



National State Auditors Association

June 30, 2008

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Ms. Sherry Hazel
Audit and Attest Standards
AICPA
1211 Avenue of the Americas
New York, NY 10036-8775

Dear Ms. Hazel:

On behalf of the National State Auditors Association, we appreciate the opportunity to respond to the AICPA Auditing Standards Board's proposed Statement on Auditing Standards No. 114 (redrafted), *The Auditor's Communication with Those Charged with Governance*.

We have reviewed the proposed statement and generally agree with the provisions in the exposure draft. Our general impression is that the proposed SAS remained consistent with the current requirements in SAS No. 114. We find the new format to be easy to follow, but only after understanding how the application and other explanatory material relates to the requirements, and the appendices and exhibits relate to main section of the standard. Therefore, we recommend the ASB continue to educate auditors about how these sections interrelate, including an improved explanation about the authoritative status of each of the sections, in future documents.

As requested, we offer the following feedback in response to the questions posed by the ASB:

Questions posed by the ASB

1. *Are the objectives to be achieved by the auditor, stated in the proposed SAS, appropriate?*

The objectives to be achieved by the auditor, stated in the proposed SAS, are appropriate.

2. *Are revisions from the existing standards to converge with ISA 260 appropriate?*

The revisions from the existing standards to converge with ISA 260 are appropriate, except as noted below.

Paragraph 3 – we recommend paragraph 10 of SAS 114 be added back to the proposed standard. This issue is an important and common one for government entity audits, and likely some smaller entities as well. We think this comment can be added as explanatory guidance around paragraph A4 and referenced to paragraph 3 (see next to the last sentence in that paragraph).

The proposed SAS removes the following language (see page 14 of 62 of the mapping document): "and, when considered necessary, request changes. If requested changes are not made, the auditor should inform those charged with governance that the auditor will consider the effect of this on the financial statements of the current and future years, and on the auditor's report." The explanation provided in the mapping document is that this language is duplicative of other standards. We suggest the ASB add a footnote to paragraph 12(a) or A22 citing which other standards (i.e., SAS) require this.

Paragraph A17 (second bullet) – we agree that those charged with governance should be aware of audit risk and materiality; however, the proposed language is confusing. To provide clarity, we suggest the ASB revise the wording as follows: "those charged with governance to understand issues of risk and materiality affecting the entity and the financial statements, and the auditor's plans to address them."

3. *Are the differences between the proposed SAS 114 and ISA 260 identified in exhibit B, and other language changes, appropriate?*

The differences between the proposed SAS 114 and ISA 260 identified in exhibit B are appropriate, except as noted below.

Footnote 3 in paragraph 13.a. is confusing since it references a standard requiring communications with management, not those charged with governance. We recommend the AICPA modify paragraph 13 to indicate that auditors should have the same communications with those charged with governance as they have with members of management regarding uncorrected misstatements, which should clarify the intent of the footnote reference.

Although paragraph A44 (in Appendix A) is lengthy, its content is important to the requirements in paragraph A22. The ASB should consider moving the information contained in paragraph A44 to the Application and Other Explanatory Material along with paragraph A22 instead of referencing Appendix A.

There appears to be numerous differences regarding paragraphs A1 through A43, some of which appear to be significant, that are not addressed in Exhibit B. Perhaps Exhibit B should acknowledge this and explain why these differences are not addressed.

4. *Have considerations for audits of smaller, less complex entities and governmental entities been dealt with appropriately?*

The proposed statement does not appropriately address considerations for governmental entities. We believe guidance for governmental entities is needed in several areas as noted below.

Paragraph 16 requires the auditor to indicate in communications with those charged with governance that the information is intended for their use only. In addition, paragraph A11 recommends the auditor meet with those charged with governance without members of management present at least annually. While the language in these paragraphs may be appropriate for such communications for audits of private companies or some nonprofit organizations, it is not appropriate for some nonprofit (direct-support) organizations or many state governments. Many governments have freedom of information statutes that could prevent the auditor from complying with these paragraphs as meetings with and information provided to those charged with governance is public information. We recommend the ASB provide guidance to auditors for addressing situations when such statutes exist.

Paragraph A5 – with respect to the last sentence of the first bullet, in the government environment, subgroups may be established as audit committees with individuals who are not employed by the government, and for which some assigned responsibilities indicate the need for auditor communication of matters required by this standard. However, those subgroups may not have been given the proper authority under the applicable statutes or other legal provisions to accept the auditor's communication of legal, access, or confidentiality matters, or for which the auditor is not legally able to provide such information. We believe the explanatory information in this paragraph should acknowledge this fact, and that the auditor may not be able to communicate matters required by this standard to those subgroups.

Paragraph A8 – we can ultimately have enough discussion to explain to some an understanding of groups and components in the context of the government environment, but are concerned that not all

auditors of government entities will. Accordingly, we recommend a few sentences be added, or a separate paragraph, to provide an example of how this is applied in the government environment (i.e., a county government [the "group"] may have components [i.e., enterprise activities and separate legal entities that are included in the county's reporting entity]).


Paragraph A13 – we believe a footnote should be added to acknowledge that for audits of government entities, auditors will commonly follow Government Auditing Standards (GAGAS), in which auditors will also have to meet the independence standards (and other general standards) of GAGAS.

In addition to our comments noted above, we suggest the ASB consider the following as it finalizes this standard:

- Paragraph 9 – the last sentence added to this paragraph is wordy, unclear and should be revised. We believe it can simply be said that the auditor should be satisfied that all those charged with governance are informed when the auditor has only communicated certain matters to some of those charged with governance.
- Paragraph 12 – the heading should include "or issues", to be consistent with bullet 12.d, and the language used throughout the Audit Documentation clarity exposure draft.
- Paragraph 17 – this paragraph states, "This communication need not include matters that arose during the course of the audit that were communicated with those charged with governance and satisfactorily resolved. (Ref: par. A35–A37)." In regard to this paragraph and its related explanatory guidance in paragraphs A35-A37, the auditor should be reminded that significant deficiencies noted by the auditor during the audit (but not by management or its internal control) that may have been corrected by management before completion of the audit should still be reported. This additional guidance should be included within paragraphs A35-A37.
- Paragraph A17 – the last bullet in this paragraph should state "...the entity and its environment, including its internal control" to be consistent with SAS 109 paragraph 1.

We appreciate the opportunity to respond to such an important document. Should you have any questions or need additional information regarding our response, please contact Sherri Rowland of NSAA at (859) 276-1147 or me at (404) 656-2174.

Sincerely,

A handwritten signature in black ink that reads "Russell W. Hinton". The signature is written in a cursive, flowing style.

Russell W. Hinton
President, NSAA