

# Audits are a Journey: We'll Guide the Way

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# Audits are a Journey We'll Guide the Way

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# Learning Objectives

#1

Understand recent and upcoming:

- Accounting Standard Updates (ASU)
- Statement on Audit Standards (SAS) updates

#2

Discuss common and expected impacts

#3

Build better, lasting relationships with those *DREADED* auditors!!



# Recent ASUs

- ASC 820 - Contractual Restrictions on Fair Value of Equity Securities

# Upcoming ASUs

- Update 2025 -06, Intangibles & Internal use software
- Update 2021 -10, Government Grants
- Update 2025 -08, CECL

# Recent ASC 820

## Effective 1/1/2025

### Contractual Restrictions on Fair Value of Equity Securities

- Insurance related funds
- If the restriction is considered part of the unit of account of the asset
  - Considered when measuring FV

## Considered a Unit of Account:

- Shares are issued through private placement
- Legally restricted until such shares are registered *OR* an exemption from registration is obtained

Impact on FV? **DEPENDS!**

- Nature and remaining duration of restriction
- Extent to which buyers are limited by restrictions
  - (large #'s of investors?)
- Qualitative & Quantitative factors!

## NOT Considered a Unit of Account:

- Eligible for sale on national securities exchange
- Over the counter market
- Contractual arrangements usually resulting from lock-up or market standoff agreements
- Specified period of time
- NO impact on FV!

# Upcoming 2025 -06

## Effective 1/1/2028

### Intangibles & Internal Use Software



## New Guidance!

Capitalization thresholds (contingent upon both)

- Management *(relevant authority)*, did they authorize?
- Probable the project will be completed? If so, what about for its intended purpose?
  - PROBABLE = 75%

# Intangibles & Internal Use Software

## Authorization & Funding

- Execution of a third-party contract
- Approval of expenditures for internal development
- Commitment to obtain software from a third party

## Capitalization continues until:

- Substantially complete
- Ready for intended use
- Generally, when all substantial testing is completed

“Is my project scoped  
into the new guidance?”

*....it DEPENDS!*

*.....it DEPENDS!*  
..... on WHAT!?



Entity's Business Activities

Nature of software in question

If a policy to ID "Software Projects" already exists

- **Significant development uncertainty  
(2 factors - *Judgement Required!*)**
  - Software being developed has technological innovations or novel, unique functions or features, and the uncertainty related to those technological innovations, functions, or features, if identified, has not been resolved through coding and testing
  - Significant performance requirements or the software have not been identified, or the identified significant performance requirements continue to be substantially revised

- **Capitalizable Costs - No Changes!**
  - Costs to obtain software from 3rd parties
  - Direct costs of materials and services to develop software
  - Payroll costs (included stock -based compensation) for employees directly associated with the project
  - Internal costs incurred while developing software
- **Expense as incurred**
  - G&A
  - Overhead
  - Data conversion/ migration/ personnel training

# Upcoming 2021-10 Government Grants

Single audits triggered at *\$1 million expended* (began 10/1/2024)

## New Guidance!

ASC 832 would require one of the following:

- Deferred Income
  - Used either for grants related to income or an asset
- Cost Accumulation
  - Used only for grants related to an asset

## Deferred Income

- Book deferral equal to cash received or expected
- “Recognize into earnings on a systematic & rational basis over the periods in which the entity recognizes as expenses the related costs for which the govt grant is intended to compensate”

## Cost Accumulation

- Monetary grants = Cost less Government Grant (rec'd or expected)
- Nonmonetary grants = Cost less Government Grant
- Subject to depreciation, impairment, etc. if a carrying value exists



# Upcoming ASC 326

## CECL

 **New Guidance!**

Early adoption permitted for annual or interim periods  
that have not been issued

**OR**

Apply prospectively beginning 1/1/2027

- Improve accounting for acquired PFAs & PCDs
- Includes all ***seasoned*** loan receivables (*no credit cards!*)
- Gross up approach! (*Purchase price + Initial ACL*)
- Interest method - recognition of amortization/accretion of premiums/discounts on ***seasoned*** loans (*no credit cards!*)
- **DOES NOT** include HTM debt securities!

**Seasoned = 90 days!**

- Option to remeasure ACL by combining *seasoned* loans & existing financial assets (with similar risk profiles)
  - Does not apply to DCF methodologies!
  - Make election at first FS date after initial recognition & measurement (not in the middle of a reporting period)
- *DO NOT* apply previous guidance for *seasoned* loans related to:
  - Accruing interest
  - Estimated expected recoveries

## Let's Discuss!

### BEFORE

- Gross up approach applied to PCDs
- PCDs required separation of discount rate & credit component
  - Credit piece - not accreted, added to PCD's purchase price
  - Offset included in ACL
- Non-PCD required provision on DAY 1
  - aka "*DOUBLE COUNT*"
- Non-PCDs required purchase discount accretion into interest income

### AFTER

- Loans acquired (NO CREDIT CARDS!)
  - Seasoned
- Singular approach between PCD and non-PCD PFAs
- Expected credit losses recorded directly to ACL on DAY 1 acquired loans
  - Eliminates "*DOUBLE COUNT*"
- Non-credit premium/discount amortized/accreted into interest income

# Recent SAS 145

## Effective 1/1/2024

### Auditor's Risk ID & Assessment Process

Updates include:

- Separate inherent and control risk assessments
- Assessing control risk at MAX
- Significant Risks - a **NEW**definition!
- Inherent risk factors and the risk spectrum
- Relevant assertions
- Significant classes of transactions, account balances, and disclosures
- Stand-back requirement
- Scalability
- System of internal controls
- Increasing complexity of entities and auditing
- Documentation requirements



## Separate Inherent and Control Risk Assessments

- Separate assessments were previously not required
- Now required to assess each risk separately at the *assertion level*

## Assessing Control Risk at MAX

- Not testing controls for operating effectiveness? MAX is ***REQUIRED***
- MAX is very common - regardless of control structure!

## Significant Risks - **NEW**Definition!

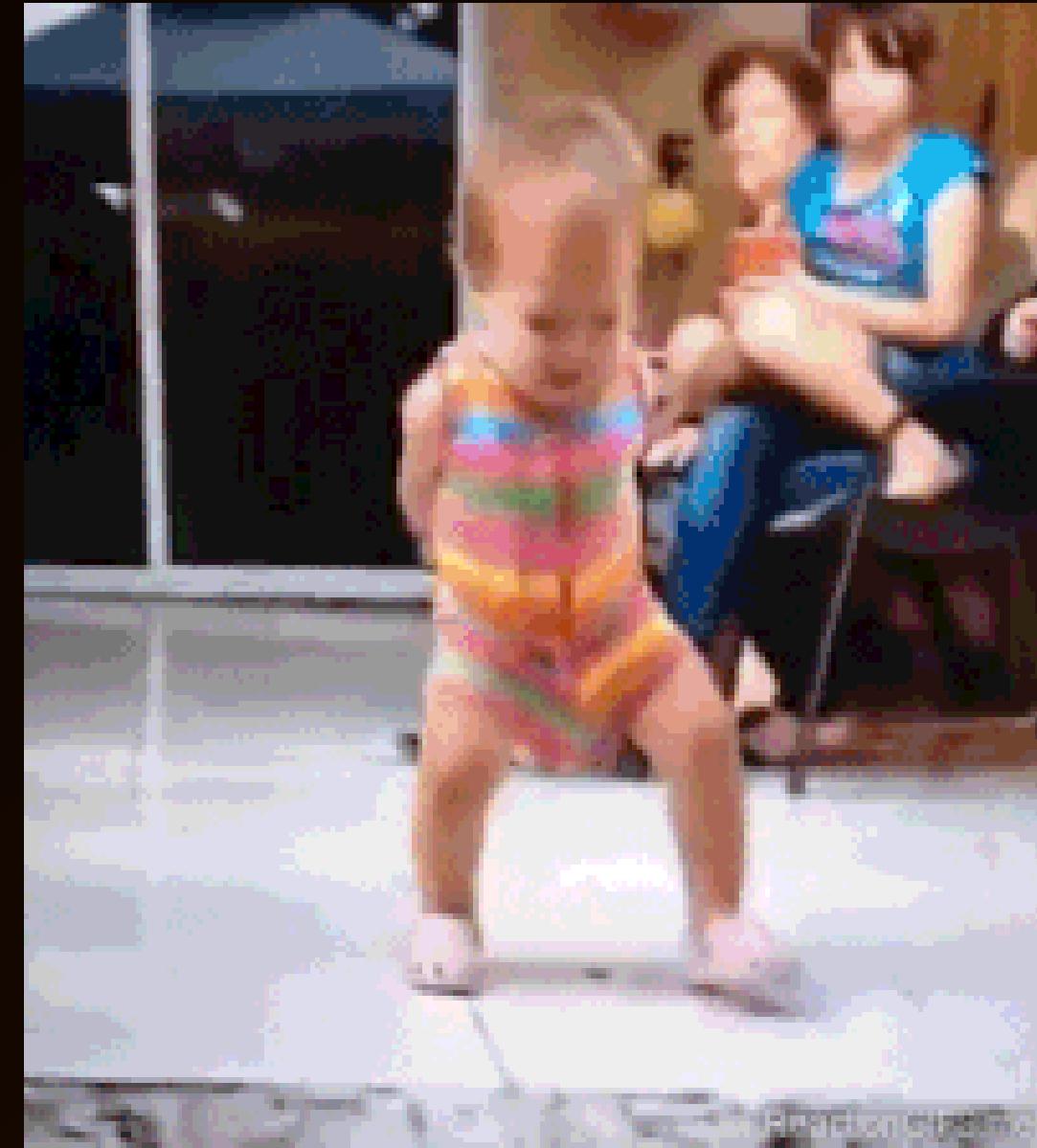
- Previous definition focused on the response to risk
- New definition focuses on the risk itself (*Risk of Material Misstatement - RMM*)

## Significant Risks - **NEW**Definition!

A significant risk is “*an identified risk of material misstatement for which the assessment of inherent risk is close to the upper end of the spectrum of inherent risk due to the degree to which inherent risk factors affect the combination of the likelihood of a misstatement occurring and the magnitude of the potential misstatement should that misstatement occur.*

# Significant Risks





Luau Baby!!!

## Inherent Risk Factors

- Conditions or events that could affect the susceptibility to misstatement.

Factors can be both *Qualitative or Quantitative*

- Complexity
- Subjectivity
- Change
- Uncertainty
- Risk of Material Misstatement
  - Management Bias!
  - Fraud!

- Is the risk close to the upper end of the spectrum for inherent risk?
- Is there reasonable possibility of material misstatement?

*Significant Risk!*

## Relevant Assertions

- When there is a *reasonable* possibility of a material misstatement
- Based on classes of transactions, account balances, and disclosures with an identified risk of material misstatement
- Update focuses on:
  - Likelihood of misstatement
  - Magnitude of misstatement

Account balance, significant class of transactions, disclosures - can be

***MATERIAL but NOT SIGNIFICANT***

## Scalability and Stand Back

- Size **DOES NOT** represent complexity!
- Increased scrutiny on verifying key controls! **NO MORE CORROBORATION!**
- Requires more detailed audit documentation

## *What does this mean for the Audit?*

- No requirement to verify controls when there is **NO RELEVANT ASSERTION**
- No requirement to substantively test when there is **NO RELEVANT ASSERTION**
- If you do test, why? Go back and reassess risk?

- **INCREASES IN AUDIT TIME RELATED TO RISK ASSESSMENT**



We didn't forget!

How can we help you build better, lasting  
relationships with those

*.....DREADED AUDITORS!*



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# Thank you!

**Feel free to contact us  
anytime.**