual goals.

What are the forms of delivery of PFP services?

There are three general forms of PFP services that CPAs provide: consultation, segmented planning engagements, and comprehensive financial planning engagements. Different services are provided based on different client circumstances.

Is there a prescribed process?

Yes. Broad guidance is provided in this practice aid. The process involves a series of actions or operations that include obtaining an understanding of the client, performing analyses, and developing recommendations that help the client make decisions. These actions are intended to help the client make progress in achieving his or her goals. The result of the process is client action leading toward goal achievement.

Is it necessary to begin financial planning by defining engagement objectives?

Yes. Engagement objectives describe the CPA's preliminary understanding of the client's reasons for seeking personal financial planning services and the general types of advice that the client expects from the CPA's services.

What information about the client should be obtained?

The information that is gathered depends on many factors, including the client's concerns and specific needs. Professional judgment is used to determine necessary information for each engagement, such as detailed descriptions of the financial and nonfinancial aspects of the client's life and consideration of the client's attitudes, risk tolerance, and financial situation.

What is the difference between engagement objectives and client objectives?

The difference is best explained by an example. A client's objective might be: "I want to be able to find the costs of sending my children to college." An engagement's objective can be: "I want you to help me make a decision (or give me advice) about providing funding for my children's college education."

What factors are considered in planning a PFP engagement?

The selection of procedures relates to areas where recommendations will be made in response to the client's goals. Coordination with the client's other advisers may be necessary. Factors that influence planning include the engagement's size and complexity, personnel available, special expertise required, and the experience of personnel to be assigned.

What analyses are necessary in a PFP engagement?

The analyses performed depend on the client's objectives. The level of an analysis should be focused and sufficient to support the recommendations. For example, an analysis of retirement planning needs may lead to recommendations about developing a saving strategy. Analysis supports the recommendations that are intended to assist the client in taking action to achieve his or her goals.

How much precision should be used in the analyses?

The level of precision can depend on the priority of goals to which the analyses relate, the time frame in which the goals are to be achieved, or the sensitivity of the analyses to other variables.

Is there a reporting responsibility for projections included in the personal financial plan?

If the projection is restricted to internal use and the client has not requested that a report be prepared, the accountant need not report; however, a caveat that the prospective results may not be achieved and a statement that the projection is for internal use only should be communicated in writing. (See SOP 90-1, paragraph 9.)

Are there any authoritative guidelines on preparing projections?

Yes. The AICPA Guide for Prospective Financial Statements contains a section that covers the preparation guidelines. See section 300 of the *Guide* for guidance.

Do analyses generate recommendations?

The analyses used in a financial planning engagement should be appropriate to generate the recommendations and advice given to the client. The analyses should provide a means to demonstrate the appropriateness of the recommendations and should provide adequate documentation of the process used to develop them.

Is reporting of recommendations a required part of personal financial planning engagement?

The end result of financial planning is client action and achievement of goals. To have action and changes in patterns that are necessary to achieve goals, a written record of recommendations and advice is important in helping the client make planning decisions.

Why is the PFP process documented?

Documentation demonstrates how the process was performed and how the recommendations and advice were developed. AICPA Code of Professional Conduct ET rule 201 indicates that members should have a reasonable basis for conclusions or recommendations in relation to professional services.

What documentation should be provided?

There should be documentation of the engagement objectives, the CPA's understanding of the client, and the CPA's analysis and recommendations. Written communication to the client for reporting the recommendations and advice should be developed. If the CPA is expected to monitor the client's progress in achieving the plan, that understanding should be stated in the engagement understanding.

What is communicated to the client when providing recommendations and advice?

A written summary may comprise a description of the client's goals, the work performed, and the scope of the engagement, including qualifications to the recommendations and a summary of the suggested actions.

What are the reporting standards that are considered when a financial plan is developed?

Reporting standards to consider include the following:

- Statements on Standards for Management Advisory Services
- Statements on Standards for Accounting and Review Services
- Statements on Responsibilities in Tax Practice
- Guide for Prospective Financial Statements
- Statement on Standards for Attestation Engagements

What is the CPA's role in effecting financial planning decisions?

The CPA may help the client to take action to carry out the planning decisions.

How does the CPA interrelate with other advisers?

The CPA may recommend the use of other advisers, identify advisers, provide information to other advisers, and coordinate other advisers' participation in this process.

What is the CPA's role in monitoring the client's progress in achieving financial goals?

The CPA may follow up to determine if action has been taken and if progress is being made with respect to the client's goals.

What is the CPA's role in revising financial planning decisions?

The CPA may update the financial planning decisions when circumstances change or progress toward the goals is different from the projections.

PART 2 -- RELEVANT PROFESSIONAL LITERATURE

Part 2
Relevant Professional Literature

INTRODUCTION

The following section of this practice aid describes professional literature that provides guidance for personal financial planning engagements. It is designed for use as educational and reference material for members of the Institute and others interested in the subject. It is not intended to establish standards. Like other practice aids issued by the PFP Executive Committee, it is nonbinding under rule 202 of the AICPA Code of Professional Conduct.

Readers should consult the AICPA professional standards when performing personal financial planning services. The following professional rules, standards, guides, and statements on responsibility have particular relevance for the performance of personal financial planning services.

- Code of Professional Conduct
- Statements on Standards for Management Advisory Services (SSMASs)
- Statements on Standards for Accounting and Review Services (SSARSs)
- Statements on Standards for Attestation Engagements (SSAEs)
- Statement on Standards for Accountants' Services on Prospective Financial Information, Financial Forecasts and Projections
- Statements on Responsibilities in Tax Practice (SRTPs)
- Guide for Prospective Financial Statements
- Personal Financial Statements
- Statement of Position 82-1, *Accounting and Financial Reporting for Personal Financial Statements*
- Statement of Position 90-1, *Accountants' Services on Prospective Financial Statements for Internal Use Only and Partial Presentations*

This practice aid summarizes some of the guidance involved in those documents. It is not intended to be a comprehensive discussion or to establish preferred practices.

ETHICS: RULES OF PROFESSIONAL CONDUCT

General Standards

The general standards are described in rule 201 in the Code of Professional Conduct and apply to all members of the AICPA as a normal part of their professional services.

Professional Competence. A member provides only those professional services that the member or the member's firm can reasonably expect to complete with professional competence (interpretation under Code of Professional Conduct rule 201 [AICPA, Professional Standards, Vol. 2, ET sec. 201.02]).

Due Professional Care. Members exercise due professional care when performing professional services. In particular, certain minimum standards are necessary in each engagement; for example, checking to be sure that advice given is consistent with current law and regulation.

Planning and Supervision. Members adequately plan and supervise the performance of professional services. Proper planning enhances the productivity of the engagement personnel. Two commonly used planning documents are the planning memo and the planning checklist. The steps in planning the engagements may include selection of the procedures tailored to the individual circumstances, which will serve a basis for developing recommendations and making planning decisions.

Sufficient Relevant Data. In the context of a planning engagement, sufficient relevant data required to complete the engagement varies depending on the scope of the engagement. Code of Professional Conduct rule 201 (AICPA, Professional Standards, Vol. 2, ET section 201.01) states that a member shall "obtain sufficient relevant data to afford a reasonable basis for conclusions or recommendations in relation to any professional services." Professional judgment is required to determine what information is relevant to a personal financial planning engagement. This is particularly important in financial planning engagements because of the interrelationship of the technical topical areas.

Compliance With Standards

Code of Professional Conduct rule 202 (AICPA, Professional Standards, Vol.2, ET section 202) states that members are required to comply with standards for conducting professional services when standards are promulgated by bodies designated by AICPA Council.

MANAGEMENT ADVISORY SERVICES

The Management Advisory Services (MAS) Executive Committee has issued Statements on Standards for Management Advisory Services. These statements provide guidance to enable members to comply with ethics rule 201 within the context of management advisory services. The SSMASs are broad general standards for all advisory services except tax advisory services. A Personal Financial Planning engagement is a form of management advisory service as defined in SSMAS No. 1, Definitions and Standards for MAS Practice (AICPA, Professional Standards, Vol. 2, MS sec. 11.04). The management consulting function is described in MS section 11.04 as "providing advice and technical assistance where the primary purpose is to help the client improve the use of its capabilities and resources to achieve its objectives."

Presently, the SSMASs are the umbrella standards for all Personal Financial Planning services. The guidance in the MAS standards is binding on practitioners providing PFP services.

Levels of Service

Two levels of service have been identified: Engagement and Consultation.

Engagement. SSMAS No. 1 defines an MAS engagement as--

> That form of MAS in which an analytical approach and process is applied in a study or project. It typically involves more than an incidental effort devoted to some combination of activities relating to determination of client objectives, fact finding, opportunity or problem definition, evaluation of alternatives, formulation of proposed action, communication of results, implementation, and follow-up. (AICPA, Professional Standards, Vol. 2 MS section 11.04)

This definition applies to services provided to an individual as well as to a business enterprise. Personal financial planning services that are segmented or comprehensive engagements would meet the definition of an MAS engagement, not the definition of an MAS consultation. For personal financial planning services that are segmented or comprehensive engagements, it is important to review the information in SSMAS No. 2, MAS Engagements (AICPA, Professional Standards, Vol. 2, MS section 21).

Consultation. For personal financial planning consultations, practitioners should refer to the guidance in SSMAS No. 3, MAS Consultations. The nature of an MAS consultation is as follows:

> Generally [the consultation] is based on the practitioner's existing personal knowledge on technical matters in question and those aspects of the client's financial, business, and, perhaps, personal affairs to which the inquiry applies. Depending on the inquiry, the practitioner's response may be immediate or may be made after reference to client file information and technical source materials, discussions with colleagues, or consideration of the advantages, disadvantages, and financial consequences of available alternatives. (AICPA, Professional Standards, Vol. 2, MS section 31.04)

Because segmented and comprehensive personal financial planning engagements involve more than existing personal knowledge and more time than a limited meeting, these services do not meet the definition of an MAS consultation.

In regard to personal financial planning consultations, a CPA is required to ensure that appropriate professional judgments are made in accordance with the SSMAS No. 3.

Documentation

MS section 21.18 states that "practitioners should exercise professional judgment in determining the nature and extent of the documentation appropriate in the circumstances." It also mentions that a documented understanding with the client may be in the form of an accepted proposal letter, a confirmation, an engagement arrangement letter, a contract, or a file memorandum documenting an oral understanding.

Understanding With the Client

SSMAS No. 2, MAS Engagements (AICPA, Professional Standards, Vol. 2 MS section 21.17) provides additional guidance by stating that the practitioner should consider the following matters in reaching an appropriate understanding with the client in an MAS engagement:

- Engagement objectives
- Nature of the services to be performed
- Engagement scope, including areas of client operations to be addressed and limitations or constraints, if any
- Respective roles, responsibilities, and relationships of the practitioner, the client, and other parties to the engagement
- The anticipated engagement approach, including major tasks and activities to be performed and, if appropriate, methods to be used
- The manner in which engagement status and results are to be communicated
- Work schedule
- Fee arrangement

Sufficient Relevant Matter

SSMAS No. 2, MAS Engagements (AICPA, Professional Standards, Vol. 2 MS section 21.13) adds that sufficient relevant data may be obtained by "interview, observation, review of client documents, research, computation, and analysis." It further says that sufficient relevant data "normally consists of information needed to analyze the courses of action that might be considered and to support conclusions and recommendations."

Gathering Information

SSMAS No. 2, MAS Engagements (AICPA, Professional Standards, Vol. 2 MS section 21.14) recognizes that practitioners should exercise professional judgment in determining the nature and quantity of information required to develop conclusions and recommendations that fulfill the objectives of the engagement. It further states that "the objectives, nature, and scope of the engagement, the costs of the data gathering versus the benefits of the added data, the intended use of the engagement results, and the related circumstances" are considered when determining the data and the information required.

Developing Recommendations

SSMAS No. 2 states that "the source, reliability, and completeness of the data, and any limitations thereof, should be considered in forming and reviewing conclusions and recommendations." (AICPA, Professional Standards, Vol.2, MS section 21.14)

For personal financial planning consultations it should be noted that SSMAS No. 3, MAS Consultations (AICPA, Professional Standards, Vol. 2 MS section 31.09) discusses that the client should be informed that the advice is dependent on the accuracy and completeness of the unverified client information when a practitioner is furnished by a client with information that is not verified, corroborated, or reviewed by the practitioner. SSMAS No. 3, MAS Consultations (AICPA, Professional Standards, Vol. 2 MS section 31.10) further states that "if the practitioner does not obtain sufficient relevant information [that is relevant to the matter at issue and sufficient to provide a basis for a definitive response to the client] the practitioner should consider whether a qualified response can be given or whether a response cannot be given without further study and analysis." This implies that the information must support the conclusions.

Client Benefit and Communicating Recommendations

SSMAS No. 3, MAS Consultations (AICPA, Professional Standards, Vol. 2 MS section 11.06) requires that the CPA review engagement recommendations objectively and advise the client of limitations, qualifications, or reservations that the client should consider when making decisions based on the recommendations. This is equally applicable to the recommendations that the CPA includes in personal financial plans.

SSMAS No. 3, MAS Consultations (AICPA, Professional Standards, Vol. 2 MS section 21.16) states that "an MAS engagement should be structured to enable [the client] to make decisions on matters requiring action by providing for review and approval of the engagement findings, conclusions, recommendations, and other results. The implementation of any course of action recommended during the MAS engagement must be authorized by management."

ATTEST SERVICES

The focus of an attest service is to provide assurance on the reliability of a written assertion of another party, thus adding credibility to the written assertion. The focus of a personal financial planning service is to provide advice or recommendations to a client. An attest service may be either required or desired. It may be performed instead of, or as part of, a personal financial planning engagement. A requirement to perform an attest service can result when there is a need to provide an appropriate level of assurance on a specific written assertion, whether it is a client's or another party's assertion.

When the CPA's personal financial planning work involves a personal financial statement or a prospective financial statement in accordance with the Statements on Standards for Accounting and Review Services (SSARSs) and the Statements on Standards for Accounting Services on Prospective Financial Information, the CPA is providing an attest service. The Statements on Standards for Attestation Engagements (SSAE) (AICPA Professional Standards, Vol. 1 AT section 100), issued by the Auditing Standards Board and the Accounting and Review Services Committee, establishes a broad framework for a variety of attest services. The attestation standards also apply to reports on investment performance statistics.

The Statements on Standards for Attestation Engagements (AICPA, Professional Standards, Vol. 1 AT Section 100) defines an "attest engagement as one in which a practitioner is engaged to issue or does issue a written communication that expresses a conclusion about the reliability of a written assertion that is a responsibility of another party." In general, personal financial planning services do not meet the definition of an attest service because a CPA is usually not engaged to express and does not issue a written communication that expresses a conclusion with respect to the reliability of a written assertion that is the responsibility of another party. When a CPA issues a financial statement or a prospective financial statement as part of a personal financial planning engagement, a CPA is performing both an attest and a personal financial planning service.

WRITTEN PERSONAL FINANCIAL PLANS

Written financial plans may include personal financial statements, supplementary schedules of personal financial information, and prospective financial information, such as projected income and cash flow. If a written plan includes personal financial statements, the CPA should comply with the requirements of either SSARS 1, Compilation and Review of Financial Statements, or SSARS 6, Reporting on Personal Financial Statements Included in Written Personal Financial Plans, depending on the nature of the engagement. If a written plan includes prospective financial information, the CPA should comply with the requirements of the AICPA's Statement on Standards for Accountants' Services on Prospective Financial Information, Financial Forecasts and Projections, and the Guide for Prospective Financial Statements. The determination of which of those documents applies depends, in part, on whether the financial information will be used only to develop the client's personal financial plan or whether third parties also will use the information.

PROSPECTIVE FINANCIAL INFORMATION

Guide for Prospective Financial Statements

The AICPA's Guide for Prospective Financial Statements provides information and guidance that is useful and relevant to providing personal financial planning services. It serves as a basis for applying professional standards to engagements involving prospective financial information. The Guide for Prospective Financial Statements provides guidelines for the preparation and presentation of financial forecasts and projections and for accountant's reports thereon. In addition, before the Guide was issued, the AICPA issued an authoritative statement entitled Financial Forecasts and Projections, which is included in the Guide for Prospective Financial Statements. The CPA who complies with the Guide for Prospective Financial Statements will also be in compliance with Financial Forecasts and Projections. This section also derives guidance from Statement of Position (SOP) 90-1, Accountants' Services on Prospective Financial Statements for Internal Use Only and Partial Presentations, which provides guidance on reporting and preparation procedures. SOP 90-1 replaces sections 900 and 1000 of the Guide for Prospective Financial Statements.

The Guide for Prospective Financial Statements discusses three levels of service that can be performed for prospective financial information for general use, limited use, and internal use. The types of services are compilations, examinations, and applications of agreed-upon procedures. In personal financial planning engagements, the client may be the only user of the prospective financial information, and it may be prepared for internal use. The Guide for Prospective Financial Statements indicates that "Plain Paper" services (no report necessary) are appropriate for internal use only engagements. When a CPA includes a financial projection in a financial planning report or other written communication (for example, with a transmittal letter), a caveat that the prospective results may not be achieved and a statement that the financial projection is for internal use only should be communicated in writing.

Types of Prospective Financial Information

Prospective financial information in personal financial plans should meet standards and disclosure requirements. The requirements provide that when an accountant provides a financial plan to a client that includes prospective financial information, the accountant cannot report on the certainty of the outcome of the future events. To the extent that the CPA is associated with the prospective financial information, the report accompanying it must discuss the degree of association. Prospective financial information is extremely useful in formulating personal financial plans.

Prospective financial statements are based on assumptions regarding future events, whose assumptions are based on available information and judgment which is based on history and plans. Financial information about the future may be presented as complete financial statements or limited to one or more elements or items.

Forecasts. A financial forecast is rarely used in a personal financial planning environment. For information about forecasts see the Guide for Prospective Financial Statements.

Projections. A financial projection is a prospective financial statement that presents, to the best of the responsible party's knowledge and belief and given one or more hypothetical assumptions, an entity's expected financial position, results of operation, and changes in financial position. It is sometimes prepared to present one or more hypothetical courses of action for evaluation, as in response to "What would happen if"? A projection, like a forecast, may contain a range.

Projections can be based on many assumptions. A forecast, however, should be based on the assumptions and rationale that are most likely to be valid. Minimum presentation guidelines are presented in section 400.06 of the Guide for Prospective Financial Statements. See appendix E for the minimum presentation requirements.

Partial Presentations. An accountant may be engaged to perform services on partial presentations. SOP 90-1, part 2, describes how the guidance in the Guide for Prospective Financial Statements applies to partial presentations and discusses the accountant's responsibility for partial presentations when he or she is engaged to issue or does issue a written communication that expresses a conclusion about the reliability of a written partial presentation. A partial presentation excludes one or more of the items required for prospective statements as described in section 400.06 of the Guide. A projection of expected retirement expenses is an example of a partial presentation. See appendix E for the minimum presentation requirements of prospective financial statements. Appendix F contains selected information related to partial presentations.

Partial presentations are not ordinarily appropriate for general use. Accordingly, a partial presentation should not be distributed to third parties who will not be negotiating directly with the client. Negotiating directly is defined as the third-party user's ability to ask questions of and negotiate the terms or structure of the transaction directly with the client. Partial presentations are appropriate for personal financial plans because personal financial planning engagements are generally limited-use situations.

Accountant's Involvement With Partial Presentations. An accountant may be engaged to prepare a financial analysis of a potential investment transaction where the engagement includes obtaining the information, making appropriate assumptions, and assembling the presentation. In such circumstances, the analysis would not be appropriate for general use and should not be characterized as forecasted or projected information. This analysis may be deemed as a partial presentation only if the client adopts the assumptions. Otherwise, the CPA is the asserter and probably should consider the MAS standards.

Types of Prospective Financial Statements Prepared. Educational funding and retirement planning computations are two types of prospective financial statements that are prepared for many personal financial planning clients. When discussing retirement planning with a client, most CPAs would prepare a projection because many different hypothetical assumptions might be considered. A hypothetical assumption is defined as an assumption used in a financial projection to present a condition or course of action that is not necessarily expected to occur but is consistent with the purpose of the projection. When developing an education-funding computation, the assumptions would be based on those situations that are most likely to occur, and a forecast may be prepared.

Services Performed on Prospective Financial Statements

Compilations. Section 500.04 of the Guide for Prospective Financial Statements describes a compilation "as a professional service that involves--

- Assembling, to the extent necessary, the financial forecast (or projection) based on the responsible party's assumptions.
- Performing the required compilation procedures, including reading the forecast (or projections) with the

summaries of significant assumptions and accounting policies and considering whether they appear to be in conformity with the AICPA guidelines and not obviously inappropriate.
- Issuing a compilation report."

A compilation is not intended to provide assurance on the statements or the underlying assumptions. The compilation involves considering the appropriateness of the statement and its conformity with the AICPA guidelines. The procedures include making inquiries and performing certain procedures to determine consistency of the assumptions, the preparation and presentation of the statement, and the adequacy of the disclosure, without seeking to verify supporting documents. Sections 600 to 620 in the Guide for Prospective Financial Statements provide guidance on engagements to compile a prospective financial statement.

Examinations. Section 500.06 of the Guide for Prospective Financial Statements describes examinations. Examination of projections are rarely provided in a personal financial planning environment.

Agreed-Upon Procedures. Section 500.08 of the Guide for Prospective Financial Statements describes an engagement to apply agreed-upon procedures to a financial forecast or a projection as a professional service that involves--
- Having the specified users participate in establishing the nature and scope of the engagement and take responsibility for the adequacy of the procedures to be performed by the accountant.
- Applying the agreed-upon procedures.
- Issuing a report that indicates it is limited in use and intended solely for the specified users, enumerates the procedures performed, states the accountant's findings, and refers to conformity with the arrangements made with the specified users.

A prospective financial statement to which agreed-upon procedures are performed must include a summary of significant assumptions. Sections 800 to 820 in the Guide for Prospective Financial Statements describes the use of applying agreed-upon procedures to financial forecasts and projections.

Other Services. When the prospective financial statement is not reasonably expected to be used by third parties and the accountant is not engaged to compile, examine, or apply agreed-upon procedures, the accountant may provide consulting or assembly services without reporting on the statements. SOP 90-1 provides optional and flexible guidance in such circumstances.

Preparation Guidelines

When a CPA prepares a financial analysis of a potential investment transaction by obtaining the information, making appropriate assumptions, and assembling the presentation, this analysis may be deemed as a partial presentation that is appropriate for limited use if the client reviews and adopts the assumptions and presentation.

On many occasions, the CPA prepares every aspect of a projection, including the development of the assumptions. In this way, the CPA assumes many of the client's responsibilities. In such circumstances, the analysis should not be characterized as forecasted or projected information. Accordingly the CPA should consider guidance for preparation of projections as well as for presentation and reporting on such statements. Section 300 of the

Guide for Prospective Financial Statements provides guidance for preparing prospective financial statements. Highlights of the guidance include the following:

- Prospective financial information should be prepared in good faith.
- Prospective financial information should be prepared with appropriate care by qualified personnel.
- Prospective financial information should be prepared using appropriate accounting principles.
- The process used to develop prospective financial information should provide for seeking out the best information that is reasonably available at the time.
- The information used in preparing prospective financial information should be consistent with the plans of the entity.
- Key factors should be identified as a basis for assumptions. Consider key factors affecting elements, accounts, or items of prospective financial statements that are interrelated with those presented. Key factors are those significant matters upon which the client's future results are expected to depend. These serve as the foundation for the projection.
- Assumptions used in preparing prospective financial information should be appropriate.
- The process used to develop prospective financial information should provide the means to determine the relative effect of variations in the major underlying assumptions.
- The process used to develop prospective financial information should provide adequate documentation of both the forecast (or projection) and the process used to develop them.
- The process used to develop prospective financial information should include, where appropriate, the regular comparison of the financial forecasts with attained results.
- The process used to develop prospective financial information should include adequate review and approval by the responsible party at the appropriate levels of authority.

For a discussion of each of these points, please refer to the Guide for Prospective Financial Statements.

Presentation Guidelines

Refer to section 400 of the Guide for Prospective Financial Statements for presentation guidelines relevant to the CPA who will report on prospective financial information. Brief highlights of the presentation guidelines are presented below.

Responsibility. The responsibility for preparation in conformity with the Guide for Prospective Financial Statements is that of the client. The accountant may make suggestions as to the form or content of the prospective financial statements, or he or she may draft them for the client.

Title. The title used for the prospective financial information should describe the nature of the presentation. For example, for a projection the title should describe or refer to any significant hypothetical assumptions.

Date. The date of completion of the preparation of the prospective financial information should be disclosed. Section 400.29 illustrates such a disclosure.

Accounting Principles and Policies. A summary of significant accounting policies used in preparing the prospective financial information should be disclosed. Ideally, prospective financial statements and historical financial statements should be available to users on the same basis of accounting.

Materiality. Materiality applies to prospective financial statements. Materiality is judged in light of the expected range of reasonableness of the information. Users should not expect information about events that have not yet occurred to be as precise as historical information.

Assumptions. The disclosure of significant assumptions is essential to the reader's understanding of the financial projection. Section 400.23 states that assumptions disclosed should include the following:

- Sensitive assumptions -- assumptions about which there is a reasonable possibility of the occurrence of a variation that may significantly affect the prospective results.
- Assumptions about anticipated conditions that are expected to be significantly different from current conditions, which are not reasonably apparent. Examples are conditions of peace and absence of natural disaster.
- Other matters deemed important to the prospective information or its interpretation.
- Hypothetical assumptions should be identified as well as improbable hypothetical assumptions.

Particularly Sensitive Assumptions. For particularly sensitive assumptions, the accountant should specify that those assumptions appeared to be particularly sensitive at the time the presentation was prepared. The assumptions would adversely affect the prospective results, because the assumptions have a high likelihood of sizable variation or a small variation would have a large impact. For example, the federal income tax rate may be significant but not sensitive.

Period to Be Covered. The client should consider the needs of the users and its ability to estimate prospective results in determining the period to be covered.

Distinguishing From Historical Financial Statements. The financial projections should be clearly labeled to preclude a reader from confusing them with the historical financial statements. When prior-period information (such as historical results and financial forecasts from prior periods) is presented alongside the financial projection to facilitate comparison, it should be clearly labeled and distinguished from the financial projections.

Internal Use Only

CPAs may be engaged to perform services on prospective financial information that is restricted to internal use only for a variety of circumstances, such as giving advice and assistance to the client on the possible consequences of proposed future actions. The CPA may provide any of a spectrum of services, including compilation, examination, and agreed-upon procedures. In part 1 of SOP 90-1, the CPA should consider the degree of consistency of interest between the responsible party and the user in deciding whether a potential use is "internal use." If the interests are substantially consistent (for example, both the responsible party and the user are employees of the entity about which the prospective financial statement is made), the use would be deemed internal use. Otherwise (where the responsible party is a nonowner and the user is an owner), the use would not be deemed for internal use.

If a financial projection is included in a written personal financial plan that is only for internal use, paragraph 9, part 1 of SOP 90-1 states that the communication should include a caveat that the prospective results may not be achieved and a statement that the financial forecast or projection is for internal use only.

Report on Forecasts or Projections for Internal Use. If the CPA decides to issue a report and he or she purports to have compiled, examined, or applied agreed-upon procedures to a financial forecast or projections for internal use only in conformity with AICPA standards, the CPA should follow the reporting guidance in sections 620, 720, or 820, respectively, in the *Guide*. If the CPA decides to issue a report on other services performed with respect to a financial projection for internal use only, the report's form and content are flexible. However, the summary of significant assumptions should not be excluded from the projection. The report preferably would --

- Be addressed to the responsible party.
- Identify the statements being reported on.
- Describe the character of the work performed and the degree of responsibility taken with respect to the financial forecast or projection.
- Include a caveat that the prospective results may not be achieved.
- Indicate the restrictions as to the distribution of the financial projection and report.
- Be dated as of the date of the completion of his or her procedures.

In addition to the elements listed above, the CPA's report on a financial projection for internal use only preferably would include a description of the limitations of the usefulness of the presentation. Where applicable, the CPA report would--

- Indicate if the CPA is not independent with respect to an entity on whose financial projection he or she is providing services. The CPA should refuse to provide any assurance on a prospective financial statement of an entity with respect to which he or she is not independent.
- Describe omitted disclosures that come to his or her attention or simply state that there are omissions of disclosures required under the guidelines for presentation of a financial projection. For example, when a financial projection is included in a personal financial plan, the description may be worded as follows: "This financial projection was prepared solely to help you develop your personal financial plan. Accordingly, it does not include all disclosures required by the guidelines established by the American Institute of Certified Public Accountants for a presentation of a financial projection."

Illustrative Report. The following is an example of a report for a financial projection that has been assembled by the CPA for which distribution is limited to internal use.

> We have assembled projections concerning your projected statement of financial condition and the related projected statement of changes on net worth, projected federal tax calculations, and projected estate tax calculations, from information provided by you. (The projected statement of financial condition omits the summary of significant accounting policies.)* We have not compiled or examined the projections and express no assurance of any kind on them. Further, there usually will be differences between the projected and actual results, because events and circumstances frequently do not

* This sentence should be included if applicable.

occur as expected, and those differences may be material. In accordance with the terms of our engagement, this report and the accompanying projections are restricted to internal use by you and your advisers who are developing your financial plan and may not be shown to third parties for any purpose.

REPORTING ON PERSONAL FINANCIAL STATEMENTS

Unaudited Personal Financial Statements

CPAs engaged to compile or review financial statements included in a personal financial planning engagement must comply with the SSARSs. If the CPA is engaged to compile or review information other than financial statement, the SSARSs do not apply. When a CPA is engaged to compile or review financial statements, the CPA should consider whether he or she should report in accordance with SSARS 1 or SSARS 6.

Unaudited personal financial statements included in a financial plan are subject to either SSARS 1 or SSARS 6. SSARS 6, Reporting on Personal Financial Statements Included in Written Personal Financial Plans, provides the accountant an exemption from reporting in accordance with SSARS 1 when he or she submits a written personal financial plan containing unaudited personal financial statements to a client after he or she establishes with the client that the financial statements (1) will not be used for credit-granting purposes or for any other purposes other than developing goals and objectives and (2) will be used exclusively to assist the client and his or her advisers to develop the goals and objectives.

If the accountant reports in accordance with SSARS 6, his or her report notes that the accompanying financial statement may be incomplete or may contain departures from generally accepted accounting principles (GAAP). (See reprint of SSARS 6 in appendix D of this document.) Although most personal financial statements in personal financial plans generally include SSARS 6 reports, some are subject to the requirements of SSARS 1, as amended.

It is necessary to perform a SSARS 1 engagement when the financial statements will be used by a third party for credit purposes. The CPA may need to report under SSARS 1 if (1) the engagement does not meet the definitions of SSARS 6 or (2) the client engages the CPA to compile or review in accordance with SSARS 1.

Because the purpose of including personal financial statements in personal financial plans is solely to assist in developing the client's personal financial plan, the statements frequently omit disclosures required by GAAP and contain departures from GAAP or from an established other comprehensive basis of accounting (OCBOA) other than GAAP. SSARS 6 provides an exemption from SSARS 1, as amended, for such financial statements. The benefit of using SSARS 6 is that departures from GAAP do not need to be disclosed in the accountant's report.

A CPA may prepare a financial statement on a tax basis or a cash basis (OCBOA). For example, doctors and other professionals frequently use the cash basis of accounting. For more practical information on OCBOA, see Technical Information for Practitioners Series (Tips) No. 1, Other Comprehensive Bases of Accounting.

Compilation and Review. The CPA follows the guidance in SSARS 1 if he or she is engaged to compile or review financial statements of a nonpublic entity.

It is necessary to compile or review the financial statements if they are going to be used by third parties or to be relied on to obtain credit. The CPA must consider the guidance in SOP 82-1 if he or she is engaged to compile or review a financial statement. When a CPA performs a compilation or review of a financial statement to be included in a personal financial plan that fails to include all the required disclosures, a provision for estimated income taxes, or other departures from GAAP, the CPA should modify the standard report to disclose these departures.

Issuing Draft Personal Financial Statements

A CPA frequently issues draft financial statements during a personal financial planning engagement for review by the client prior to final issuance of the plan. The Accounting and Review Services Committee issued an interpretation noting that a CPA should not submit draft financial statements without intending to submit those in final form accompanied by an appropriate compilation or review report. The interpretation states that as long as the accountant intends to submit those financial statements in final form and labels each page with words such as "Draft" or "Preliminary Draft," the accountant does not have to report in accordance with SSARSs with respect to those draft financial services.

Reporting When the Accountant Is Not Independent

A CPA frequently is asked to compile or review personal financial statements when the CPA is not independent of the client. ET section 101 of the Code of Professional Conduct states that independence is considered impaired if a member or a member's firm had, for example, any of the following transactions, interests, or relationships:

- Had or was committed to acquire any direct or material indirect financial interest in the client's business
- Acted as a trustee of any trust or executor or administrator of any estate if such trust or estate had or was committed to acquire any direct or material indirect financial interest in the client or the client's business
- Had any loan to or from the client
- Acted in the capacity equivalent to that of the member of management or of an employee

SSARS 1 states that if a CPA is not independent of the client, he or she is not precluded from issuing a report with respect to his or her compilation of financial statements for that client (AICPA, Professional Standards, Vol. 2, AR sec. 100.22). SSARS 1 further states that a CPA is precluded from issuing a report on his or her review of financial statements with respect to a client with respect to which he or she is not independent (AICPA, Professional Standards, Vol. 2, AR sec. 100.38). When issuing such a report on his or her compilation of financial statements the CPA should disclose the lack of independence. However, the reason for the lack of independence should not be described. When the CPA is not independent, the last paragraph of the compilation report should include the following sentence: "I am (we are) not independent with respect to Mr. and Ms. Will I. Say."

PREPARING PERSONAL FINANCIAL STATEMENTS

In most personal financial planning engagements, the analysis of the client's statement of financial condition is a key component in the development of the overall financial plan. The statement of financial condition provides information about the client's asset allocation, liquidity, leverage, and net worth.

The Personal Financial Statement Guide

The Personal Financial Statement Guide provides information and guidance that is useful and relevant to providing personal financial planning services. It serves as a basis for applying professional standards to engagements involving personal financial statements. The Personal Financial Statements Guide includes SOP 82-1, Accounting and Financial Reporting for Personal Financial Statements. When the Accounting Standards Executive Committee developed SOP 82-1 it had in mind the interests of the third-party users of the financial statements. SOP 82-1 is generally used for the preparation of financial statements if the client is seeking credit or if the client intends for third parties to use the financial information. A brief discussion of the guidance in SOP 82-1 appears later in this section.

When submitting and reporting on financial statements that will be used for personal financial planning engagements in accordance with SSARS 6, CPAs may decide not to follow the guidance in SOP 82-1. Some of the guidance in Personal Financial Statements Guide and SOP 82-1 is helpful to consider when providing personal financial planning engagements even if personal financial statements are not issued to the client, for example, client acceptance procedures and the development of an understanding with a client. The presentation guidance, however, is often not economical for personal financial planning engagements prepared in accordance with SSARS 6.

The Personal Financial Statements Guide (page 1) states that "some procedures are common to all personal financial statement engagements; for example,

- A decision is made whether to accept a prospective client.
- An understanding is reached with the client regarding the type of service to be rendered.
- Ordinarily information is gathered."

Client Acceptance Procedures. The Personal Financial Statements Guide (page 2) states that "before accepting an engagement involving personal financial statements, the accountant ordinarily would evaluate certain aspects of the potential client relationship." The guide describes factors to consider, including--

- Facts that might bear on the integrity of the prospective client.
- His or her ability to serve the prospective client.
- Whether available accounting records or other data provide a sufficient basis for providing the services requested. The Personal Financial Statements Guide also notes that "the accountant may wish to consult predecessor accountants or auditors, attorneys, bankers, and others having business relationships with the individuals regarding facts that might bear on the integrity of the prospective client."

Understanding With the Client. Understanding with the client is described in many areas of professional literature. The Personal Financial Statements Guide states that "once an accountant has decided to accept an engagement involving personal financial statements, he should establish an understanding with the client, preferably in writing, regarding the services to be performed and the terms and objectives of the engagement." SSARS 1 (AICPA, Professional Standards, Vol. 2, AR sec. 100.08) adheres to those same thoughts and adds that the "understanding should include a description of the nature and limitation of the services to be performed and a description of the report the accountant expects to render."

Level of Knowledge. The Personal Financial Statements Guide states that professional standards require the accountant to attain a certain level of knowledge of the client's financial activities. That knowledge relates to the individual's financial transactions, accounting methods, sources of information, and the form and content of the financial statements.

Gathering Information. The Personal Financial Statements Guide suggests that it may be necessary to obtain information from outside sources such as bankers, financial consultants, and attorneys who may know about the client's financial affairs (page 4). A list of possible sources of information is included in appendix B of the Personal Financial Statements Guide.

IDENTIFYING WHEN FINANCIAL DATA IS A FINANCIAL STATEMENT

Both ET section of the Code of Professional Conduct and SSARS 1 (AICPA, Professional Standards, Vol. 2, AR sec. 100.04) define the term financial statements. Financial statements show (1) financial position at a point in time or (2) changes in financial position over time, and (3) use cash or other incomplete basis of accounting (ET section 92.04). AR section 100.04 broadly defines a financial statement as "a presentation of financial data, including accompanying notes, derived from accounting records and intended to communicate an entity's economic resources or obligations at a point in time, or changes therein for a period of time, in accordance with generally accepted accounting principles or a comprehensive basis of accounting other than generally accepted accounting principles."

An individual may not have accounting records and may provide a list of assets and liabilities to the accountant. If the accountant includes this information in the written financial plan, some believe the information is incidental financial data rather than a financial statement. ET section 92.04 indicates that "incidental financial data included in management advisory services reports to support recommendations to a client and tax return and supporting schedules do not constitute financial statements." When financial data is presented in the form of a financial statement, it is subject to the reporting requirements of the SSARSs.

To determine whether the financial information included in the plan is a financial statement rather than incidental financial data, it can be inferred from TIS section 9600.03 of AICPA Technical Practice Aids that a list of assets and liabilities with totals or subtotals is a financial statement. TIS section 9600.03 indicates that when an accountant adds captions to classify and provides subtotals and totals for each classification, a working trial balance becomes a financial statement. Thus, a financial profile shown in the format of a financial statement with totals or subtotals is subject to the guidance found in the SSARSs.

Personal Financial Statement Presentation

SOP 82-1 deals with the preparation and presentation of personal financial statements. Such statements present assets and liabilities at their estimated current amounts at the date of the financial statements (SOP 82-1, paragraph 4). The form (SOP 82-1, paragraph 6) of the statements consists of--

- A Statement of Financial Condition. This is the basic financial statement.
- A Statement of Changes in Net Worth. This presents basic increases and decreases in net worth. It pres-

ents income, expenses, and changes in estimated current assets and liabilities. It is optional to present a Statement of Changes in Net Worth.

- Comparative Financial Statements. Financial statements for the current period and one or more prior periods may sometimes be desirable. This presentation is optional.

Presentation Method. The method of presentation is as follows:

- The accrual basis is used, not the cash basis (SOP 82-1, paragraph 7).
- Assets and liabilities are presented in order of liquidity and maturity without classification between current and noncurrent (SOP 82-1, paragraph 8). A categorized statement that group assets based on common factors such as liquid assets, investments, and personal assets is permitted.
- If property is jointly owned only the person's beneficial interests in the property as determined by the state property laws should be included in the statements (SOP 82-1, paragraph 9).
- The estimated current value of business interests that (1) constitute a large portion of a person's total assets and (2) are marketable as a going concern is shown separately from similar personal assets (SOP 82-1, paragraph 10). Summarized financial information about such an entity is presented in the footnotes (SOP 82-1 paragraph, 31f).
- Limited business activities not conducted as a separate business are presented separately. As an example, for an investment in real estate the estimated value of the land is shown under assets, and a related mortgage is shown under liabilities.

Determining Estimated Current Values

The guidelines for determining estimated current values of assets and liabilities are useful for preparing personal financial statements that will be used by third parties. Depending on the nature of the engagement, current-value information may be necessary to support the recommendations included in the financial plan. For further discussion concerning the values and amounts at which the assets and liabilities are presented, see appendix C.

Generally accepted accounting principles other than those discussed in SOP 82-1 apply to personal financial statements. For example, FASB Statement No. 5, Accounting for Contingencies, and FASB Statement No. 57, Related Party Disclosures (SOP 82-1, paragraph 32).

STATEMENTS ON RESPONSIBILITIES IN TAX PRACTICE

The Statements on Responsibilities in Tax Practice provide guidance when--

- Preparing federal income tax projections.
- Reviewing prior-year tax returns and discovering an error.
- Preparing a tax return following a financial planning engagement.

PREPARING INCOME TAX PROJECTION MODELS AND DEVELOPING A TAX PLAN

The AICPA's Statements on Responsibilities in Tax Practice No. 8, Form and Content of Advice to Clients (AICPA, Professional Standards, Vol. 2, TX sec. 182), should be considered by CPAs who include income and estate tax advice and projections in personal financial planning engagements. Although no standard format for communicating written or oral advice to a client is provided, the statement explains that "in providing tax advice to a client, the CPA should use judgment to ensure that the advice given reflects professional competence and appropriately serves the client's needs" (AICPA, Professional Standards, Vol. 2, TX section 182.02).

TX section 182.04 indicates that "the CPA may choose to communicate with a client when subsequent developments affect advice previously provided with respect to significant matters." The CPA is expected to initiate such communications (1) while helping a client implement procedures or plans associated with the advice provided or (2) when the CPA undertakes this obligation by specific agreement.

TX section 182.06 further states "written communication are recommended in important, unusual, complicated transactions. In the judgment of the CPA, oral advice may be followed by written communication to the client."

TX section 182.07 describes some factors to consider in deciding on the form of advice provided to a client. These include the following:

- Importance of the transaction and amounts involved
- Specific or general nature of the client's inquiry
- Time available for development and submission of the advice
- Technical complications presented
- Existence of authorities and precedents
- Tax sophistication of the client
- Need to seek legal advice

TX section 182.08 states that "the CPA may assist a client in implementing procedures or plans associated with the advice offered. During this active participation, the CPA continues to advise and should review and revise such advice as warranted by new developments and factors affecting the transaction." TX section 182.09 observes that "sometimes the CPA is requested to provide tax advice but does not assist in the implementing the plans adopted." Because the purpose of the planning engagement is to get the client to do something and the client wants something to happen, the CPA may help the client with this.

TX 182.09 notes, however, that the CPA cannot be expected to communicate legislative or administrative changes or further judicial interpretations that affect advice previously provided "unless the CPA undertakes this obligation by specific agreement with the client." The communication of significant developments affecting previous advice is considered as "an additional service rather than an implied obligation in the normal CPA- client relationship."

TX section 182.10 provides the guidance that "the client should be informed that advice reflects professional judgment based on an existing situation and that subsequent developments could affect previous professional advice." This explanation says that "CPAs should use precautionary language to effect that their advice is based on facts as stated and authorities that are subject to change." CPAs preparing personal financial plans often include a precautionary statement that explains that the income and estate tax planning recommendations are based on information received from the client and tax laws and regulations that are subject to change. Such statements remind the client that tax advice in a financial plan may not be current may and need updating.

The AICPA's Statement on Responsibilities in Tax Practice No. 1, Tax Return Positions (AICPA, Professional Standards, Vol. 2, TX sec. 112), should be considered by CPAs who recommend income tax positions when developing projections in personal financial planning engagements. CPAs have a duty to their clients as well as to the tax system. The major thrust of TX section 112.02 is that before a CPA recommends a tax return position, he or she must have "a good faith belief that the position has a realistic possibility of being sustained administratively or judicially on its merits if challenged." If there is no such good faith belief, a tax return position may be recommended only if there is disclosure of the position and the position is not frivolous. TX section 112.02 provides that CPAs should, "where relevant, advise the client as to the potential penalty consequences of the recommended tax return position." TX section 112.03 provides additional guidance that "the CPA should not recommend a tax position that exploits the Internal Revenue Service audit selection process." The CPA has both the right and the responsibility to be an advocate for the client with respect to the tax positions (AICPA, Professional Standards, Vol. 2, TX section 112.04).

REVIEWING A PRIOR YEAR TAX RETURN AS PART OF A PFP ENGAGEMENT AND DISCOVERING AN ERROR

The AICPA's Statements on Responsibilities in Tax Practice No. 6, Knowledge of Error: Return Preparation (AICPA, Professional Standards, Vol. 2, TX sec. 162), should be considered by CPAs who become aware of an error in a client's previously filed tax return or of the client's failure to file a required tax return during personal financial planning engagements. TX section 162.03 indicates that "the CPA should inform the client promptly upon becoming aware of an error in a previously filed return or upon becoming aware of a client's failure to file a required return. The CPA should recommend the measures to be taken. Such recommendation may be given orally." TX section 162.05 notes that "it is the client's responsibility to decide whether to correct the error." If the client will not correct the error, the CPA should consider withdrawing or "whether to continue a professional relationship with the client."

TX section 162.08 observes that when the CPA becomes aware of an error during an engagement that does not involve tax return preparation, "the responsibility of the CPA is to advise the client of the existence of the error and to recommend that the error be discussed with the client's tax return preparer."

PREPARING A TAX RETURN FOLLOWING A FINANCIAL PLANNING ENGAGEMENT

The AICPA's Statements on Responsibilities in Tax Practice No. 3, Certain Procedural Aspects of Preparing Returns (AICPA, Professional Standards, Vol. 2, TX sec. 132), should be considered by CPAs who prepare a client's tax return following a personal financial planning engagement. TX section 132.02 indicates that, "the CPA should not ignore the implications of information furnished and should make reasonable inquiries if the information furnished appears to be incorrect, incomplete, or inconsistent either on its face or on the basis of other facts known to the CPA." For example, the CPA should inquire about information obtained from cash flow modeling or data gathering about related business income that was used to prepare a cash flow projection but was not included in the tax return information.

Appendix A
AICPA Professional Standards

Professional Standards. The following table lists the types of documents that are applicable to personal financial planning and the degree of authoritativeness of each.

DOCUMENT	AUTHORITATIVENESS
Statements of Standards on Accounting and Review Services	Binding
Statements on Standards for Attestation Engagements	Binding
Statement on Standards for Management Advisory Services	Binding
Statement on Standards for Accountant's Services on Prospective Financial Information	Binding
Statements of Position	See discussion following
Audit and Accounting Guides	See discussion following
Technical Information Service Inquiries and Replies	See discussion following
Statements on Responsibilities in Tax Practice	See discussion following

Statements of Position. Statements of position of the Accounting Standards Division present the conclusions of at least a majority of the Accounting Standards Executive Committee, which is the senior technical body of the Institute authorized to speak for the Institute in the areas of financial accounting and reporting. Statements of position of the Auditing Standards Division are issued to revise or clarify certain recommendations in industry-oriented audit guides or areas to which they relate. Statements of position have the same authority as that of an audit and accounting guide.

AICPA Audit and Accounting Guides. Audit and accounting guides present recommendations of the AICPA Committee on the Application of Generally Accepted Auditing Standards to audits of financial statements and recommendations and descriptions of financial accounting and reporting principles and practices. The Accounting Standards Executive Committee and members of the Auditing Standards Board review guides before issuance to assure that they are consistent with existing standards and principles covered by rules 202 and 203 of the AICPA Code of Professional Conduct. AICPA members must be prepared to justify departures from guides.

AICPA Technical Information Service Inquiries and Replies. These are not official positions of the AICPA or any of its committees and the material should be considered when developing a position.

Statements on Responsibilities in Tax Practice. These present the Tax Division's opinions of what it considers to be appropriate standards of responsibility in tax practice. The statements are not intended to establish a separate code of conduct in federal income tax practice and depend on general acceptability of the opinions expressed. They are advisory (that is, they do not constitute enforceable technical standards) and educational in nature.

Appendix B
Excerpted From AICPA Code of Professional Conduct

Integrity and Objectivity. Ethics rule 102 requires that in the performance of any professional service, a member shall maintain objectivity and integrity, shall be free of conflicts of interest, and shall not knowingly misrepresent facts or subordinate his or her judgment to others. Examples of such violations include the following:

- Knowingly making, permitting, or directing another to make false and misleading entries in an entity's financial statements or records (ET section 102.02)
- A conflict of interest may occur if a member performs a professional service for a client or employer and the member or his or her firm has a significant relationship with another person, entity, product, or service that could be viewed as impairing the member's objectivity. If this significant relationship is disclosed to and consent is obtained from the client, employer, or other appropriate parties, the rule shall not operate to prohibit the performance of the professional service (ET section 102.03)

Confidentiality. Clients expect that information about their personal finances will be kept confidential. Ethics rule 301 states that confidential client information may be disclosed after obtaining the specific consent of a client (ET section 301.01).

Contingent Fees. Ethics rule 302 permits contingent fee arrangements for personal financial planning engagements for a client for whom the member or the member's firm does not also perform: (1) an audit or review of a financial statement or (2) a compilation of a financial statement when the member expects, or reasonably might expect, that a third party will use the financial statement and the member's compilation report does not disclose a lack of independence; or (3) an examination of prospective financial information. (This rule became effective August 9, 1990, on the same date the final order of the Federal Trade Commission became effective.)

Acts Discreditable. Ethics rule 501 prohibits acts that are discreditable to the profession. Examples of such acts include the following:

- Retention of the client's records after demand is made for them (ET section 501.02)
- Negligence in the preparation of financial statements. Negligence means making, permitting, or directing another to make false and misleading entries in the financial statements or records of an entity (ET section 501.05)

Advertising and Other Forms of Solicitation. Ethics rule 502 requires that advertising and other forms of solicitation not be false, misleading, or deceptive. ET section 502.02 describes prohibited advertising activities which include the following:

- Creating false or unjustified expectations of favorable results
- Consisting of self-laudatory statements or making comparison with other CPAs that are not based on verifiable facts
- Containing any other representations that would be likely to cause a rea-

sonable person to misunderstand or be deceived.

A CPA who has the Accredited Personal Financial Specialist designation or other designations, such as a certified financial planner, may use the designation if the use of such a designation is permitted by the CPA's state board of accountancy.

Engagements Obtained Through Efforts of Third Parties Are Permitted. (ET section 502.06). Members are required to ascertain that third parties' promotional efforts are within the bounds of the rules of conduct. Because members receive benefits from the efforts of third parties, they are prohibited from using third parties to do what they are prohibited from doing.

Commissions. Ethics rule 503 permits members engaged in the practice of public accounting to accept a payment for the referral of products or services of others to a client in certain situations. A member who is not prohibited from performing services for or receiving a commission and who is paid or expects to be paid a commission is required to disclose that fact to any person or entity to whom the member recommends or refers a product or service to which the commission relates. A member in public practice shall not for a commission recommend or refer to a client any product or service, or for a commission recommend or refer any product or service to be supplied by a client, or receive a commission, when the member or the member's firm also performs for that client: (1) an audit or review of a financial statement; or (2) a compilation of a financial statement when the member expects, or reasonably might expect, that a third party will use the financial statement and the member's compilation report does not disclose a lack of independence; or (3) an examination of prospective financial information.

This prohibition applies during the period in which the member is engaged to perform any of the services listed above and the period covered by any historical financial statements involved in such listed services.

Any member who accepts a referral fee for recommending or referring any service of a CPA to any person or entity or who pays a referral fee to obtain a client shall disclose such acceptance or payment to the client.

Form of Practice and Name. Ethics rule 505 covers the form of practice and name for members in the practice of public accounting to be in compliance with the Rules. It is permissible for a member to invest in a commercial corporation that provides financial planning services to the public if the member's financial interest is not material to the corporation's net worth and the member's interest in and relationship to the corporation is solely that of an investor (ET section 505.02). Interpretation of ET section 505-2 provides that a member in the practice of public accounting can participate in the operation of a separate business that offers financial planning services to clients if the member observes all of the rules of conduct in the operation of the separate business. Because financial planning is a service provided by public accountants, a member who operates a separate business is required to follow all of the rules of conduct in the operation of that business. (In July 1990, the Board of Directors voted to recommend that Council authorize a mail ballot of the membership to amend ethics rule 505 in order to make it possible for CPAs to practice in limited liability corporations.)

Appendix C
Guidelines for Determining Estimated Current Values of Assets and Liabilities

Determining Estimated Current Values. SOP 82-1 defines the estimated current value of an asset in paragraph 12 as "the amount a buyer and a seller, each of whom is well informed and willing, neither of whom is compelled to buy or sell." Current value of an asset is the current selling price less expected direct costs of disposal. Because the current values of some assets are difficult to estimate and the cost of obtaining the value may exceed the benefits of doing so, judgment is exercised in determining estimates of current values.

Other factors to consider include the following:

- Recent sales transactions involving similar assets and liabilities in a similar situation (paragraph 13)
- Capitalization of past or prospective earnings (paragraph 13)
- Liquidation values (paragraph 13)
- Historical cost adjusted for changes in specific price index (paragraph 13)
- Appraisal (paragraph 13)
- Discounted amounts of projected cash receipts and payments (paragraph 13)
- Consultation with a specialist (paragraph 14)

The guidelines for determining estimated current values of assets and liabilities are useful for preparing personal financial statements. Depending on the nature of the engagement, current-value information may be necessary to support the recommendations included in the financial plan.

Receivables. The current value is the discounted amounts of cash expected to be collected, using appropriate interest rates (paragraph 16).

Marketable Securities. Market quotations are used generally. The current value is the closing prices of the securities if traded on the securities exchanges on the date of the financial statement (valuation date). If the securities were not traded on that date but published bid and asked prices are available, the estimated current value should be within the range of those prices (paragraph 17).

For over-the-counter market securities many sources are available for quotes of the bid and asked prices. To determine the estimated current values for those securities, use either the mean of (1) bid prices, (2) bid and asked prices, or (3) prices of a representative selection of broker-dealers quotes of the securities (paragraph 18).

It may be necessary to adjust recent market price of the security to determine the estimated current market value. Factors to consider include quantity of securities held. For example, a large block of equity securities may not be salable at the price a small number of shares were recently sold or quoted (paragraph 19). For further discussion on valuing marketable securities, see AICPA Audit and Accounting Guide Audits of Investment Companies, pp. 15 - 17.

Options. When published prices are unavailable, the estimated current values are based on the values of the assets subject to option, considering such factors as exercise prices and length of the option periods (paragraph 20).

Investment in Life Insurance. The estimate current value is the cash value of the policy less the amount of loans against it. The face amount of the life insurance is disclosed (paragraph 21).

Investments in Closely Held Businesses. For closely held business investments, the net investment in a business enterprise at its estimated current value is presented in the statement of financial condition. This value is usually difficult to determine because there is usually no ready market for such an investment. Several procedures or a combination of procedures may be used to determine the estimated current value of a closely held business, including a multiple of earnings, liquidation value, reproduction value, appraisals, discounted amounts of projected cash receipts and payments, or adjustments of book values or cost of the person's share of the equity in the business. If a buy - sell agreement exists it should be considered, but it does not necessarily determine the estimate current value (paragraphs 22 - 23).

Real Estate (Including Leaseholds). Information to determine the estimated current value includes the following:

- Sales of similar property in similar situations
- Discounted projected cash receipts and payments relating to the property or the net realizable value of the property, based on planned courses of action, including leaseholds whose current rental value exceeds the rent in the lease
- Appraisals used to obtain financing or based on estimates of selling prices and costs from independent real estate agents or brokers with similar properties in similar locations
- Assessed values for property taxes, including consideration of the basis for such assessments and their relationship to market values in the area (paragraph 24)

Intangible Assets. If both the amounts and the timing of the cash receipts and payments arising from the planned use or sale of the assets can be reasonably estimated, use the projected discounted amounts. For example, a record of receipts under a royalty agreement may provide sufficient information to determine its estimated current value. The cost of a purchased intangible is used if no other information is available (paragraph 25).

Future Interests and Similar Assets. Discounted amounts are used for nonforfeitable rights to receive future sums that (1) are for fixed or determinable amounts, (2) are not contingent on the holder's life expectancy or the occurrence of a particular event, such as disability or death, and (3) do not require future performance of service by the holder. Assets that may meet those characteristics include the following:

- Guaranteed minimum portions of pensions
- Vested interests in pension or profit sharing plans
- Deferred compensation contracts
- Beneficial interests in trusts
- Remainder interests in property subject to life estates
- Annuities
- Fixed amounts for alimony for a definite future period (paragraph 26)

Payables and Other Liabilities. The estimated current value of payables and other liabilities is the discounted amounts of cash to be paid. The rate implicit in the transaction in which the debt was incurred is the discount rate. If the debtor is able to discharge the debt currently at a lower amount, the debt should be presented at the lower amount (paragraph 27).

Noncancelable Commitments. Discounted amounts are used for noncancelable commitment to pay future sums that meet the characteristics described as future interests. Examples may include alimony and charitable pledges.

Income Taxes Payable. The liability should include (1) unpaid income taxes for completed tax years and (2) the estimated amount for income taxes accrued for the elapsed portion of the current tax year to the date of the financial statements. That estimate is based on the relationship of taxable income earned to date to total estimated taxable income for the year, net of taxes withheld or paid with estimated tax returns (paragraph 29).

Estimated Income Taxes. SOP 82-1 requires that (paragraph 30) estimated income taxes be calculated on the differences between the estimated current values of assets and the estimated current amounts of liabilities and their tax bases. The methods and assumptions used to compute the estimated taxes should be disclosed. The estimated taxes should be presented between the liabilities and net worth.

When an accountant is engaged to compile or review a financial statement that fails to include a provision for estimated income taxes, the accountant should consider modifying the standard report to disclose this departure. If the written person financial plan includes personal financial statements that will be used solely to assist in developing a personal financial plan and not used to obtain credit, the accountant may comply with SSARS 6.

Required Disclosures. SOP 82-1 describes financial disclosures necessary to make the financial statements adequately informative in paragraph 31. SSARS 1, paragraphs 19 - 21, permits an accountant to compile a financial statement that omits the required disclosures if the omission is clearly indicated in the accountant's report, and it is not done to mislead the users of the financial statement. A paragraph describing the omission should be added to the standard report. If the financial statement does not disclose that assets are presented at estimated current values and liabilities at estimated current amounts, the accountant should include the following sentence at the end of the first paragraph of his report: "The financial statements are intended to present the assets of Model Person at estimated current values and their liabilities at estimated current amounts."

SSARS 6, Reporting on Personal Financial Statements Included in Written Personal Financial Plans, provides information on the special reporting requirements for personal financial statements included in written personal financial plans that are not expected to be used for credit granting purposes and that are intended to help the client and his or her advisers implement the plan. This special disclaimer states that the statement of financial condition may not be prepared in accordance with GAAP (see reprint of SSARS 6 in appendix D of this document).

Appendix D
SSARS 6, Reporting on Personal Financial Statements Included in Written Personal Financial Plans

1. This statement provides an exemption from Statement on Standards for Accounting and Review Services (SSARS) 1, as amended, for personal financial statements that are included in written personal financial plans prepared by an accountant, and specifies the form of written report required under the exemption.[1] However, this statement does not preclude an accountant from complying with SSARS 1 in such engagements.

2. Because the purpose of such financial statements is solely to assist in developing the client's personal financial plan, they frequently omit disclosures required by generally accepted accounting principles (GAAP) and contain departures from GAAP or from an established comprehensive basis of accounting other than GAAP.

3. An accountant may submit a written personal financial plan containing unaudited personal financial statements to a client without complying with the requirements of SSARS 1, as amended, when all of the following conditions exist:

a. The accountant establishes an understanding with the client, preferably in writing, that the financial statements—

  (i) Will be used solely to assist the client and the client's advisers to develop the client's personal financial goals and objectives.

  (ii) Will not be used to obtain credit or for any purposes other than developing these goals and objectives.

b. Nothing comes to the accountant's attention during the engagement that would cause the accountant to believe that the financial statements will be used to obtain credit or for any purposes other than developing the client's financial goals and objectives.

4. An accountant using the exemption provided by this statement should issue a written report stating that the unaudited financial statements—

a. Are designed solely to help develop the financial plan.

b. May be incomplete or contain other departures from GAAP and should not be used to obtain credit or for any purposes other than developing the personal financial plan.

c. Have not been audited, reviewed, or compiled.

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1. For purposes of this statement, personal financial statements are those financial statements of an individual that meet the definition of financial statements in paragraph 4 of SSARS 1, *Compilation and Review of Financial Statements*.

5. The following is an illustration of an appropriate report when an accountant uses the exemption provided by this statement.

> The accompanying Statement of Financial Condition of X, as of December 31, 19XX, was prepared solely to help you develop your personal financial plan. Accordingly, it may be incomplete or contain other departures from generally accepted accounting principles and should not be used to obtain credit or for any purposes other than developing your financial plan. We have not audited, reviewed, or compiled the statement.

6. Each of the personal financial statements should include a reference to the accountant's report.

Effective Date

7. This statement is effective on September 30, 1986.

Note: *Statements on Standards for Accounting and Review Services are issued by the AICPA Accounting and Review Services Committee, the senior technical committee of the Institute designated to issue pronouncements in connection with the unaudited financial statements or other unaudited financial information of a nonpublic entity. Council has designated the AICPA Accounting and Review Services Committee as a body to establish technical standards under Rule 204 of the Institute's Rules of Professional Conduct. Rule 204 requires adherence to those technical standards and requires that members be prepared to justify departures from them.*

Appendix E
Minimum Presentation Requirements for Prospective Financial Statements
EXCERPTED FROM THE AICPA GUIDE FOR PROSPECTIVE FINANCIAL STATEMENTS, SECTION 400.06

Format

.06 Prospective information presented in the format of historical financial statements facilitates comparisons with financial position, results of operations, and changes in financial position of prior periods, as well as those actually achieved for the prospective period. Accordingly, financial projections preferably should be in the format of the historical financial statements that would be issued for the period(s) covered if there is no agreement between the responsible party and potential users specifying another format. Financial projections may take the form of complete basic financial statements [3] or may be limited to the following items (where such items would be presented for historical financial statements for the period): [4]

a. Sales or gross revenues
b. Gross profit or cost of sales
c. Unusual or infrequently occurring items
d. Provision for income taxes
e. Discontinued operations or extraordinary items
f. Income from continuing operations
g. Net income
h. Primary and fully diluted earnings per share
i. Significant changes in financial position [5]
j. A description of what the responsible party intends the financial projection to present, a statement that the assumption are based on the responsible party's judgment at the time the prospective information was prepared, and a caveat that the projected results may not be achieved
k. Summary of significant assumptions
l. Summary of significant accounting policies

.07 Items a through i, above, represent the minimum items that constitute a financial forecast. A presentation that omits one or more of these that are applicable [6] would be a partial presentation and, thus, would not ordinarily by appropriate for general use. [7] If the omitted applicable item is derivable from the information presented, the presentation would *not* be deemed to be a partial presentation.

.08 Items j through l, above, are disclosures that should accompany the forecast whether the presentation is limited to applicable minimum items or presents more detail. The omission of item j, k, or l from a presentation that contains at least the applicable minimum items would not make it a partial presentation; it would be a deficient presentation because of the lack of required disclosures.

.09 The guidelines for preparation of financial forecasts (section 300) apply even if the presentation is limited to the minimum items above. Therefore, the underlying data used in the preparation of financial forecasts should be sufficient to allow presentation of detailed statements even though only the minimum is to be presented. [8]

.10 Each page of a financial forecast should contain a statement that directs the reader to the summaries of significant assumptions and accounting policies.

FOOTNOTES:

[3] The details of each statement may be summarized or condensed so that only the major items in each are presented. The usual footnotes associated with historical financial statements need not be included as such. However, significant assumptions and accounting policies should be disclosed.

[4] Similar types of financial information should be presented for entities for which these terms do not describe operations, as illustrated in section 410.02. Further, similar items should be presented if a comprehensive basis of accounting other than generally accepted accounting principles is used to present the forecast. For example, if the forecast is presented on the cash basis, item a would be cash receipts. The basis of accounting on which the forecast is presented should be appropriate for the use of the forecast.

[5] This item does not require a balance sheet or a statement of changes in financial position. Exhibits 2, 3, and 5 in section 410 illustrate alternative methods of presenting significant changes in financial position.

[6] An applicable item is one that would be presented for historical financial statements. For example, earnings per share would not be an applicable item for a nonpublic entity since earnings per share are not required to be presented for historical financial statements for such entities.

[7] See section 1000 for a discussion of partial presentations.

[8] This level of detail should be comparable to that presented in historical financial statements.

Appendix F
Selected Information About Partial Presentations of Projections

Partial presentations are not ordinarily appropriate for general use. Accordingly, a partial presentation should not be distributed to third parties who will not be negotiating directly with the responsible party. *Negotiating directly* is defined as the third-party user's ability to ask questions of and negotiate the terms or structure of the transaction directly with the responsible party. The following guidance describes matters to be considered with respect to partial presentations:

Key Factors. The key factors affecting elements, accounts, or items of prospective financial statements that are interrelated with those presented should be considered.

Titles. The title used for the partial presentation should describe the limited nature of the presentation and not state that it is a "financial forecast" or a "financial projection." Examples of appropriate titles are "projected college costs for each child based on current college cost" or "projected life insurance needs assuming your spouse will never work and all funds will be exhausted when your spouse reaches age 85."

Materiality. The concept of materiality should be related to the partial presentation taken as a whole.

Assumptions. Assumptions deemed to be significant to the partial presentation of prospective financial information should be disclosed.

Introduction to Summary of Assumptions. The introduction preceding the summary of assumptions for a partial presentation should include a description of the purpose of the presentation and any limitations on the usefulness of the presentation.

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