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

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**2009 NSAA Annual Conference**

**June 18, 2009  
Savannah, GA  
Marcia Buchanan, GAO**

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## **Session Objectives**

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- Highlight major revisions in the July 2007 Revision of the Yellow Book
  - Discuss guidance issued by GAO to assist auditors implement the July 2007 Yellow Book
  - Discuss GAO's current work in the standards area
  - Touch on GAO's work on single audit
  - Touch on GAO's work on Recovery Act
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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
    - A listing of technical changes from the January 2007 revision is posted to the yellow book web page
  - Effective date -- For financial audits and attestation engagements, the standards are effective for audits of periods beginning on or after January 1, 2008
  - Still contains 8 chapters
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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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## **Chapter 3: General Standards**

### **Audit Quality Control and Assurance**

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- Added a requirement that the quality control policies and procedures collectively address
  - Leadership responsibilities within the audit organization
  - Independence, legal, and ethical requirements
  - Initiation, acceptance, and continuance of audit and attestation engagements
  - Human resources
  - Audit and attestation performance, documentation, and reporting
  - Monitoring of quality

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## **Chapter 3: General Standards**

### **Audit Quality Control and Assurance**

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- Added requirements for
  - Audit organizations to analyze and summarize the results of monitoring procedures at least annually
    - Include identification of any systematic issues needing improvement
    - Include recommendations for corrective action

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## Chapter 3: General Standards

### Audit Quality Control and Assurance

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- External audit organizations to make peer review reports publicly available
  - Does not include letter of comment
  - Can be done by posting the peer review opinion on an external web site or to a publicly available file designed for public transparency of peer review results
- Internal audit organizations to provide a copy of the peer review report to those charged with governance
- Government audit organizations should also communicate the overall results and the availability of their external peer review reports to appropriate oversight bodies

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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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## **Implementation of Government Auditing Standards**

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### **Professional Requirement Tools to Assist Audit Organizations and Auditors in Implementing the July 2007 Revision of Government Auditing Standards**

GAO-08-210G, December 2007

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## Professional Requirements Tools

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- Contains 4 parts
    - General requirements for audit organizations
    - Specific requirements for financial audits
    - Specific requirements for attestation engagements
    - Specific requirements for performance audits
  - Guidance to help auditors sort out the use of the terms “must” and “should”
  - Available on Yellow Book Web Page
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## Professional Requirements Tools

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- For financial audits and attestation engagements, GAGAS incorporates
    - AICPA field work and reporting standards
      - The related Statements on Auditing Standards (SAS)
      - The related Statements on Standards for Attestation Engagements (SSAE)
  - Auditors need to comply with requirements in the AICPA standards in addition to the requirements listed in the tools
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## Professional Requirements Tools

- May assist auditors with documenting compliance with GAGAS
- Use of the tools in isolation does not constitute adequate documentation with GAGAS requirements
- Columns to the right of the requirements may be used to support compliance with the GAGAS requirement
- Explanatory material that identifies and describes other procedures or actions does not impose additional requirements
- Significant sections of explanatory materials have been omitted
  - Auditors should read the entire text of the July 2007 Revision

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## Other Guidance

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## SSAE 15 and SAS 115: Revisions to AT 501 and SAS 112

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- Why revised?
    - To conform definitions of control deficiencies, material weakness and significant deficiency to PCAOB AS 5.
    - To provide for more professional judgment
    - Not intended to reduce quality of communication
  - Main Changes with SAS 115
    - No real change to material weakness definition
    - Significant deficiencies
      - Matters that merit the attention of governance
      - No longer a mathematical process
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## Interim Guidance on Reporting Deficiencies in Internal Control

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- Issued to assist auditors in complying with
    - SAS No. 115, *Communicating internal Control Related Matters Identified in an Audit*
    - SSAE No. 15, *An Examination of an Entity's Internal Control Over Financial Reporting That Is Integrated With an Audit of Its Financial Statements*
  - Revised AICPA standards have different definitions of material weaknesses and significant deficiencies than GAGAS
    - Can use revised definitions for GAGAS report if provide the revised definitions and describe the scope of testing performed on the entity's internal control over financial reporting
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## Future Work in the Standards Area

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### GAO's Auditing Standards Team Mission and Activities

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**Mission**-to support and advance the Comptroller General's goal of transforming and modernizing the accountability profession and to fulfill GAO's auditing standards setting responsibilities and act as a catalyst for reform in this area

**Work activities:**

1. Develop and maintain auditing standards that are tailored to government's unique characteristics and are generally accepted
  2. Provide leadership, advocacy, and tangible input for high quality government and private sector auditing standards
  3. Provide technical advice and leadership to GAO
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## Updates in Future Planned Work on Government Auditing Standards

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### Planned Projects

- Crosswalk between GAGAS and INTOSAI standards
- Public sector perspectives for AICPA “clarified” standards
- Develop guidance to address commonly asked questions
- Revise Government Auditing Standards based on
  - Issues associated with independence
  - Revisions/issues raised by other standard setters

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## Work on Independence Issues

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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
    - 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
  - Reconsider GAO's Independence Q&A
  - Update independence standard as necessary
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## Single Audit Issues

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## Recent Events

- 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 Congressional interest and expectations
- Persistent single audit quality problems affect grants management and accountability
- March 2009 GAO report (GAO-09-307R), Single Audit Improvements

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## Evolution of Single Audit Act and Its Underlying Principles

- 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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## **Opportunities Exist to Improve Single Audit Process and Oversight (GAO-09-307R)**

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In order to monitor risk, cost-benefit, and efficiency and effectiveness of the single audit process, we recommend OMB take the following actions:

- Designate an entity to (1) evaluate and comprehensively monitor the single audit process government-wide, (2) assess the efficiency and effectiveness of how agencies carry out their single audit responsibilities, and (3) identify additional guidance and resources need to carry out single audit requirements;

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## **Opportunities Exist to Improve Single Audit Process and Oversight (Con't.)**

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- Designate a federal workgroup to evaluate the current single audit process to identify simplified alternatives for meeting the accountability objectives of the Single Audit Act for the audits of small entities, while achieving the proper balance between risk and cost-effective accountability for the smallest to the largest entities; and
- Monitor the status of OMB workgroups, AICPA task forces, and NASBA referral project activities, and evaluate completed actions and their impact on addressing the PCIE report recommendations to improve single audit quality

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## American Recovery and Reinvestment Act of 2009 (Recovery Act)

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## American Recovery and Reinvestment Act of 2009 (Recovery Act)

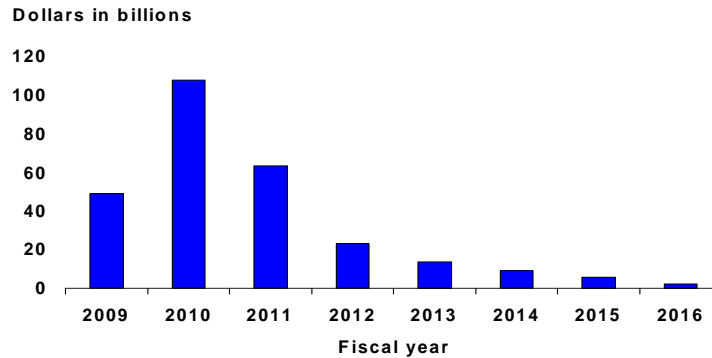
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- Signed February 17, 2009
  - Purposes:
    - preserve and create jobs and promote recovery
    - assist those most impacted by the recession
    - invest in science and health-care technology
    - invest in infrastructure
    - stabilize state and local government budgets
  - Total cost, tax and spending: \$787 billion, including over \$580 billion in additional spending (CBO estimate)
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## Recovery Act Spending by States and Localities will Occur Over Time

- Projected timing of Recovery Act funding made available to states and localities by fiscal year:



Source: GAO analysis of CBO and FFIS data.

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## What GAO Found: Single Audit Approach May Need to be Adjusted

- Single Audit Act and OMB Circular No. A-133 call for a “risk based” approach to determine which programs will be included in Single Audit testing.
- Under the current approach for risk determination, certain risks may not receive full consideration.
- Unique challenges associated with Recovery Act funding:
  - ✓ sudden increase in funds that most recipients are experiencing
  - ✓ new government programs and programs that are new for the recipient entity
  - ✓ need for timely and efficient oversight in response to the Recovery Act’s accountability requirements

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## GAO's Recommendations to OMB

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### Single Audit

To provide additional leverage as an oversight tool for Recovery Act programs, the Director of OMB should adjust the current audit process to:

- focus the risk assessment auditors use to select programs to test for compliance with 2009 federal program requirements on Recovery Act funding
- provide for review of the design of internal controls during 2009 over programs to receive Recovery Act funding, before significant expenditures in 2010
- evaluate options for providing relief related to audit requirements for low-risk programs to balance new audit responsibilities associated with the Recovery Act.

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## GAO Ongoing Concerns on Single Audit and Recovery Act

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### Timing

- Reporting deadline is 9 months after the end of the period under audit
- Extensions beyond this deadline are common
- No provision of interim internal control reporting or other means of timely communication to management before the report date

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## GAO Ongoing Concerns on Single Audit and Recovery Act

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### Insufficient Guidance

- 2009 Compliance Supplement issued end of May
  - Does not provide detailed guidance covering Recovery Act requirements
  - Auditors should watch for periodic addendums
  - Lack of information on federal programs that comprise program clusters
  - Guidance does not address how programs with significant increases in expenditures as a result of the Recovery Act will be included in years that audit procedures would have the most value
  - Does not address new programs under the Recovery Act

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## GAO Ongoing Concerns on Single Audit and Recovery Act

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### No appropriate solutions to provide auditor relief

- State and local auditors' lack of resources sufficient to perform effective single audits with increased workload imposed by Recovery Act funding
  - OMB has discussed to reduce or eliminate Type B risk assessment
    - GAO has concluded this change in itself does not provide adequate relief
- OMB and Congress are exploring other means to increase funding directly available to auditors
  - Timing and extent of relief uncertain

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## GAO's Accountability & Standards Team

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### Yellow Book Team:

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### We also get lots of help from:

- Bob Dacey, GAO Chief Accountant
- Abe Akresh, GAO Senior Expert, Auditing Standards
- Jennifer Allison, Advisory Council Administrator

Contact us at [yellowbook@gao.gov](mailto:yellowbook@gao.gov)

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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)