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

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**17<sup>th</sup> Biennial Forum of Government  
Auditors**

**Philadelphia, PA  
May 22, 2008  
Marcia B. Buchanan**

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## Session Objectives

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- Latest updates in implementing Government Auditing Standards
  - Issues being considered for additional guidance or revision in GAGAS
  - Audit quality issues in Single Audits, and the current status of reform efforts
  - Other trends that could impact audits of federal, state, and local governments and nonprofit entities receiving federal funding
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## Updates in Implementing Government Auditing Standards

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### Yellow Book Professional Requirements Tool

- 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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## Updates in Implementing Government Auditing Standards

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### Guidance on Complying with GAGAS and Sarbanes-Oxley Act

- GAGAS can be used in conjunction with PCAOB standards
- When auditors must or chose to meet the requirements of both standards, the PCAOB framework could result in inconsistencies
- GAO provided the following guidance:
  - Include in the internal control report an material weakness based on the definition in PCAOB AS 5
  - Also include other internal control weaknesses (material weakness and significant deficiency) as defined by SAS No. 112
  - GAGAS report should state PCAOB definitions were used
  - Reminder of other GAGAS reporting requirements

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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
  - Hierarchy of GAGAS and associated guidance
  - Revise Government Auditing Standards based on
    - Issues associated with independence
    - Revisions/issues raised by other standard setters
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## Overview of Advisory Council Meeting

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- Overview of Current GAGAS Independence Standards
  - Issues Addressed:
    1. Independence Definitions/Independence in Fact and Appearance
    2. Conceptual Framework: Principles vs. Rules
    3. Legislative Mandates/Firewalls
  - Management Representation Letters in Performance Audits
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## Overview of Current GAGAS Independence Standards

- 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
- Staff conclusions

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## Independence Definitions/Independence in Fact and Appearance

### 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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### Issues:

- A conceptual framework provides a common risk-based approach to analyzing independence matters that allows auditors to use their professional judgment
- A conceptual framework requires professional judgment and relies on the concept of risk

### Action items:

- Consider whether to add a conceptual framework to GAGAS
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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:

- Develop elements required in the report disclosure
  - Consider criteria that would allow for the use of firewalls as an appropriate safeguard (“carve-out” option)
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## Management Representation Letters in Performance Audits

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### Issues:

- Management representations may be appropriate in certain situations for performance audits
- Current GAGAS does not recognize management representations as a tool that auditors can use

### Action items:

- Add guidance to emphasize the importance of management representations to obtain sufficient appropriate audit evidence
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## Next steps

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- Develop guidance to address issue of management representations in performance audits
  - Develop guidance to deal with mandates/firewall issues
  - Develop proposed revisions on independence as needed
  - Follow due process for amending GAGAS
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## GAO Hot Topics

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### Single Audit Issues

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## Overview of Testimony

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GAO's perspectives on

- History and importance of the Single Audit Act and the principles behind the Act
  - GAO's preliminary analysis of the recommendations made by the PCIE for improving audit quality
  - Additional factors to consider for improving the quality of single audits
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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

- 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 Position on PCIE Recommendations

- GAO supports the recommendations made in the PCIE report
- However, GAO believes that a number of issues regarding the proposed training requirement need to be resolved
- Answers to the following questions will be important:
  - What are the efficiency and cost-benefit considerations for providing the proposed training for auditors currently performing single audits?
  - How can mechanisms already in place be leveraged to implement the proposed training?
  - How will the proposed training requirement affect the availability of audit firms that are qualified and willing to perform single audits?

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## Other Critical Factors

- GAO believes two other critical factors that need to be considered in evaluating the potential dollar impact and the efficiency and effectiveness of proposed actions:
  1. rate of problem audits by size
  2. the distribution of single audits by size within the universe of single audits
- PCIE study found that the rate of problem audits was much higher for audits of entities expending less than \$50 million in federal awards than for larger audits of those with \$50 million or more in expenditures

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## GAO Conclusions

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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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## Where to Find GAO's Single Audit Testimony

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- The Testimony is available on GAO's Web site at

[www.gao.gov](http://www.gao.gov)

- Testimony number is GAO-08-213T
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## What's Happening Now on Single Audit?

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- Currently focused on identifying any further actions needed to improve federal oversight and accountability for grants
    - Improvements needed to the current oversight structure for single audits across federal agencies
    - Improvements needed to single audit process and audit requirements to improve overall accountability for grant funds
  - Monitoring work of OMB subcommittees
  - Monitoring work of AICPA Task Forces
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## GAO Hot Topics

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## Other Trends

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## High-Risk Series: An Update

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- 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, January 2007)
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## Call for Stewardship: Tools for 21<sup>st</sup> Century Challenges

- 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

- 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

- 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

### Yellow Book Team:

- Jeanette Franzel (202) 512-9471
- Paula Rascona (202) 512-9816
- Marcia Buchanan (202) 512-9321
- Gail Vallieres (202) 512-9370
- Michael Hrapsky (202) 512-9535
- Heather Keister (202) 512-2943

### 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)
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