
**Government Auditing Standards
January 2007 Revision**

**Mid-America Intergovernmental
Audit Forum
May 3 - 4, 2007**

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Session Objectives

- Explain the process being used to issue the 2007 Yellow Book
 - Highlight major revisions in the January 2007 Revision of the Yellow Book
 - Discuss the reasons for the changes and what these changes will mean for government auditors
 - Outline the proposed revision to quality control and peer review standards
 - Discuss effective dates
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2007 Yellow Book: Development of Issues

- Identified need for revising Yellow Book based on activities of AICPA, PCAOB, and other standard setters in Fall 2005
 - Three Advisory Council meetings
 - Frequent requests for feedback based on drafts
 - June 2006 Exposure Draft
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Process for Analyzing Comments

- Comments received - 118 commenters
- Systematic review process to analyze every comment
- All comments entered into an Access database
- Collaborative team review of comments

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January 2007 Revision

- 2007 revision supersedes the 2003 revision
- Issued revision late January 2007
- At same time issued exposure draft requesting comments on redrafted sections on quality control and peer review
- The complete 2007 revision will be available after the quality assurance and peer review sections are finalized and incorporated into the standards

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Chapter 1 Use and Applicability of GAGAS

- Reinforced the key role of auditing in maintaining accountability and improving government operations
- Clarified the standards through standardized language to define the auditors' level of responsibility and distinguish between requirements and additional guidance.
- Added guidance on citing compliance with GAGAS in the auditors' report
- Clarified and expanded the standards to recognize other sets of standards that can be used in conjunction with GAGAS
- Retained the same types of government audits and attestation engagements, but updated and expanded the definitions and descriptions of performance audits and attestation engagements

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Chapter 1
Use of Terminology

Standardized language to define the auditor requirements

- **Consistent with SAS No. 102**
 - “**Must**” and “**is required**” indicate an unconditional requirement
 - “**Should**” indicates a presumptively mandatory requirement
 - Text not using the above conventions is considered explanatory material

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Chapter 1
Compliance with GAGAS & Other Standards

- **Citing GAGAS in auditors’ report**
- **Recognizing other sets of professional standards**

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Chapter 2
Ethical Principles in Government Auditing

Heightened emphasis on ethical principles

Five principles

- **Public interest**
- **Integrity**
- **Objectivity**
- **Proper use of government information, resources, and position**
- **Professional behavior**

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Chapter 3
General Standards

- Clarified and streamlined the discussion of the impact of professional services other than audit services (nonaudit services) and their impact on auditor independence
- Stressed the critical role of professional judgment in complying with GAGAS
- Expanded competence to emphasize its importance and relate it to key steps in performing an audit and reporting on the auditors' conclusions
- Updated CPE requirements to incorporate April 2005 changes
- Re-exposed quality control and peer review sections

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Chapter 3: General Standards
Nonaudit Services

- Moved nonaudit services from “personal impairments” to “organizational impairments”
- Created three distinct categories of nonaudit services and consolidated and streamlined the examples previously interspersed throughout the independence section

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Chapter 3: General Standards
Independence

- Streamlined requirements for auditors regarding independence when using the work of a specialist
- Added that an externally imposed restriction on access to records, government officials, or other individuals needed to conduct the audit may impair external independence
- Added steps that audit organizations should take if an impairment to independence is identified after the audit report is issued

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Chapter 3: General Standards
Continuing Professional Education

- Incorporated the revised CPE requirements that were issued in April 2005 (GAO-05-568G).
- Clarified CPE requirements to include internal specialists who are part of the audit organization and part of the team

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All Types of GAGAS Audits and Attestation Engagements

- Defined those charged with governance
- Added a requirement for controls over electronically maintained audit documentation
- Clarified and streamlined
 - Developing elements of a finding
 - Reporting confidential or sensitive information
 - Reporting views of responsible officials
 - Issuing and distributing reports

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All Types of GAGAS Audits
The Role of Those Charged with Governance

- Have the duty to oversee the strategic direction and obligations related to the accountability of the entity
- Because it may be unclear who is charged with governance functions, auditors evaluate organizational structure for directing and controlling operations to achieve the entity's objectives

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All Types of GAGAS Audits
Controls over Electronic Audit Documentation

- Whether audit documentation is in paper, electronic, or other media, the integrity, accessibility, and retrievability of the underlying information could be compromised if
 - Documentation is altered, added to, or deleted without auditors' knowledge
 - Documentation is lost or damaged
- For documentation retained electronically, the audit organization should establish information systems controls concerning the accessing and updating the audit documentation

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All Types of GAGAS Audits
Developing Elements of a Finding

- Elements needed depend on the objectives of the audit
- Finding is complete to the extent the audit objectives are satisfied
- Auditor should plan and perform procedures to develop the elements of a finding that are relevant

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All Types of GAGAS Audits
Reporting Confidential and Sensitive Information

- If information is excluded from the auditors' report, auditors
 - Should disclose that certain information has been omitted and reason for the omission
 - May issue a separate report and distribute it to only persons authorized to receive it
- If subject to public records laws, auditors should
 - determine the impact of such laws on the availability of the separate report
 - determine whether other means of communicating would be more appropriate

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All Types of GAGAS Audits
Reporting Views of Responsible Officials

- If the report discloses deficiencies in internal control, fraud, illegal acts, violations of provisions of contracts or grant agreements, or abuse, auditors should
 - Obtain and report views of responsible officials concerning
 - Findings, conclusions, and recommendations
 - Planned corrective actions
 - Include in the report an evaluation of the comments
 - If the audited entity does not provide comments, auditors may issue the report and indicate that the audited entity did not provide comments

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All Types of GAGAS Audits
Distributing Reports

- Distribution of reports depends on
 - The relationship of the auditors to the audited organization
 - The nature of the information contained in the report
- Different requirements for
 - Government audit organizations (external)
 - Internal audit organizations in government
 - Public accounting firms

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Changes Related to Internal Auditors

- Encouraged internal auditors to use IIA standards in conjunction with GAGAS
- Modernized the criteria for organizational independence for internal audit functions
- Emphasized the importance of internal audit as part of the overall governance, accountability, and internal control
- Clarified that internal auditors may follow IIA standards to communicate results of the audit to parties who can ensure that the results are given due consideration

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Chapter 4
Financial Audit Field Work

- Updated communications during planning
- Clarified and streamlined the auditors' responsibilities for contract provisions or grant agreements
- Clarified and streamlined the auditors' responsibilities in field work for abuse
- Added a clear and prominent discussion on consideration of fraud and illegal acts
- Updated GAGAS based on recent developments in financial auditing and internal control

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Chapter 4: Financial Audit Field Work
Communication During Planning

- Auditors are required to communicate their understanding of the services to be performed for each audit

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Chapter 4: Financial Audit Field Work
Contract Provisions or Grant Agreements

- Auditors should design the audit to provide reasonable assurance of detecting misstatements that result from violations of provisions of contracts or grant agreements that could have a direct and material effect on financial statement amounts or other financial data significant to the audit objectives
- When auditors conclude that a violation of provisions of contracts or grant agreements has or is likely to have occurred, they should determine the effect on the financial statements as well as implications for other aspects of the audit

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Chapter 4: Financial Audit Field Work Abuse

- If the auditor becomes aware of indications of abuse that could be material, the auditor should apply audit procedures specifically to ascertain
 - Whether material abuse has occurred
 - The potential effect on the subject matter of the audit

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Chapter 4: Financial Audit Field Work Fraud and Illegal Acts

- Clarifies the existing standard but does not change auditors' responsibilities
- Auditors have responsibilities under both the AICPA standards and GAGAS

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Chapter 4: Financial Audit Field Work Audit Documentation

- Updated the standard to achieve consistency with SAS No. 103
- The auditor should prepare audit documentation that enables an experienced auditor, having no previous connection to the audit, to understand
 - The nature, timing, and extent of procedures performed
 - The results of procedures performed and evidence obtained
 - How the audit evidence relates to the audit conclusions
 - The conclusions reached on significant matters

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Chapter 5 Financial Audit Reporting

- Updated reporting requirements for internal control deficiencies
- Encouraged communicating, in the auditors' report, significant concerns, uncertainties, or other unusual events that could have a significant impact on the financial condition or operations
- Increased transparency surrounding reporting on restated financial statements

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Chapter 5: Financial Audit Reporting Internal Control

Definitions of internal control deficiencies
(consistent with SAS No. 112)

- Significant deficiency
- Material weakness

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Reporting Internal Control Deficiencies

Old Definitions	New Definitions – SAS 112
Material weakness (GAGAS paragraph 5.14 and AU 325.15)	Material weakness
Reportable condition (GAGAS paragraph 5.13 and AU 325.02)	Significant deficiency
Management letter comment (GAGAS paragraph 5.16)	Other matters related to internal control

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Chapter 5: Financial Audit Reporting
Fraud, Illegal Acts, Other Noncompliance, Abuse

When auditors conclude that any of the following has occurred or is likely to have occurred, they should include in the audit report the relevant information about

- Fraud and illegal acts that are greater than inconsequential
- Material violations of contracts or grant agreements
- Material abuse

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Chapter 5: Financial Audit Reporting
Management Letter

- Illegal acts, violations of provisions of contracts or grant agreements, or abuse that is inconsequential
- Internal control deficiencies that have an inconsequential effect on the financial statements
- Violations of provisions of contracts or grant agreements or abuse that have an effect that is less than material but more than inconsequential
 - Should be communicated in writing

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Chapter 5: Financial Audit Reporting
Communicating Significant Matters

- Auditors may communicate certain matters when they become aware that such issues exist
- Determining whether to communicate in the auditors' report is a matter of professional judgment

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Chapter 5: Financial Audit Reporting
Restatements - Increased Transparency

- Auditors should advise management to make appropriate disclosures when the auditors believe it is likely that previously-issued financial statements are misstated and the misstatement could be material (AU 561)
- Under GAGAS, auditors have additional responsibilities

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Chapter 5: Financial Audit Reporting
Restatements - Increased Transparency

Evaluating the timeliness and appropriateness of management's disclosures and actions (AU 561)

- Auditors should evaluate the timeliness and appropriateness of
 - management's disclosures to those likely to rely on the financial statements and
 - management's actions to determine and correct misstatements in previously-issued financial statements

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Chapter 5: Financial Audit Reporting
Restatements - Increased Transparency

Evaluating the timeliness and appropriateness of management's disclosures and actions

Under GAGAS, auditors should also evaluate whether management

- Acted in an appropriate time frame after new information was available
- Disclosed the nature and extent of the known or likely material misstatements
- Disclosed whether specified information was in the entity's restated financial statements

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Chapter 5: Financial Audit Reporting
Restatements - Increased Transparency

Report on restated financial statements

Auditors should perform audit procedures sufficient to reissue or update the auditor's report on the restated financial statements regardless of whether the restated financial statements are separately issued or presented on a comparative basis

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Chapter 5: Financial Audit Reporting
Restatements - Increased Transparency

Report directly when the audited entity does not take the necessary steps

- Auditors should notify those charged with governance if the entity management
 - Does not act in an appropriate timeframe
 - Does not restate with reasonable timeliness
- Auditors should inform management that they will take steps to prevent further reliance on the auditors' report and advise those charged with governance to notify oversight bodies and funding organizations

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Chapter 6
Attestation Engagements

Conforming changes have been made for the following items

- Definitions of internal control deficiencies
- Description of abuse
- Audit documentation
- Use of terminology to define professional requirements
- Reporting views of responsible officials and confidential and sensitive information
- Issuing and distributing reports

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**Chapters 7 & 8
Performance Audits**

- Enhanced performance audit standards that elaborate on the overall framework for high-quality performance audits
- Added a section describing the auditors' overall assessment of the collective evidence to support the findings and conclusions
- Added a section on information systems controls for the purpose of assessing audit risk and planning the audit

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**Chapters 7 & 8
Performance Audits**

- Expanded the auditors' compliance with GAGAS in the performance audit report
- Clarified and streamlined auditors' responsibility for
 - Reporting the views of responsible officials
 - Reporting confidential and sensitive information
 - Issuing and distributing reports

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**Chapters 7 & 8
Performance Audits**

Level of assurance in performance audits

- Performance audits that comply with GAGAS provide reasonable assurance that the evidence is sufficient and appropriate to support the auditors' findings and conclusions

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**Chapters 7 & 8
Performance Audits**

- **Concept of significance in a performance audit**
- **Audit risk**
- **Sufficient, appropriate evidence**

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**Chapters 7 & 8
Performance Audits**

Added a section describing the overall assessment of the collective evidence to support the findings and conclusions

Evidence is not sufficient and appropriate when it

- **Carries an unacceptably high risk that it could lead to an incorrect or improper conclusion**
- **Has significant limitations**
- **Does not provide an adequate basis for addressing the audit objectives or supporting the findings and conclusions**

Added a section on information systems controls for the purpose of assessing audit risk and planning the audit

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**Chapters 7 & 8: Performance Audits
Fraud and Abuse**

- **If an auditor becomes aware of indications of abuse that could be qualitatively or quantitatively significant to the program under audit, auditors should apply audit procedures specifically to ascertain the potential effect on the program under audit within the context of the audit objectives**
- **However, because the determination of abuse is subjective, auditors are not required to provide reasonable assurance of detecting abuse**
- **After performing additional work, auditors may discover that the abuse represents potential fraud or illegal acts**

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Chapters 7 & 8: Performance Audits
Legal and Regulatory Requirements, Contract Provisions or Grant Agreements

- Auditors should determine which laws, regulations, and provisions of contracts or grant agreements are significant within the context of the audit objectives and assess the risk that violations of those laws, regulations, and provisions of contracts or grant agreements could occur.
- Auditors should design and perform procedures to provide reasonable assurance of detecting instances of violations of legal and regulatory requirements or violations of provisions of contracts or grant agreements that are significant within the context of the audit objectives.

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Chapters 7 & 8: Performance Audits
GAGAS Statement

GAGAS statement in auditor's report

When auditors comply with all applicable GAGAS requirements, they should use specified language in the report

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Chapters 7 & 8: Performance Audits
Discovery That Report Was Issued without Sufficient, Appropriate Evidence

- If after the report is issued, auditors discover the report was not supported by sufficient, appropriate evidence, they should communicate it
- If the report was posted to the auditors' publicly accessible Web site
 - Remove the report
 - Post a public notification that the report was removed
- Determine whether to conduct additional audit work necessary to reissue report with revised findings

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**Appendix
Supplemental Guidance**

Added an appendix to provide supplemental guidance to assist auditors in the implementation of GAGAS

Proposed Revisions

**Quality Control and Assurance
and
Peer Review**

**Chapter 3 Exposure Draft
Audit Quality Control and Assurance**

Major changes

- Strengthened emphasis on audit quality and expanded description of overall objectives and elements of quality control
- Added flexibility to have peer review cycles of up to 5 years for performance audits
- Increased transparency regarding the effectiveness of quality control systems by requiring that external peer review reports be made public

**Chapter 3 Exposure Draft
Audit Quality Control and Assurance**

Strengthened emphasis on audit quality and expanded description of overall objectives and elements of quality control

Added flexibility to have peer review cycles of up to 5 years for performance audits

Increased transparency regarding the effectiveness of quality control systems by requiring that external peer review reports be made public

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**Chapter 3 Exposure Draft
Audit Quality Control and Assurance**

- **If peer review opinion is adverse and related to or impact audits performed under GAGAS**
 - Each GAGAS report should disclose the peer review results until such time as the adverse opinion is replaced by an unqualified or qualified opinion
 - **Those audit organizations seeking to enter into a contract for such services should provide the following to the party contracting for such services**
 - The audit organization's most recent peer review report and any letter of comment
 - Any subsequent peer review reports and letters of comment received during the period of the contract
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January 2007 Revision: Implementation Dates

- For performance audits, the standards are to become effective for audits beginning on or after January 1, 2008
 - For financial audits and attestation engagements, the standards become effective for audits of periods beginning on or after January 1, 2008
 - Early implementation is permissible and encouraged
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Questions or comments?

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Where to Find the Yellow Book

- The Yellow Book is available on GAO's Web site at
www.gao.gov/govaud/ybk01.htm
 - For technical assistance, contact GAO at
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