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# **GAO Hot Topics: What You Need to Know About Yellow Book, and More**

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## **2008 NASACT Training Forum**

**Pittsburgh, PA  
September 10, 2008**

**Marcia B. Buchanan**

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## **Session Objectives**

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- Highlight major revisions in the July 2007 Revision of the Yellow Book
  - Discuss the reasons for the changes and what these changes will mean for government auditors
  - Discuss GAO's future work in the area of independence and other topics
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## ***Government Auditing Standards July 2007 Revision***

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## **July 2007 Revision**

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- July 2007 Revision supersedes the 2003 Revision
    - Also available on the Yellow Book webpage
      - Listing of major changes from the 2003 Revision
      - Listing of technical changes from the January 2007 Revision
  - Implementation dates
    - For financial audits and attestation engagements, the standards are effective for audits of periods beginning on or after January 1, 2008
    - For performance audits, the standards are effective for audits beginning on or after January 1, 2008.
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## Overview of July 2007 Revision Chapters 1-3

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- Standardized language to define auditor requirements
  - Citing compliance with GAGAS
  - Using GAGAS with other professional standards
  - New chapter 2 – Ethical Principles in Government Auditing
  - Clarified and streamlined the discussion of nonaudit services
  - Incorporated the revised CPE requirements issued in 2005
  - Internal specialists who are part of the audit organization and perform as a member of the audit team should comply with CPE requirements
  - Added requirements for the audit organization’s system of quality control
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## Chapter 3: General Standards Continuing Professional Education

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- Incorporated the revised CPE requirements that were issued in April 2005 (GAO-05-568G) Under these requirements
    - All auditors should complete every 2 years at least 24 hours of CPE that relates to GAGAS
    - Auditors involved in planning, directing, or reporting on GAGAS assignments and all auditors who charge more than 20 percent or more of their time annually to GAGAS assignments, also should obtain at least an additional 56 hours of CPE that enhances the auditors’ professional proficiency to conduct audits
    - Clarified that auditors still are required to obtain 20 hours of CPE each year
  - Clarified CPE requirements to include internal specialists who are part of the audit organization and part of the team
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## Overview of July 2007 Revision Chapters 4-6

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- Updated for consistency with recent developments in financial auditing and internal control by aligning
    - Audit documentation with AICPA SAS No. 103, Audit Documentation
    - Definitions of internal control deficiencies with AICPA SAS No. 112, Communicating Internal Control Related Matters Identified in an Audit
  - Requirements for reporting on the restatement of previously-issued financial statements
  - Encouraged communication of significant concerns, uncertainties or other unusual or catastrophic events
  - Clarified and revised the description of attestation engagements
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## Overview of July 2007 Revision Chapters 7-8, Appendix

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- Overall framework for high-quality performance audits
    - Reasonable assurance, significance, and audit risk
  - Revised definition of performance audits (chapter 1)
  - Internal control that is significant within the context of the audit objectives
  - Information systems controls to assess audit risk and plan the audit within the context of the audit objectives
  - Overall assessment of the sufficiency and appropriateness of evidence
  - Subsequent discovery that reported findings or conclusions were not supported by sufficient, appropriate evidence
  - Enhanced GAGAS compliance statement for performance audits
  - Appendix to provide supplemental guidance
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## Yellow Book Professional Requirements Tool

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- Guidance to help auditors sort out the use of the terms “must” and “should”
  - Simple tabular format
  - Identifies the terms used by paragraph
  - Electronic PDF form
  - Can be used to document compliance with GAGAS
- Available on Yellow Book Web Page
- *Implementation Tool* GAO-08-210G, December 2007

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## Related Guidance that Accompanies the 2007 Revision

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- Guidance on GAGAS Requirements for Continuing Professional Education (GAO-05-568G, April 2005)
- Answers to Independence Questions (GAO-02-870G, July 2002)
- Available at <http://gao.gov/govaud/ybk01.htm>

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## Updates in Implementing Government Auditing Standards

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### Planned Projects

- Performance audit implementation guide
- GAGAS/IIA standards comparison (joint project with IIA)
- Crosswalk between GAGAS and INTOSAI standards
- Public sector perspectives for AICPA “clarified” standards
- Revise guidance documents in “clarity” format
- Revise Government Auditing Standards based on
  - Issues associated with independence
  - Revisions/issues raised by other standard setters

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## Current Work on Independence Issues

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## Overview of February 2008 Advisory Council Meeting

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- GAGAS Independence Standards and Guidance
    1. Independence Definitions/Independence in Fact and Appearance
    2. Conceptual Framework: Principles vs. Rules
    3. Future of “Answers to Independence Standard Questions.” (GAO-02-870G)
    4. Legislative Mandates/Firewalls
  
  - Management Representation Letters in Performance Audits
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## Overview of Current GAGAS Independence Standards

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- Organization and scope of GAGAS independence standards
    - Q&A addresses specific situations rather than a comprehensive approach, resulting in de facto rules
    - Q&A is dated and does not fully conform with the 2007 GAGAS
    - 2007 GAGAS recognizes ethical principles but does not provide a uniform approach for dealing with ethical issues
    - Other standard-setting bodies have made significant developments in the area of auditor independence since 2002
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## Independence Definitions/Independence in Fact and Appearance

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**Issues:**

- GAGAS does not explicitly define independence in appearance or the types of independence
  - Personal independence
  - External independence
  - Organizational independence
- Council also recommended discussing conflicts of interest

**Action items:**

- Add definitions to GAGAS
    - Independence in fact and in appearance
    - Types of independence
    - Conflicts of interest
    - Third parties
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## Conceptual Framework: Principles vs. Rules

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- A conceptual framework
  - provides a common risk-based approach, including threats and safeguards, for use in analyzing independence matters
  - requires the use of professional judgment

**Action items:**

- Continue working with AICPA and others on the conceptual framework
  - Begin re-writing/updating GAO's Independence Q&A
  - Update independence standard as necessary
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## Legislative Mandates/Firewalls

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**Issues:**

- Government auditors are sometimes mandated to perform nonaudit services
- These nonaudit services may impair the GAGAS organizational independence
- Some government auditors have suggested that organizational firewalls should be available as a means to allow them to provide required nonaudit services

**Action items:**

- Create guidance that includes criteria that would allow for the use of firewalls as an appropriate safeguard (“carve-out” option), and
  - provides elements required in the report disclosure
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## Re-Evaluating the Single Audit Process

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## Objectives

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- Present current issues, risks, and known problems regarding Single Audits as an accountability mechanism for federal programs.
- Discuss current actions in process by OMB, AICPA, and GAO intended to address the current issues and what this might mean for the Single Audit process of the future.

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## Recent Events

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- July 2007 PCIE Study on Single Audit Quality
- October 2007 Hearing – Senate Subcommittee on Federal Financial Management, Committee on Homeland Security and Governmental Affairs
- Establishment of Federal Workgroups and AICPA task forces
- AGA Partnership project – Leveraging Single Audits
- Ongoing GAO study and evaluation
- Ongoing Congressional interest and expectations

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## Evolution of Single Audit Act and Its Underlying Principles

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- Congress passed the Single Audit Act in response to concerns
    - that large amounts of federal financial assistance were not subject to audit and
    - that agencies sometimes overlapped on oversight activities
  
  - Objectives of the Single Audit Act:
    - promote sound financial management and effective internal control over federal awards
    - establish uniform requirements for audits of those awards
    - promote the efficient and effective use of audit resources
    - reduce burdens on grant recipients
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## PCIE Report and Recommendations

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- PCIE report presents compelling evidence that there continues to be a serious problem with single audit quality
  
  - PCIE report recommended a three-pronged approach to improving the quality of single audits:
    1. improving standards and guidance
    2. establishing continuing professional education as a prerequisite to conducting single audits
    3. enhancing the professional disciplinary processes for unacceptable audits
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## **GAO– Oct 2007 Testimony (GAO-08-213T)**

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- Actions must be taken to improve single audit quality and the related accountability over federal awards
  
  - There may be opportunities for
    - Considering size characteristics when implementing actions to improve single audit quality
    - Strengthening the cognizant agency oversight for larger auditees
  
  - Considering the recommendations of the PCIE within this larger context is important in achieving the proper balance between risk and cost-effective accountability
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## **Larger Effort To Review the Overall Framework**

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- Effort could include answering questions such as the following:
    - What types of simplified alternatives exist for meeting the accountability objectives for the smallest audits?
    - Is the current federal oversight structure adequate and consistent across federal agencies?
    - What alternative federal oversight structures could improve overall accountability and oversight in the single audit process?
    - What role can the auditing profession play in increasing single audit quality?
    - Do the specific requirements in Circular A-133, the compliance supplement, and/or the Single Audit Act need updating or streamlining?
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## Other Trends

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## High-Risk Series: An Update

- Added one new program (the 2010 Census) in March 2008--  
See *Information Technology: Significant Problems of Critical Automation Program Contribute to Risks Facing the 2010 Census* (GAO-08-550T, March 5, 2008)
- In January 2007, added 3 new high risk areas:
  - Financing the Nation's Transportation System
  - Ensuring the Effective Protection of Technologies Critical to U.S. National Security Interests
  - Transforming Federal Oversight of Food Safety
- In January 2007, removed 2 areas:
  - U.S. Postal Service's transformation efforts and long-term outlook
  - HUD's single-family mortgage insurance and rental housing assistance program
- See *High-Risk Series: An Update* (GAO-07-310, Jan. 2007)

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## Call for Stewardship: Tools for 21<sup>st</sup> Century Challenges

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- Establishes an approach to a top-to-bottom review of federal programs and policies
  - Meant to address issues raised in GAO's previously issued *21<sup>st</sup> Century Challenges: Reexamining the Base of the Federal Government*
  - Intended to help policymakers
    - Reach consensus on outcomes Americans want their government to achieve
    - Increase transparency and accountability
    - Better prioritize competing demands
    - Make more informed decisions
    - Modernize federal operations and management
  - *Call for Stewardship* GAO-08-93SP, December 17, 2007
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## Audit of the Federal Government's FY 2007 Consolidated Financial Statements

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- Statement of Social Insurance
    - Second year of presenting as a basic financial statement of the U.S. government
    - Was able to render an unqualified opinion on the statement
  - Certain material weaknesses in financial reporting and other limitations on the scope of its work resulted in conditions that prevented GAO from expressing an opinion on the federal government's accrual basis consolidated financial statements
  - Major impediments to an opinion
    - Serious financial management problems at the Department of Defense
    - Inability to adequately account for and reconcile intergovernmental activity and balances between federal agencies
    - Ineffective processes for preparing the consolidated financial statements
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## Measuring Natural Resources and Environmental Sustainability

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- Four broad criteria to use in determining the components of environmental accounting
    - Identifying the objectives of the accounts
    - Considering the availability and quality of data
    - Ensuring that accounts provide information on current natural wealth
    - Considering the timeliness and regularity with which accounts can be produced
  - *Measuring Our Nation's Natural Resources and Environmental Sustainability: Highlights of a Forum Jointly Convened by the Comptroller General of the United States and the National Academy of Science (GAO-08-127SP) October 24, 2007*
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## GAO's Accountability & Standards Team

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### We also get lots of help from:

- Bob Dacey, GAO Chief Accountant
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- Jennifer Allison, Advisory Council Administrator

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**GAO Hot Topics**

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Questions or Comments?

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**Where to Find the Yellow Book**

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- The Yellow Book is available on GAO's website at:

[www.gao.gov/govaud/ybk01.htm](http://www.gao.gov/govaud/ybk01.htm)

- For technical assistance, contact us at [yellowbook@gao.gov](mailto:yellowbook@gao.gov)