

AU Section 336 — *Using the Work of a Specialist*

(Supersedes SAS No. 11)

Source: SAS No. 73; Auditing Standard Nos. 8–15; Auditing Standard No. 18.

See [section 9336](#) for interpretations of this section.

Effective for audits of periods ending on or after December 15, 1994.

Introduction and Applicability

.01 The purpose of this section is to provide guidance to the auditor who uses the work of a specialist in performing an audit in accordance with generally accepted auditing standards. For purposes of this section, a specialist is a person (or firm) possessing special skill or knowledge in a particular field other than accounting or auditing.^[fn 1]

.02 Specialists to which this section applies include, but are not limited to, actuaries, appraisers, engineers, environmental consultants, and geologists. This section also applies to attorneys engaged as specialists in situations other than to provide services to a client concerning litigation, claims, or assessments to which [section 337](#), *Inquiry of a Client's Lawyer Concerning Litigation, Claims, and Assessments*, applies. For example, attorneys may be engaged by a client or by the auditor as specialists in a variety of other circumstances, including interpreting the provisions of a contractual agreement.

.03 The guidance in this section is applicable when—

- a. Management engages or employs a specialist and the auditor uses that specialist's work as evidential matter in performing substantive tests to evaluate material financial statement assertions.
- b. Management engages a specialist employed by the auditor's firm to provide advisory services^[fn 2] and the auditor uses that specialist's work as evidential matter in performing substantive tests to evaluate material financial statement assertions.
- c. The auditor engages a specialist and uses that specialist's work as evidential matter in performing substantive tests to evaluate material financial statement assertions.

.04 The guidance provided in this section applies to audits of financial statements prepared in conformity with generally accepted accounting principles (GAAP)^[fn 3] and to engagements performed under [section 623](#), *Special Reports*, including a comprehensive basis of accounting other than GAAP.

.05 *[The following paragraph is effective for audits of fiscal years beginning on or after December 15, 2010. See PCAOB Release 2010-004.]*

This section does not apply to situations in which a specialist employed by the auditor's firm participates in the audit. Auditing Standard No. 10, *Supervision of the Audit Engagement*, applies in those situations.

Decision to Use the Work of a Specialist

.06[The following paragraph is effective for audits of fiscal years beginning on or after December 15, 2010. See PCAOB Release 2010-004.]

The auditor's education and experience enable him or her to be knowledgeable about business matters in general, but the auditor is not expected to have the expertise of a person trained for or qualified to engage in the practice of another profession or occupation. During the audit, however, an auditor may encounter complex or subjective matters potentially material to the financial statements. Such matters may require special skill or knowledge and in the auditor's judgment require using the work of a specialist to obtain appropriate evidential matter.

.07 Examples of the types of matters that the auditor may decide require him or her to consider using the work of a specialist include, but are not limited to, the following:

- a. Valuation (for example, special-purpose inventories, high-technology materials or equipment, pharmaceutical products, complex financial instruments, real estate, restricted securities, works of art, and environmental contingencies)
- b. Determination of physical characteristics relating to quantity on hand or condition (for example, quantity or condition of minerals, mineral reserves, or materials stored in stockpiles)
- c. Determination of amounts derived by using specialized techniques or methods (for example, actuarial determinations for employee benefits obligations and disclosures, and determinations for insurance loss reserves^(fn 4))
- d. Interpretation of technical requirements, regulations, or agreements (for example, the potential significance of contracts or other legal documents or legal title to property)

Qualifications and Work of a Specialist

.08 The auditor should consider the following to evaluate the professional qualifications of the specialist in determining that the specialist possesses the necessary skill or knowledge in the particular field:

- a. The professional certification, license, or other recognition of the competence of the specialist in his or her field, as appropriate
- b. The reputation and standing of the specialist in the views of peers and others familiar with the specialist's capability or performance
- c. The specialist's experience in the type of work under consideration

.09 The auditor should obtain an understanding of the nature of the work performed or to be performed by the specialist.

This understanding should cover the following:

- a. The objectives and scope of the specialist's work
- b. The specialist's relationship to the client (see paragraphs .10 and .11)
- c. The methods or assumptions used
- d. A comparison of the methods or assumptions used with those used in the preceding period
- e. The appropriateness of using the specialist's work for the intended purpose^[fn 5]
- f. The form and content of the specialist's findings that will enable the auditor to make the evaluation described in paragraph .12

Relationship of the Specialist to the Client

.10 The auditor should evaluate the relationship^[fn 6] of the specialist to the client, including circumstances that might impair the specialist's objectivity. Such circumstances include situations in which the client has the ability—through employment, ownership, contractual right, family relationship, or otherwise—to directly or indirectly control or significantly influence the specialist.

.11 When a specialist does not have a relationship with the client, the specialist's work usually will provide the auditor with greater assurance of reliability. However, the work of a specialist who has a relationship with the client may be acceptable under certain circumstances. If the specialist has a relationship with the client, the auditor should assess the risk that the specialist's objectivity might be impaired. If the auditor believes the relationship might impair the specialist's objectivity, the auditor should perform additional procedures with respect to some or all of the specialist's assumptions, methods, or findings to determine that the findings are not unreasonable or should engage another specialist for that purpose.

Using the Findings of the Specialist

.12 The appropriateness and reasonableness of methods and assumptions used and their application are the responsibility of the specialist. The auditor should (a) obtain an understanding of the methods and assumptions used by the specialist, (b) make appropriate tests of data provided to the specialist, taking into account the auditor's assessment of control risk, and (c) evaluate whether the specialist's findings support the related assertions in the financial statements. Ordinarily, the auditor would use the work of the specialist unless the auditor's procedures lead him or her to believe the findings are unreasonable in the circumstances. If the auditor believes the findings are unreasonable, he or she should apply additional procedures, which may include obtaining the opinion of another specialist.

Effect of the Specialist's Work on the Auditor's Report

.13*[The following paragraph is effective for audits of fiscal years beginning on or after December 15, 2010. See PCAOB Release 2010-004.]*

If the auditor determines that the specialist's findings support the related assertions in the financial statements, he or she reasonably may conclude that sufficient appropriate evidential matter has been obtained. If there is a material difference between the specialist's findings and the assertions in the financial statements, he or she should apply additional procedures. If after applying any additional procedures that might be appropriate the auditor is unable to resolve the matter, the auditor should obtain the opinion of another specialist, unless it appears to the auditor that the matter cannot be resolved. A matter that has not been resolved ordinarily will cause the auditor to conclude that he or she should qualify the opinion or disclaim an opinion because the inability to obtain sufficient appropriate evidential matter as to an assertion of material significance in the financial statements constitutes a scope limitation. (See section 508, *Reports on Audited Financial Statements*, paragraphs .22 and .23.)

.14 The auditor may conclude after performing additional procedures, including possibly obtaining the opinion of another specialist, that the assertions in the financial statements are not in conformity with GAAP. In that event, the auditor should express a qualified or adverse opinion. (See section 508.35, .36, and .41.)

Reference to the Specialist in the Auditor's Report

.15 Except as discussed in paragraph .16, the auditor should not refer to the work or findings of the specialist. Such a reference might be misunderstood to be a qualification of the auditor's opinion or a division of responsibility, neither of which is intended. Further, there may be an inference that the auditor making such reference performed a more thorough audit than an auditor not making such reference.

.16 The auditor may, as a result of the report or findings of the specialist, decide to add explanatory language to his or her standard report or depart from an unqualified opinion. Reference to and identification of the specialist may be made in the auditor's report if the auditor believes such reference will facilitate an understanding of the reason for the explanatory paragraph or the departure from the unqualified opinion.

Effective Date

.17 This section is effective for audits of periods ending on or after December 15, 1994. Early application of the provisions of this section is encouraged.

AU Section 9336 — Using the Work of a Specialist: Auditing Interpretations of

Source: Auditing Standard Nos. 8–15.

1. The Use of Legal Interpretations As Evidential Matter to Support Management's Assertion

That a Transfer of Financial Assets Has Met the Isolation Criterion in Paragraph 9(a) of Financial Accounting Standards Board Statement No. 140

.01Introduction—Financial Accounting Standards Board (FASB) Statement No. 140,^[fn 1] *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*, requires that a transferor of financial assets must surrender control over the financial assets to account for the transfer as a sale. Paragraph 9(a) states one of several conditions that must be met to provide evidence of surrender of control:

The transferred assets have been isolated from the transferor—put presumptively beyond the reach of the transferor and its creditors, even in bankruptcy or other receivership.

Paragraph 27 of FASB Statement No. 140 describes in greater detail the evidence required to support management's assertion that transferred financial assets have been isolated:

The nature and extent of supporting evidence required for an assertion in financial statements that transferred financial assets have been isolated—put presumptively beyond the reach of the transferor and its creditors, either by a single transaction or a series of transactions taken as a whole—depend on the facts and circumstances. All available evidence that either supports or questions an assertion shall be considered. That consideration includes making judgments about whether the contract or circumstances permit the transferor to revoke the transfer. It also may include making judgments about the kind of bankruptcy or other receivership into which a transferor or SPE might be placed, whether a transfer of financial assets would likely be deemed a true sale at law, whether the transferor is affiliated with the transferee, and other factors pertinent under applicable law. Derecognition of transferred assets is appropriate only if the available evidence provides reasonable assurance that the transferred assets would be beyond the reach of the powers of a bankruptcy trustee or other receiver for the transferor or any consolidated affiliate of the transferor that is not a special-purpose corporation or other entity designed to make remote the possibility that it would enter bankruptcy or other receivership.

A determination about whether the isolation criterion has been met to support a conclusion regarding surrender of control is largely a matter of law. This aspect of surrender of control, therefore, is assessed primarily from a legal perspective.

.02Effective Date and Applicability—This interpretation is effective for auditing procedures related to transfers of financial assets that are required to be accounted for under FASB Statement No. 140, as amended by FASB Technical Bulletin (FTB) No. 01-1, *Effective Date for Certain Financial Institutions of Certain Provisions of Statement 140 Related to the Isolation of Transferred Financial Assets*.^[fn 2]

.03Question—What should the auditor consider in determining whether to use the work of a legal specialist^[fn 3] to obtain persuasive evidence to support management's assertion that a transfer of financial assets meets the isolation criterion of FASB Statement No. 140?

.04[The following paragraph is effective for audits of fiscal years beginning on or after December 15, 2010. See PCAOB Release 2010-004.]

Interpretation—Section 336, *Using the Work of a Specialist*, paragraph .06, states that "during the audit...an auditor may encounter complex or subjective matters potentially material to the financial statements. Such matters may require special skill or knowledge and in the auditor's judgment require using the work of a specialist to obtain

appropriate evidential matter."

.05*[The following paragraph is effective for audits of fiscal years beginning on or after December 15, 2010. See PCAOB Release 2010-004.]*



Use of a legal specialist may not be necessary to obtain appropriate evidential matter to support management's assertion that the isolation criterion is met in certain situations, such as when there is a routine transfer of financial assets that does not result in any continuing involvement by the transferor.^(In 4)

.06 Many transfers of financial assets involve complex legal structures, continuing involvement by the transferor, or other legal issues that, in the auditor's judgment, make it difficult to determine whether the isolation criterion is met. In these situations, use of a legal specialist usually is necessary. A legal specialist formulating an opinion as to whether a transfer isolates the transferred assets beyond the reach of the transferor and its creditors may consider, among other things, the structure of the transaction taken as a whole, the nature of any continuing involvement, the type of insolvency or other receivership proceedings to which the transferor might become subject, and other factors pertinent under applicable law.



.07 If a legal opinion is used as evidence to support the accounting conclusion related to multiple transfers under a single structure, and such transfers occur over an extended period of time under that structure, the auditor should evaluate the need for management to obtain periodic updates of that opinion to confirm that there have been no subsequent changes in relevant law or applicable regulations that may change the applicability of the previous opinion to such transfers. The auditor also should evaluate the need for management to obtain periodic updates of an opinion to confirm that there have been no subsequent changes in relevant law or applicable regulations that may affect the conclusions reached in the previous opinion in the case of other transfers (see paragraph 55 of FASB Statement No. 140).



.08 If management's assertion with respect to a new transaction is that the transaction structure is the same as a prior structure for which a legal opinion that complies with this interpretation was used as evidence to support an assertion that the transfer of assets met the isolation criterion, the auditor should evaluate the need for management to obtain an update of that opinion to confirm that there have been no changes in relevant law, applicable regulations, or in the pertinent facts of the transaction that may affect the applicability of the previous opinion to the new transaction.



.09*Question*—If the auditor determines that the use of a legal specialist is required, what should he or she consider in assessing the adequacy of the legal opinion?



.10*Interpretation*—In assessing the adequacy of the legal opinion, the auditor should consider whether the legal specialist has experience with relevant matters, including knowledge of the U.S. Bankruptcy Code, and other federal, state, or foreign law, as applicable, as well as knowledge of the transaction upon which management's assertion is based. For transactions that may be affected by provisions of the Federal Deposit Insurance Act, the auditor should consider whether the legal specialist has experience with the rights and powers of receivers, conservators, and liquidating agents under that Act. The auditor should obtain an understanding of the assumptions that are used by the legal specialist, and make appropriate tests of any information that management provides to the legal specialist and upon which the specialist indicates it relied. For example, testing management's information underlying a legal specialist's assumption regarding the adequacy of consideration received may depend on the nature of the transaction and the relationship of the parties. When the legal specialist's opinion has assumed the adequacy of consideration for transfers from a particular legal entity to its wholly owned subsidiary, changes in the subsidiary's capital accounts plus other consideration generally would be sufficient audit evidence as to the adequacy of consideration. In the case of other transfers, such as those that are not

a wholly owned subsidiary of a particular legal entity that is the transferor, obtaining additional audit evidence may be necessary to evaluate management's assertion with regard to the adequacy of consideration upon which the legal specialist relied, because changes in the transferee's capital accounts do not solely benefit the transferring entity.

.11 [The following paragraph is effective for audits of fiscal years beginning on or after December 15, 2010. See PCAOB Release 2010-004.]

The auditor also should consider the form and content of the documentation that the legal specialist provides and evaluate whether the legal specialist's findings support management's assertions with respect to the isolation criterion. Section 336.13 states that "if the auditor determines that the specialist's findings support the related assertions in the financial statements, he or she reasonably may conclude that sufficient appropriate evidential matter has been obtained." FASB Statement No. 140's requirement regarding reasonable assurance that the transferred assets would be isolated provides the basis for what auditors should consider in evaluating the work of a legal specialist.

.12 Findings of a legal specialist that relate to the isolation of transferred financial assets are often in the form of a reasoned legal opinion that is restricted to particular facts and circumstances relevant to the specific transaction. The reasoning of such opinion may rely upon analogy to legal precedents that may not involve facts and circumstances that are comparable to that specific transaction. The auditor also should consider the effect of any limitations or disclaimers of opinion in assessing the adequacy of any legal opinion.

.13 An example of the conclusions in a legal opinion for an entity that is subject to the U.S. Bankruptcy Code that provides persuasive evidence, in the absence of contradictory evidence, to support management's assertion that the transferred financial assets have been put presumptively beyond the reach of the entity and its creditors, even in bankruptcy or other receivership, follows:

"We believe (or it is our opinion) that in a properly presented and argued case, as a legal matter, in the event the Seller were to become a Debtor, the transfer of the Financial Assets from the Seller to the Purchaser would be considered to be a sale (or a true sale) of the Financial Assets from the Seller to the Purchaser and not a loan and, accordingly, the Financial Assets and the proceeds thereof transferred to the Purchaser by the Seller in accordance with the Purchase Agreement would not be deemed to be property of the Seller's estate for purposes of [the relevant sections] of the U.S. Bankruptcy Code."

The following additional paragraph addressing substantive consolidation applies when the entity to which the assets are sold (as described in the opinion) is an affiliate of the selling entity and may also apply in other situations as noted by the legal specialist. For example, if a so-called "two-step" structure has been used to achieve isolation, this paragraph usually will be required with respect to the transferee in the first step of such structure (see paragraph .15 and related footnotes for additional guidance on the second step of a two-step structure as described in paragraph 83 of FASB Statement No. 140). When the transferor has entered into transactions with an affiliate that the issue of substantive consolidation, the opinion should address the effect of that involvement on the

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"Based upon the assumptions of fact and the discussion set forth above, and on a reasoned analysis of analogous case law, we are of the opinion that in a properly presented and argued case, as a legal matter, in a proceeding under the U.S. Bankruptcy Code,^[fn 5] in which the Seller is a Debtor, a court would not grant an order consolidating the assets and liabilities of the Purchaser with those of the Seller in a case involving the

insolvency of the Seller under the doctrine of substantive consolidation."

In the case of a transferor that is not entitled to become a debtor under the U.S. Bankruptcy Code, a legal opinion regarding whether the isolation criterion is met would consider whether isolation is satisfactorily achieved under the insolvency or receivership laws that apply to the transferor.

.¹⁴ Following are two examples of the conclusions in a legal opinion for an entity that is subject to receivership or conservatorship under provisions of the Federal Deposit Insurance Act. The conclusions in these two examples provide persuasive evidence, in the absence of contradictory evidence, to support management's assertion that the transferred financial assets have been put presumptively beyond the reach of the entity and its creditors, even in conservatorship or receivership. Insolvency and receivership laws applicable to depository institutions, and how those laws affect the legal isolation criterion, differ depending upon the nature of the depository institution and its chartering authority. Accordingly, legal opinions addressing the legal isolation criterion may be formulated in different ways to accommodate those differences.^[fn 6]



Example 1: "*We believe (or it is our opinion) that in a properly presented and argued case, as a legal matter, in the event the Seller were to become subject to receivership or conservatorship, the transfer of the Financial Assets from the Seller to the Purchaser would be considered to be a sale (or a true sale) of the Financial Assets from the Seller to the Purchaser and not a loan and, accordingly, the Financial Assets and the proceeds thereof transferred to the Purchaser by the Seller in accordance with the Purchase Agreement would not be deemed to be property of, or subject to repudiation, reclamation, recovery, or recharacterization by, the receiver or conservator appointed with respect to the Seller.*"^[fn 7]

Example 2: "The Federal Deposit Insurance Corporation (FDIC) has issued a regulation, 'Treatment by the Federal Deposit Insurance Corporation as Conservator or Receiver of Financial Assets Transferred by an Insured Depository Institution in Connection with a Securitization or Participation,' 12 CFR section 360.6 (the Rule). Based on and subject to the discussion, assumptions, and qualifications herein, it is our opinion that:

A. Following the appointment of the FDIC as the conservator or receiver for the Bank:

(i) The Rule will apply to the Transfers,

(ii) Under the Rule, the FDIC acting as conservator or receiver for the Bank could not, by exercise of its authority to disaffirm or repudiate contracts under 12 U.S.C. §1821(e), reclaim or recover the Transferred Assets from the Issuer or recharacterize the Transferred Assets as property of the Bank or of the conservatorship or receivership for the Bank,

(iii) Neither the FDIC (acting for itself as a creditor or as representative of the Bank or its shareholders or creditors) nor any creditor of the Bank would have the right, under any bankruptcy or insolvency law applicable in the conservatorship or receivership of the Bank, to avoid the Transfers, to recover the Transferred Assets, or to require the Transferred Assets to be turned over to the FDIC or such creditor, and

(iv) There is no other power exercisable by the FDIC as conservator or receiver for the Bank that would permit the FDIC as such conservator or receiver to reclaim or recover the Transferred Assets from the Issuer, or to recharacterize the Transferred Assets as property of the Bank or of the conservatorship or receivership for the Bank; provided, however, that we offer no opinion as to whether, in receivership, the FDIC or any creditor of the Bank may take any such actions if the Holders [*holders of beneficial interests in the transferred assets*] receive payment of the principal amount of the Interests and the interest earned thereon (at the

contractual yield) through the date the Holders are so paid; and

B. Prior to the appointment of the FDIC as conservator or receiver for the Bank, the Bank and its other creditors would not have the right to reclaim or recover the Transferred Assets from the Issuer, except by the exercise of a contractual provision [insert appropriate citation] to require the transfer, or return, of the Transferred Assets that exists solely as a result of the contract between the Bank and the Issuer."^[fn 8]

The following additional paragraph addressing substantive consolidation applies when the entity to which the assets are sold or transferred (as described in the opinion) is an affiliate of the selling entity and may also apply in other situations as noted by the legal specialist.^[fn 9] For example, if a so-called two-step structure has been used to achieve isolation, the following paragraph usually will be required with respect to the transferee in the first step of the structure (see paragraph .15 and related footnotes for additional guidance on the second step of a two-step structure as described in paragraph 83 of FASB Statement No. 140). When the transferor has entered into transactions with an affiliate that could affect the issue of substantive consolidation, the opinion should address the effect of that involvement on the opinion.

"Based upon the assumptions of fact and the discussion set forth above, and on a reasoned analysis of analogous case law, *we are of the opinion that* in a properly presented and argued case, as a legal matter, in a receivership, conservatorship, or liquidation proceeding in respect of the Seller, a court *would not* grant an order consolidating the assets and liabilities of the Purchaser with those of the Seller."

Certain powers to repudiate contracts, recover, reclaim, or recharacterize transferred assets as property of a transferor that are exercisable by the FDIC under the Federal Deposit Insurance Act may, as of the date of the transfer, be limited by a regulation that may be repealed or amended only in respect of transfers occurring on or after the effective date of such repeal or amendment.^[fn 10] With respect to the powers of a receiver or conservator that may not be exercised under that regulation, it is acceptable for attorneys to rely upon the effectiveness of the limitation on such powers set forth in the applicable regulation, provided that the attorney states, based on reasonable assumptions, that: (1) the affected transfer of financial assets meets all qualification requirements of the regulation, and (2) the regulation had not, as of the date of the opinion, been amended, repealed, or held inapplicable by a court with jurisdiction with respect to such transfer. The opinion should separately address any powers of repudiation, recovery, reclamation, or recharacterization exercisable by a receiver or conservator notwithstanding that regulation (for example, rights, powers, or remedies regarding transfers specifically excluded from the regulation) in a manner that provides the same level of assurance as would be provided in the case of opinions that conform with requirements of paragraph .13, except that such opinion shall address powers arising under the Federal Deposit Insurance Act. The considerations in the immediately preceding three sentences are adequately addressed either by the example 1 opinion or the example 2 opinion described in this paragraph or by the variations described in the second paragraph of footnote 8 and in footnote 9.

.15[The following paragraph is effective for audits of fiscal years beginning on or after December 15, 2010. See PCAOB Release 2010-004.]



A legal letter that includes an inadequate opinion, inappropriate limitations, or a disclaimer of opinion, or that effectively limits the scope of the opinion to facts and circumstances that are not applicable to the transaction, does not provide persuasive evidence to support the entity's assertion that the transferred assets have been put presumptively beyond the reach of the transferor and its creditors, even in bankruptcy or other receivership. Likewise, a legal letter that includes conclusions that are expressed using some of the following language would not provide persuasive evidence that a transfer of financial assets has met the isolation criterion of FASB Statement No. 140 (see paragraphs .20 and .21 of this interpretation):

- "We are unable to express an opinion..."
- "It is our opinion, based upon limited facts..."
- "We are of the view..." or "it appears..."
- "There is a reasonable basis to conclude that..."
- "In our opinion, the transfer would *either* be a sale *or* a grant of a perfected security interest..."^(fn 11)
- "In our opinion, there is a reasonable possibility..."
- "In our opinion, the transfer *should* be considered a sale..."
- "It is our opinion that the company will be able to assert meritorious arguments..."
- "In our opinion, it is more likely than not ..."
- "In our opinion, the transfer would *presumptively* be..."
- "In our opinion, it is probable that..."

Furthermore, conclusions about hypothetical transactions may not be relevant to the transaction that is the subject of management's assertions. Paragraph 6 of Auditing Standard No. 15, *Audit Evidence*, states, "[t]o be appropriate, audit evidence must be both relevant and reliable in providing support for the conclusions on which the auditor's opinion is based." Additionally, conclusions about hypothetical transactions may not contemplate all of the facts and circumstances or the provisions in the agreements of the transaction that is the subject of management's assertions, and generally would not provide persuasive evidence.^(fn 12)

.16 Question—Are legal opinions that restrict the use of the opinion to the client, or to third parties other than the auditor, acceptable audit evidence?



.17 Interpretation—No. Footnote 5 to section 336.09 states: "In some cases, the auditor may decide it is necessary to contact the specialist to determine that the specialist is aware that his or her work will be used for evaluating the assertions in the financial statements." Given the importance of the legal opinion to the assertion in this case, and the precision that legal specialists use in drafting such opinions, an auditor should not use as evidence a legal opinion that he or she deems otherwise adequate if the letter restricts use of the findings expressed therein to the client or to third parties other than the auditor. In that event, the auditor should request that the client obtain the legal specialist's written permission for the auditor to use the opinion for the purpose of evaluating management's assertion that a transfer of financial assets meets the isolation criterion of FASB Statement No. 140.



.18 An example of a letter from a legal specialist to a client that adequately communicates permission for the auditor to use the legal specialist's opinion for the purpose of evaluating management's assertion that a transfer of financial assets meets the isolation criterion of FASB Statement No. 140 is as follows:



"Notwithstanding any language to the contrary in our opinions of even date with respect to certain bankruptcy issues relating to the above-referenced transaction, you are authorized to make available to your auditors such

opinions solely as evidential matter in support of their evaluation of management's assertion that the transfer of the receivables meets the isolation criterion of FASB Statement No. 140, provided a copy of this letter is furnished to them in connection therewith. In authorizing you to make copies of such opinions available to your auditors for such purpose, we are not undertaking or assuming any duty or obligation to your auditors or establishing any lawyer-client relationship with them. Further, we do not undertake or assume any responsibility with respect to financial statements of you or your affiliates."^[fn 13]

.19 A letter from a legal specialist to a client might authorize the client to make copies of the legal opinion available to the auditor to use in his or her evaluation of management's assertion that a transfer of financial assets meets the isolation criterion of FASB Statement No. 140, but then state that the auditor is not authorized to rely thereon. Such "use but not rely on" language, or other language that similarly restricts the auditor's use of the legal specialist's opinion, does not adequately communicate permission for the auditor to use the legal specialist's opinion as evidential matter. The auditor may wish to consult with his or her legal counsel in circumstances where it is not clear that the auditor may use the legal specialist's opinion.

.20 *Question*—If the auditor determines that it is appropriate to use the work of a legal specialist, and either the resulting legal response does not provide persuasive evidence that a transfer of assets has met the isolation criterion, or the legal specialist does not grant permission for the auditor to use a legal opinion that is restricted to the client or to third parties other than the auditor, what other steps might an auditor consider?

.21 *Interpretation*—When other relevant evidential matter exists, the auditor should consider it before reaching a conclusion about the appropriateness of management's accounting for a transfer.^[fn 14] However, since the isolation aspect of surrender of control is assessed primarily from a legal perspective, the auditor usually will not be able to obtain persuasive evidence in a form other than a legal opinion. In the absence of persuasive evidence that a transfer has met the isolation criterion, derecognition of the transferred assets is not in conformity with generally accepted accounting principles and the auditor should consider the need to express a qualified or adverse opinion in accordance with section 508, *Reports on Audited Financial Statements*, paragraphs .35 through .60. However, if permission for the auditor to use a legal opinion that he or she deems otherwise adequate is not granted, this would be a scope limitation and the auditor should consider the need to express a qualified opinion or to disclaim an opinion in accordance with section 508.22–26 and 508.61–63.

[Issue Date: December, 2001.]

Footnotes

fn 1 Because income taxes and information technology are specialized areas of accounting and auditing, this section does not apply to situations in which an income tax specialist or information technology specialist participates in the audit. Auditing Standard No. 10, *Supervision of the Audit Engagement*, applies in those situations. [Footnote revised, effective for audits of fiscal years beginning on or after December 15, 2010. See PCAOB Release 2010-004.] [\[back\]](#)

fn 2 The auditor should consider the effect, if any, that using the work of a specialist employed by the auditor's firm has on independence. [\[back\]](#)

fn 3 References in this section to "financial statements" and to "generally accepted accounting principles" include special reports covered under section 623, *Special Reports*. [\[back\]](#)

fn 4 In the specific situation involving the audit of an insurance entity's loss reserves, an outside loss reserve specialist—that is, one who is not an employee or officer of the insurance entity—should be used. When the auditor has the requisite knowledge and experience, the auditor may serve as the loss reserve specialist. (See Statement of Position 92-4, *Auditing Insurance Entities' Loss Reserves*.) [\[back\]](#)

fn 5 In some cases, the auditor may decide it is necessary to contact the specialist to determine that the specialist is aware that his or her work will be used for evaluating the assertions in the financial statements. [\[back\]](#)

fn 6 The term *relationship* includes, but is not limited to, those situations meeting the definition of "related parties" contained in the financial reporting framework applicable to the company under audit. *[Footnote revised, effective for audits of fiscal years beginning on or after December 15, 2014. See PCAOB Release 2014-002.]* [\[back\]](#)

fn 1 Financial Accounting Standards Board (FASB) Statement No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*, is a replacement of FASB Statement No. 125 and is effective for transfers and servicing of financial assets and extinguishments of liabilities occurring after March 31, 2001, except as provided in paragraphs 19–25 of FASB Statement No. 140 as amended by FASB Technical Bulletin (FTB) No. 01-1, *Effective Date for Certain Financial Institutions of Certain Provisions of Statement 140 Related to the Isolation of Transferred Financial Assets*. [\[back\]](#)

fn 2 FTB No. 01-1 amends FASB Statement No. 140 to change the effective date for paragraphs 9(a), 27, 28, and 80–84 of FASB Statement No. 140 for transfers of financial assets by certain financial institutions. Paragraphs 6–8 of FTB No. 01-1 also provide additional transition time for transfers by financial institutions to certain master trusts. [\[back\]](#)

fn 3 Client's internal or external attorney who is knowledgeable about relevant sections of the U.S. Bankruptcy Code and other federal, state, or foreign laws, as applicable. [\[back\]](#)

fn 4 FASB Emerging Issues Task Force Topic No. D-99, *Questions and Answers Related to Servicing Activities in a Qualifying Special-Purpose Entity under FASB Statement No. 140*, characterizes *no* continuing involvement with the transferred assets as "no servicing responsibilities, no participation in future cash flows, no recourse obligations other than standard representations and warranties that the financial assets transferred met the delivery requirements under the arrangement, no further involvement of any kind." If a contractual provision (such as a call or removal of accounts provision) gives the transferor the unilateral ability to require the return of specific financial assets, the auditor should consider the effect of paragraph 9(c) of FASB Statement No. 140. [\[back\]](#)

fn 5 For an entity subject to additional regulation (e.g., a broker-dealer subject to the Securities Investor Protection Act), the legal opinion also generally should address the effect of such regulation and the policies of the regulators implementing such regulations (e.g., the Securities Investor Protection Corporation). [\[back\]](#)

fn 6 For an entity subject to conservatorship or liquidation under the National Credit Union Act, the examples and discussion in this paragraph would be modified to make appropriate references to "liquidation" and "liquidating agent" and additional information relating to rights and regulations of the National Credit Union Administration. [\[back\]](#)

fn 7 When the opinion indicates that isolation is achieved without reference to a true sale, the opinion also should provide reasonable assurance that the transferred assets are beyond the reach of the transferor and its creditors other than the transferee to the same extent that is provided in example 2, paragraph B. [\[back\]](#)

fn 8 See the second paragraph of footnote 4. [\[back\]](#)

Paragraph B is not required if the opinion includes both a conclusion, as set forth in example 1, that the transfer constitutes a "true sale" and the conclusions set forth of example 2, paragraph A. It is not necessary to include any provision of example 2 if the opinion is as set forth in example 1.

fn 9 An additional substantive consolidation opinion is not required if the opinion states that its conclusion includes the inability to recover the transferred financial assets or recharacterize the transfer by application of the doctrine of "substantive consolidation." [\[back\]](#)

fn 10 The applicable regulation is 12 CFR section 360.6, effective September 11, 2000. [\[back\]](#)

fn 11 Certain transferors are subject only to receivership (and not to proceedings under the U.S. Bankruptcy Code or the Federal Deposit Insurance Act) under laws that do not allow a receiver to reach assets in which a security interest has been granted. In such circumstances, an opinion that concludes that the transfer would either be a sale or a grant of a security interest that puts the transferred assets beyond the reach of such receiver and other creditors would provide persuasive evidence that the isolation criterion is met. In certain circumstances, a legal specialist may provide an opinion on both steps of a two-step structure. Such language would be acceptable in an opinion for a transfer of assets in the second step of a two-step structure as described in paragraph 83 of FASB Statement No. 140 provided that the opinion on the transfer in the first step is consistent with paragraphs 13 or 14 of this interpretation. [\[back\]](#)

fn 12 For example, a memorandum of law from a legal specialist usually analyzes (and may make conclusions about) a transaction that may be completed subsequently. Such memorandum generally would not provide persuasive evidence unless the conclusions conform with this interpretation and a legal specialist opines that such conclusions apply to a completed transaction that is the subject of management's assertion. [\[back\]](#)

fn 13 This language may appear in the legal specialist's opinion rather than in a separate letter. In that case, the wording would be modified slightly to indicate the context. [\[back\]](#)

fn 14 See section 336.13 as to additional procedures that may be applied. [\[back\]](#)