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October 31, 2012

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 entitled *Omnibus Statement on Auditing Standards—2012*.

We have reviewed the exposure draft and generally agree with the proposed revisions to AU-C Sections 600 and 800. Below we have provided our response to the issue for consideration posed in the exposure draft. We have also provided, by paragraph, comments or suggestions that we believe the Board should consider as it finalizes this document.

Issue for Consideration – AU-C section 600 precludes making references to the audit of a component auditor when the financial reporting framework used by the component differs from that used by the group. The ASB is considering removing this preclusion, and is seeking feedback on whether the removal of this preclusion is appropriate.

We believe it is appropriate to remove the provision of AU-C Section 600 which precludes making references to the audit of a component auditor in the auditor's report on group financial statements when the financial reporting framework used by the component differs from that used by the group. In practice, it is not uncommon for a governmental entity to have group financial statements in which components are based on a different financial reporting framework (both general purpose and special purpose frameworks) and audited by a component auditor. The group auditor needs to make reference in these cases because jurisdictionally or by engagement, the group auditor cannot audit the component. We believe that we have had many years of experience in these matters, which typically involve the group auditor obtaining sufficient appropriate evidence of group and component managements' conversions and consolidations and still making reference to the component auditor's report on the component financial statements. The other provisions of this ED with respect to the procedures group auditors should perform and including language in the group auditor's report about the additional procedures performed should provide readers appropriate context for these audits.

Other Comments

- **Paragraph A53** – The added language includes a reference to Appendix B. It seems that this is a reference to the overall AU-C Appendix B, not Appendix B in Section 600. This should be clarified.
- **Paragraph A54** – It is not clear whether the proposed revisions to the standard do, in fact, anticipate that the conversion of the component's financial statements could be reviewed by the component auditor, but the component auditor would not specifically provide a report on the conversion. For example, could a component auditor perform agreed-upon procedures to review the conversion, for which the group auditor could review the work and subsequently assume responsibility for it? We believe that this would be allowable under the proposed standard and suggest wording be added to clarify this for the final standard.

- *Paragraph A54* – This paragraph states, “In rare circumstances, the group engagement partner may...” We disagree with this statement. We can envision many examples where the group auditor – the one most knowledgeable about the government’s operations – is in the best position to audit the conversion. In fact, given the complexities of large governments, we believe the component auditor would have extreme difficulties auditing the conversion in certain circumstances. As an example, in one state, revenue bond programs are considered components, audited by CPA firms. Transactions of the revenue bond programs are combined with transactions recorded on the group’s accounting system and reported in debt service funds and capital project funds. The group auditor is in the best position to audit the conversion. We suggest the language be revised to read, “In certain situations, the group.....” This allows auditors to more readily apply auditor judgment in assessing who is in the best position to audit the adjustments.
- *Paragraph A55* – The last sentence of this paragraph states, “In most cases, special purpose frameworks.....are not comparable to GAAP.” We believe this statement is unnecessarily too restrictive. The governmental modified accrual basis is relatively comparable to the cash basis special purpose framework and certain government components may be required by legislation to prepare cash-basis financial statements. Auditing the adjustments to convert those statements to a GASB modified accrual basis would be relatively straightforward. Therefore, we believe it would be appropriate to remove the last sentence of .A55 and believe the information in .A56 provides enough guidance for an auditor to exercise professional judgment about comparative frameworks.
- *Paragraph A56* – We believe the lead sentence should be revised to indicate that the bulleted information is related to circumstances surrounding differing frameworks. One suggestion is as follows: “Additional considerations **a group auditor may consider** in determining whether it may be appropriate to make reference to the audit of the component in the auditor’s report on the group financial statements **when the component prepares financial statements using a differing financial reporting framework include:**”.
- *Paragraph A57* – We understand that paragraph .26 allows for different financial reporting frameworks that would include special purpose frameworks other than GAAP. As noted in .A57, the financial reporting framework established by the Governmental Accounting Standards Board (GASB) allows for inclusion of component financial statements prepared in accordance with a different financial reporting framework. To that end, it should be noted that GASB standards only allow for inclusion of legally separate component units with a different reporting framework that is considered GAAP. For example, a governmental university may include its foundation’s statements prepared in accordance with FASB standards, and GASB standards allow the university to include the foundation’s statements on a separate page or to be reconfigured to conform to the university’s governmental presentation. In these situations, paragraphs .26 and .29 would not be relevant for governmental entities.

However, there are other governmental situations where a component may not be legally separate but could be audited by other auditors and prepared in a financial reporting framework other than GAAP, including a special purpose framework such as the cash basis. GASB standards do not provide for this type of inclusion. Therefore, if a governmental entity group auditor chooses to refer to this type of component’s audit, the group engagement team would need to determine whether they can reasonably expect to obtain sufficient appropriate audit evidence to take responsibility for auditing the adjustments to convert the component’s financial statements prepared in a differing framework. In these situations paragraphs .26 and .29 would apply to governmental entities.

The language in .A57 appropriately indicates that “when the **provisions established** by the applicable financial reporting framework for inclusion of those component financial statements **have been followed**, the requirements in paragraphs .26 and .29 are not relevant.” However, we believe that the language is not clear enough to ensure that governmental entity group auditors will understand that paragraphs .26 and .29 may in fact apply to them in certain situations. We recommend an additional sentence at the end of .A57 that states something like, “In certain situations

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where there are no provisions established by the applicable financial reporting framework for inclusion of component financial statements prepared in accordance with a different financial reporting framework, such as a special purpose framework, the requirements in paragraphs .26 and .29 would be relevant.”

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 (916) 323-0913.

Sincerely,

A handwritten signature in black ink that reads "Elaine M. Howle". The signature is written in a cursive style with a large, prominent initial "E".

Elaine M. Howle
President, NSAA