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American Institute of Certified Public Accountants. Auditing Standards Board

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AICPA

American
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August 2, 1994

File Ref. No. 1120

To the Auditing Standards Board:

Re: Exposure Draft on Compliance Auditing Considerations in Audits of Governmental Entities and Other Recipients of Governmental Financial Assistance

Here are the comment letters received to date on the exposure draft on Compliance Auditing Considerations in Audits of Governmental Entities and Other Recipients of Governmental Financial Assistance.

Name/Affiliation

Location

- | | |
|-------------------------------------------------------------|-----------------|
| 1. Deborah D. Lambert
Johnson, Lambert & Capron | New York, NY |
| 2. L. Karl Denton
L.K. Denton & Co., PC | Englewood, CO |
| 3. Michael D. Williams, CPA
Hochschild, Bloom & Co. | Washington, MO |
| 4. Richard J. Serluco
New Jersey Society of CPAs | Roseland, NJ |
| 5. Charles L. Lester
Office of the Auditor General | Tallahassee, FL |
| 6. Douglas R. Norton
Office of the Auditor General | Phoenix, AZ |
| 7. David R. Bean
Governmental Accounting Standards Board | Norwalk, CT |
| 8. Donald E. Davis
Department of Defense | Arlington, VA |

<u>Name/Affiliation</u>	<u>Location</u>
9. Jim Heist U.S. Department of Housing and Urban Development	Washington, DC
10. Mario A. Lauro, Jr. U.S. Department of Transportation	Washington, DC
11. Daniel G. Kyle, CPA, CFE State of Louisiana	Baton Rouge, LA
12. Georgene L. Bailey Secretary of State Audits Divison	Salem, OR
13. Peter L. McClintock U.S. Small Business Administration	Washington, DC
14. Montana Office of the Legislative Auditor	Helena, MT
15. Richard D. Johnson Office of Auditor State	Des Moines, IA
16. Accounting and Auditing Standards Committee Louisiana Society of CPAs	Louisiana
17. Patrick McNamee US General Accounting Office	Washington, DC
18. Linda S. Huneycutt Minter, Morrison and Grant	Alexandria, VA
19. Marcia L. Taylor Pensylvania Institute of CPAs	Harrisburg, PA
20. Arthur A. Hayes, Jr. Comptroller of the Treasury	Nashville, TN
21. Margaret Kelly, CPA State Auditor of Missouri	Jefferson City, MO
22. Arthur A. Hayes, Jr., CPA Association of Government Accountants	Alexandria, VA
23. Maurice C. Christiansen, CPA National State Auditors Association	Washington, DC
24. Maryland Association of CPAs	Lutherville, MD

<u>Name/Affiliation</u>	<u>Location</u>
25. Mark T. Hobbs Hobbs and Corley, PA	Columbia, SC
26. Sylvia L. Ayers, CPA University of Alabama System	Huntsville, AL
27. Mark Sleasman, CPA Alten Sakai & Company	Portland, OR
28. Thomas H. McTavish, CPA Office of the Auditor General	Lansing, MI
29. Dennis O. Teinert, CPA Office of the State Auditor	Austin, TX
30. Harvey C. Eckert Commonwealth of Pennsylvania	Harrisburg, VA
31. Coopers & Lybrand	New York, NY
32. Colorado Society of CPAs	Denver, CO
33. Michael L. Cheney Washington Society of CPAs	Bellevue, WA
34. Timothy E. Durbin Arthur Andersen	Detroit, MI
35. Walter J. Kucharski Commonwealth of Virginia	Richmond, VA
36. New York State Society of CPAs	New York, NY

Sincerely,



A. Louise Williamson, CPA
Technical Manager
Auditing Standards Division

ALW/jw

cc: SAS 68 Revision Task Force



May 31, 1994

AICPA
c/o Louise Williamson
Technical Manager
Auditing Standards Division, File 2357
1211 Avenue of the Americas
New York, NY 10036-8775

Re: Comments on the May 12, 1994 Exposure Draft on Compliance Auditing
File 2357

The above-mentioned Exposure Draft does a good job of meeting the objectives outlined in the Summary to the Exposure Draft. The following minor comments are intended to clarify the draft as written to avoid any ambiguities.

1. Paragraph 1a: The way this sentence is worded is confusing and seems to imply an elevated responsibility under SAS No. 54 for laws and regulations that apply to governmental financial assistance. It is unclear that for those items that this sentence is referring only to "direct and material effect." Consider reordering the sentence as follows:

"Apply the provision of Statement on Auditing Standards (SAS) No. 54, Illegal Acts by Clients (AICPA, Professional Standards, vol. 1, AU sec. 317), related to detecting misstatements resulting from illegal acts related to laws and regulations that have a direct and material effect on the determination of financial statement amounts in the audits of financial statements of governmental entities and other recipients of governmental financial assistance."

2. Paragraph 7: To be consistent and to avoid confusion, consider replacing the term "governmental funds" with governmental financial assistance".

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Washington, DC 20036
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May 31, 1994

Page Two

3. Paragraph 8: It is unclear to me from this paragraph whether the general standards of GAS go beyond GAAS. Thus as an auditor, it is unclear to me whether I need to be concerned with them or, should I just focus on the expanded fieldwork and reporting requirements only.
4. Paragraph 17 and 18: In paragraph 14 it was indicated by footnote that general requirements also may be referred to as common requirements. To be consistent and to avoid confusion, I would continue to refer to such requirements as "general" in paragraphs 17 and 18.

Very truly yours,



Deborah D. Lambert
Partner

EXPOSURE DRAFT

FILE 2357

PROPOSED STATEMENT ON AUDITING STANDARDS

COMPLIANCE AUDITING CONSIDERATIONS IN AUDITS OF GOVERNMENTAL ENTITIES AND OTHER RECIPIENTS OF GOVERNMENTAL FINANCIAL ASSISTANCE

May 12, 1994

Comment Date: July 29, 1994

Name and Affiliation: *L Karl Denton LK Denton & Co, PC*

Comments: _____

This draft appears to be much shorter and to the point. I think it is a step in the right direction.

Reference should be made to the 1994 Revision of the Yellow Book.

Instructions for Response Form

This form may be used for comments or suggestions relating to any aspect of the exposure draft that is of concern or interest to you. Return this response form to the address indicated on the reverse side by the comment date.

EXPOSURE DRAFT

FILE 2357

PROPOSED STATEMENT ON AUDITING STANDARDS

COMPLIANCE AUDITING CONSIDERATIONS IN AUDITS OF GOVERNMENTAL ENTITIES AND OTHER RECIPIENTS OF GOVERNMENTAL FINANCIAL ASSISTANCE

May 12, 1994

Comment Date: July 29, 1994

Name and Affiliation: Michael D. Williams, CPA, AICPA member,
Accounting and Auditing Director, Hochschild, Bloom & Company
Washington, Missouri

Comments: With respect to the request expressed in your
letter accompanying the exposure draft about audit engagements
involving small entities, I have two comments.

A significant common problem is the lack of the auditor's
documentation of testing of material laws and regulations.
Therefore, I suggest to help reduce this common problem would be
to add additional wording to the SAS. This can be done by adding
a sentence to paragraph 4 or 8 such as "It is also the auditor's
responsibility to document his understanding of which laws
and regulations are material, what he did to identify these,
what he did to test compliance and the results of his audit
procedures as required by Government Auditing Standards and
federal audt requirements."

Another significant common problem is the lack of documentation
of the internal control structure over laws and regulations and
the related testing of that internal control structure. I
suggest that the SAS include additional wording to help encourage
compliance, when required by Federal guidelines, to
paragraph 4 or 8 such as "It is also the auditor's
responsibility to document his understanding of which internal
control features management has established to monitor
compliance for each law and regulation identified. If
testing of the internal control structure is required, then
the auditor is required to document the procedures used to test
internal control (as is done with financial amounts) and to
summarize the results of the testing with a conclusion statement
in the workpapers."

Instructions for Response Form

This form may be used for comments or suggestions relating to any aspect of
the exposure draft that is of concern or interest to you. Return this response form to
the address indicated on the reverse side by the comment date.



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New Jersey Society of Certified Public Accountants

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July 15, 1994

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WILLIAM C. SWEENEY, JR.
MADISON

RICHARD D. WALTON
CLINTON

ROBERT S. ZARRA
WAYNE

American Institute of Certified
Public Accountants
A. Louise Williamson, Technical Manager
Auditing Standards Division, File 2357
1211 Avenue of the Americas
New York, New York 10036-8775

Re: Proposed Statement on Auditing Standards
Compliance Auditing Considerations in Audits of
Governmental Entities and Other Recipients of
Governmental Financial Assistance

Dear Ms. Williamson:

The Auditing and Accounting Standards Committee ("the Committee") of the New Jersey Society of Certified Public Accountants ("NJSCPA") is pleased to submit its comments on the Auditing Standards Board's Proposed Statement on Auditing Standards entitled, Compliance Auditing Considerations In Audits of Governmental Entities and Other Recipients of Governmental Financial Assistance ("the Statement"). The views expressed in this letter represent the majority of the members of the Committee and are not necessarily indicative of the views held by the full membership of the NJSCPA.

The Committee supports your continuing efforts in this area and overall was pleased with the Proposed Statement. However, the Committee believes that one change should be made to the Statement regarding paragraph six, page eleven. The Committee believes that the second sentence of paragraph six is vague and ambiguous and should be clarified. The language presented does not make it clear whether the quotation from paragraph 5.5 of the AICPA Audit and Accounting Guide, Audits of State and Local Governmental Units, sets forth a SAS level audit requirement for all entities within the scope of this statement. If the Board believes that the existing audit practice discussed in the Guide should be endorsed in this Proposed Statement than the language of the Statement should be modified to reflect that endorsement. We further suggest that no reference should be made to lower level auditing or accounting literature in the body of the Statement. We did not identify a benefit of such referencing, however, there is a cost of updating such reference as the underlying source document becomes superseded.

Thank you for your consideration of our comments.

Very truly yours,

Richard J. Serluco, Chairman
Auditing and Accounting
Standards Committee



(5)

STATE OF FLORIDA
OFFICE OF THE AUDITOR GENERAL



CHARLES L. LESTER, C.P.A.
AUDITOR GENERAL

July 14, 1994

TELEPHONE:
904/488-5534
S/C 278-5534

A. Louise Williamson, Technical Manager
Auditing Standards Division, File 2357
American Institute of Certified Public Accountants
1211 Avenue of the Americas
New York, NY 10036-8775

Dear Board Members,

I am responding to the Exposure Draft of the Proposed Statement on Auditing Standards, COMPLIANCE AUDITING CONSIDERATIONS IN AUDITS OF GOVERNMENTAL ENTITIES AND OTHER RECIPIENTS OF GOVERNMENTAL FINANCIAL ASSISTANCE, dated May 12, 1994 (PSAS).

As stated in the PSAS's summary, SAS 68 currently includes detail guidance which would be more appropriately covered in existing audit guides and statements of positions. I concur that the level of such guidance included in the SASs should be reduced as provided in this PSAS. In my opinion, the SASs should be considered the foundation for additional authoritative guidance. Accordingly, the SASs should be generic in content. Other authoritative guidance such as Interpretations (ASI) and Statements of Positions (SOP) should be used to implement specific details for auditing practices including performance and reporting guidance.

My comments relating to the PSAS are as follows:

1. Various language in the PSAS refers to compliance with laws and regulations. The PSAS is not clear as to whether other sources of compliance requirements, for example, contracts, grant award documents, and bond covenants, are included in this terminology. This is primarily directed at the audit level of state and local governments, including their financial assistance. If these compliance areas are considered to be included within the scope of the PSAS, appropriate clarification should be incorporated into the PSAS.
2. Section 9.b., Federal Audit Requirements, uses the terminology "accounting and administrative controls." Other literature, i.e., SAS 55 and SOP 92-7, appears to have gotten away from using this terminology. The terminology should be considered for deletion from the PSAS.

3. Section 12, State and Local Laws and Regulations, states that this Statement should be applied to these engagements as applicable. While many Federal compliance requirements subject to audit are identified for the auditors, usually state and local governmental compliance requirements are not similarly identified. The final PSAS should provide additional guidance to assist the auditor in clarifying the audit scope as it relates to state and local governmental compliance auditing. This would also provide for a more economical and efficient audit in that only significant and relevant state and local governmental compliance requirements, agreed to in writing, would be identified and subjected to audit. Accordingly, an additional paragraph should be added to Section 12 as follows, "Engagements involving state and local governmental compliance auditing would, preferably, include the joint written identification by the audited entity and the auditor of the appropriate state and local governmental compliance requirements agreed to be subject to audit. However, the identification of state and local governmental compliance requirements would not limit the nature of the auditor's responsibilities related to illegal acts under SAS 54."
4. Section 16, Compliance Requirements Applicable to Federal Financial Assistance Programs. As currently stated, it could be incorrectly interpreted that specific requirements for all Federal programs are to be obtained from both the OMB's Compliance Supplement and the grant agreement or contract and that the OMB's Compliance Supplement may be relied upon without review of laws and regulations such as the U. S. Code and the Code of Federal Regulations (Federal Codes). Accordingly, Section 16 should be revised as follows, "The auditors should review the applicable Federal Codes for any changes in laws and regulations which might impact the requirements enumerated in the OMB's Compliance Supplements. Specific compliance requirements not included in the OMB's Compliance Supplements, may also be enumerated in the applicable Federal Codes and the grant agreement or contract."
5. Sections 19 through 22, Evaluating Results of Compliance Audit Procedures on Major Federal Financial Assistance Programs. The word "Major" should be eliminated in the Section title. Also, "Major Programs" should be added as a subtitle above Section 19, and "Nonmajor Programs" should be added as a subtitle above Section 22. This will clarify the information included in these sections.

6. The timing of the release of the final PSAS in relation to changes proposed by other current studies applicable to other relevant authoritative guidance could have a major impact on the effectiveness of the SAS. The PSAS should make references that Federal compliance requirements may be significantly impacted by the implementation of these proposed changes. Perhaps, the PSAS should include a summary of these proposed changes as an appendix.

I thank the Board and staff for the time spent and the good job performed on this project. Also, I appreciate the opportunity to comment on the PSAS.

Sincerely,



Charles L. Lester

CLL/sd



6

DOUGLAS R. NORTON, CPA
AUDITOR GENERAL

STATE OF ARIZONA
OFFICE OF THE
AUDITOR GENERAL

DEBRA K. DAVENPORT, CPA
DEPUTY AUDITOR GENERAL

July 15, 1994

Ms. A. Louise Williamson, Technical Manager
Auditing Standards Division - File 2357
American Institute of CPAs
1211 Avenue of the Americas
New York, NY 10036-8775

Re: AICPA Exposure Draft (ED) of a Proposed Statement on Auditing Standards - Compliance Auditing Considerations in Audits of Governmental Entities and Other Recipients of Governmental Financial Assistance (to supersede SAS No. 68, *Compliance Auditing Applicable to Governmental Entities and Other Recipients of Governmental Financial Assistance*)

Dear Ms. Williamson:

We have reviewed subject ED and are in general agreement with the document, particularly the concept of providing generic guidance to practitioners engaged to perform compliance audits of governmental entities and other recipients of governmental financial assistance. Eliminating the detailed guidance and example reports included in SAS No. 68, which are included in other authoritative pronouncements, will reduce the frequency of the need to revise this proposed standard when the other pronouncements are revised.

Consistent with the goal of minimizing subsequent revisions, we offer the following specific comments related to references to other authoritative pronouncements.

- ¶ 1 The last sentence of footnote 3 should be updated since the revised "Yellow Book" has now been issued.

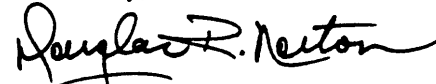
Footnote 4 refers specifically to SOP 92-7 and 92-9. A generic reference to the AICPA Audit Guides and related AICPA SOPs would minimize potential obsolescence when the specified SOPs are revised or incorporated into the ASLGU. This comment also applies to ¶ 18, footnote 11.

Ms. A. Louise Williamson
July 15, 1994
Page two

- ¶ 6 Since the ASLGU is currently being revised, the reference in the last sentence may be obsolete before this proposed SAS is issued. Suggest the use of generic language to solve the problem.

If you have any questions concerning this response, please contact David I. Williams or Mina Van Dyne of the Professional Practice Group of my Office at (602) 553-0333.

Sincerely,


Douglas R. Norton
Auditor General

DRN:sm

cc: Arthur A. Hayes, Jr., Chairman
NSAA Audit Standards and Reporting Committee

7

GOVERNMENTAL ACCOUNTING STANDARDS BOARD

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DAVID R. BEAN
Director of Research

July 19, 1994

Ms. A. Louise Williamson
Technical Manager, Auditing Standards Division
File 2357
American Institute of CPAs
1211 Avenue of the Americas
New York, NY 10036-8775

Dear Ms. Williamson:

Following are comments of the staff of the Governmental Accounting Standards Board on the AICPA's Exposure Draft (ED) of a proposed Statement on Auditing Standards (SAS), *Compliance Auditing Considerations in Audits of Governmental entities and Other Recipients of Governmental Financial Assistance*. These comments have not been deliberated by the Board and do not constitute a formal response by the Board.

In paragraph 3 and footnote 5, the ED uses a definition of *subrecipient* that varies from the definition in federal literature (as did SAS 68 before it). OMB Circular A-128, *Audits of State and Local Governments*, defines *subrecipient* as "any person or government department, agency or establishment that receives Federal financial assistance to carry out a program through a State or local government, but does not include an individual that is a beneficiary of such a program." The Institute should again consider using the federal definition (to avoid continuing two definitions for the same term in the same environment) and recognize a third type of governmental recipient—the beneficiary. This would cause the first sentence of paragraph 3 to read: "Federal, state, and local governmental entities provide financial assistance to other entities, including not-for-profit organizations and business enterprises, that are either primary recipients, subrecipients, or beneficiaries."

Paragraph 6 states that the auditor should design the audit to provide reasonable assurance that the financial statements are free of material misstatements resulting from violations of laws and regulations that have a direct and material effect on the determination of financial statement amounts. (Paragraph 13 expands on this with suggested procedures.) Codification Section 1200, "Generally Accepted Accounting Principles and Legal Compliance," paragraph .112 requires disclosure of material violations of legal and *contractual* provisions. The Codification does not define

Ms. A. Louise Williamson
July 19, 1994
Page 2



material; however, we believe it would be helpful if these paragraphs at least referenced the GAAP provision for disclosure of violations.

All references to the State and Local Government Audit Guide should be updated to the new Guide. For example, footnote 10 references the Statements of Position that are incorporated into the new Guide.

If you have any questions about these comments, please contact me at (203) 847-0700, extension 244 or Venita Wood, project manager at extension 299.

Sincerely,

David R. Bean

SAS68res.doc

8



INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
400 ARMY NAVY DRIVE
ARLINGTON, VIRGINIA 22202-2884



Audit Policy
and Oversight

JUL 18 1994

Ms. A. Louise Williamson
Technical Manager
Auditing Standards Division
American Institute of Certified
Public Accountants
1211 Avenue of the Americas
New York, New York 10036-8775

Dear Ms. Williamson:

We have reviewed the Exposure Draft - Proposed Statement of Auditing Standards - Compliance Auditing Considerations in Audits of Governmental Entities and Other Recipients of Governmental Financial Assistance. Our comments are enclosed for your consideration.

We appreciate the opportunity to review the exposure draft and provide comments. Please contact me or Mr. Steven E. Zane, of my staff, at (703) 693-0011, with any questions you may have.

Sincerely,

Donald E. Davis
Assistant Inspector General
for Audit Policy and Oversight

Enclosure

(8)

OFFICE OF INSPECTOR GENERAL, DEPARTMENT OF DEFENSE
COMMENTS ON
AMERICAN INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS
EXPOSURE DRAFT
PROPOSED STATEMENT ON AUDITING STANDARDS
COMPLIANCE AUDITING CONSIDERATIONS
IN AUDITS OF GOVERNMENTAL ENTITIES
AND OTHER RECIPIENTS OF GOVERNMENTAL FINANCIAL ASSISTANCE

Paragraph 1:

o Footnote 2:

The first sentence explains, "A single or organization-wide audit is an audit of an entity's financial statements and of compliance with federal regulations relating to federal financial assistance." This sentence includes two of the three key components required by the Office of Management and Budget (OMB) Circulars A-128 and A-133. We recommend you revise the first sentence to include the required assessment of internal controls to make it all inclusive of the Federal requirements.

o Footnote 3:

We suggest you replace the reference to the July 1993 exposure draft of proposed changes to Government Auditing Standards with the June 1994 revision of Government Auditing Standards.

Paragraph 6:

o In the case of an audit performed in accordance with either OMB Circular A-128 or A-133, we believe materiality evaluations should be applied at the program level. Consideration should be given to include language to explain that materiality relates to the individual program being evaluated, not to the financial statements as a whole. All too often, materiality thresholds for such audits are improperly established based on the dollars reported in the entity's financial statements which generally far exceeds the dollar amounts associated with specific Federal financial assistance programs.

Enclosure



U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
WASHINGTON, D.C. 20410-4500

OFFICE OF INSPECTOR GENERAL

July 13, 1994

Ms. A. Louise Williamson
Technical Manager
Auditing Standards Division
American Institute of CPAs
1211 Avenue of the Americas
New York, New York 10036-8775

Dear Ms. Williamson:

Thank you for the opportunity to comment on the exposure draft of the proposed statement of auditing standard entitled Compliance Auditing Considerations in Audits of Governmental Entities and Other Recipients of Governmental Assistance. We have reviewed the draft and agree that the provisions of SAS No. 68 on reporting under Government Auditing Standards and responsibilities under the Single Audit Act are too detailed and that a more general standard is desirable. We have the following comments on the proposed SAS:

Paragraph No.

Comment

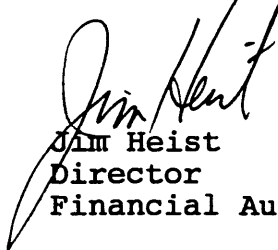
- 13. SAS No. 68, paragraph 11.f., suggested the auditor inquire of program administrators that awarded the grants, to assist in identifying laws and regulations that have a direct and material effect on financial statements. This was not included in the proposed SAS and we believe it should be reinserted.
- 13.g. We suggest that you add "specific program audit guides such as the SFA Audit Guide and the HUD Audit Guide" to the documents containing information about compliance requirements.
- 19.c. We note that the proposed SAS lacks a specific definition of materiality for audits of major Federal financial assistance programs, as was contained in SAS No. 68, paragraph 57. We believe that this paragraph should be added to the proposed SAS.

20. We agree with the requirement to project the amount of known questioned costs. We have noted that auditors are often reluctant to attach costs to the findings they report.

We are sympathetic to the Auditing Standard Board concern for the relationship between costs and benefits. We believe that any costs due to our suggested changes would not exceed the expected benefits.

Thank you again for the opportunity to comment on the proposed auditing standard. Should you have any questions, please contact Peter Bell of my staff at (202) 708-0383.

Sincerely,



Jim Heist
Director
Financial Audits Division



**U.S. Department of
Transportation**

Office of the Secretary
of Transportation

Office of Inspector General

10

July 18, 1994

Ms. A. Louise Williamson
Technical Manager
Auditing Standards Division, File 2357
American Institute of Certified Public Accountants
1211 Avenue of the Americas
New York, New York 10036-8775

Dear Ms. Williamson:

Enclosed are the U.S. Department of Transportation's comments to the Exposure Draft on the Proposed Statement on Auditing Standards, dated May 12, 1994. We are suggesting the proposed statement be revised to recognize the June 1994 revision to the Government Auditing Standards and be expanded to identify a minimum acceptable sample size and to require reporting of likely questioned costs.

I appreciate this opportunity to comment on this new proposed Statement on Auditing Standards. If I can answer any questions or be of further assistance, please feel free to call me on (202) 366-6767.

Sincerely,

Mario A. Lauro, Jr.
Deputy Inspector General

Enclosure

cc:

Mr. James B. Thomas, Jr., Chair, PCIE

PROPOSED STATEMENT ON AUDITING STANDARDS

COMPLIANCE AUDITING CONSIDERATIONS IN AUDITS OF
GOVERNMENTAL ENTITIES AND OTHER RECIPIENTS OF
GOVERNMENTAL FINANCIAL ASSISTANCE

May 12, 1994

Comment Date: July 12, 1994

Name and Affiliation: Mario A. Lauro, Jr., Deputy Inspector General
U.S. Department of Transportation

Comments: The exposure draft on "Compliance Auditing Considerations in Audits of Governmental Entities and Other Recipients of Governmental Financial Assistance" is an improvement over SAS No. 68 in that it does not contain detailed instructions already available in various AICPA accounting and auditing guides and statements of position. We offer the following comments to further improve this proposed Statement on Auditing Standards.

- Footnote 3 should be changed to recognize that in June 1994, the General Accounting Office issued a 1994 revision to the Government Auditing Standards.
- Paragraph 20 should be expanded to provide a minimum sample size. Currently, the selection and testing must include a sufficient number of transactions from each major program to support the auditor's opinion on each major program. The President's Council on Integrity & Efficiency (PCIE) Study on Improving the Single Audit Process recommends the auditor test 40 to 60 transactions when there is a significant compliance requirement and populations of 200 or more. The auditor may reduce the sample size to a minimum of 25 transactions after a major program has been found to be effective and previous audits have not found compliance deviations. We believe this PCIE recommendation should be incorporated into the proposed Statement on Auditing Standards.
- Paragraph 21 states the auditor is not required to report "likely questioned costs," only those that are known. We suggest that auditors be required to report "likely questioned costs." This information would be invaluable to Federal program officials in assessing the impact on their program and assigning priority to obtain appropriate corrective action.



DANIEL G. KYLE, PH.D., CPA, CFE
LEGISLATIVE AUDITOR

OFFICE OF
LEGISLATIVE AUDITOR
STATE OF LOUISIANA
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17

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July 18, 1994

Ms. A. Louise Williamson, Technical Manager
Auditing Standards Division, File 2357
1211 Avenue of the Americas
New York, New York 10036-8775

Dear Ms. Williamson:

I have reviewed the board's exposure draft *Compliance Auditing Considerations in Audits of Governmental Entities and Other Recipients of Governmental Financial Assistance*. I support the issuance of the draft without modification.

Sincerely,

Daniel G. Kyle, CPA, CFE
Legislative Auditor

DGK/GCA/db

SAS68



Secretary of State

Audits Division

Auditing for a Better Oregon

July 19, 1994

Ms. A. Louise Williamson
Technical Manager
Auditing Standards Division, File 2357
AICPA 1211 Avenue of the Americas
New York, NY 10036-8775

Re: Exposure Draft, Proposed Statement on Auditing Standards
Compliance Auditing Considerations in Audits of
Governmental Entities and Other Recipients of
Governmental Financial Assistance

The Oregon Division of Audits agrees with the exposure draft concerning the subject Statement on Auditing Standards dated May 12, 1994.

Revising SAS No. 68 to provide generic rather than specific guidance is desirable. The need for frequent revisions and updates of the SAS is avoided. The specific guidance currently included in SAS No. 68 is more appropriately provided in the AICPA accounting and auditing guides and statements of position.

OREGON AUDITS DIVISION

Georgene L. Bailey
Audit Administrator

GLB:bfs

U.S. SMALL BUSINESS ADMINISTRATION
Washington, D.C. 20416



JUL 21 1994

A. Louise Williamson, Technical Manager
Auditing Standards Division, File 2357
American Institute of Certified Public Accountants
1211 Avenue of the Americas
New York, NY 10036-8775

Dear Ms. Williamson:

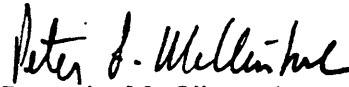
We have reviewed the AICPA Exposure Draft entitled "Proposed Statement on Auditing Standards - Compliance Auditing Considerations in Audits of Governmental Entities and Other Recipients of Governmental Financial Assistance." We have the following suggestions for improving the exposure draft.

1. Page 9, paragraph 1 - We agree with the purpose of the exposure draft (i.e., to provide generic guidance to practitioners performing compliance audits of governmental entities and other recipients of governmental financial assistance). We agree with providing specific guidance in the related statements of position and audit and accounting guides. This would allow changes to be made more easily and timely. In order to ensure that this is understood by practitioners, however, we suggest that you change paragraph 1 to read "...This Statement provides *general* guidance..." [emphasis added] We also suggest that you add a footnote at the word "general" and state that "Specific guidance is provided in the applicable statements of position and audit and accounting guides."
2. Page 10, paragraph 2 - To be consistent with the indented paragraph on that page, and to ensure there is no confusion about funds relating to "structure" instead of "money", we suggest that you change paragraph 2 to read "Such laws and regulations may deal with *fund structure* required by..." [emphasis added]
3. Page 11, paragraph 7 - To be consistent with *Government Auditing Standards*, paragraph 1.1, we recommend you change "...audits of governmental funds received by nonprofit organizations..." to "...audits of government assistance received by contractors, nonprofit organizations..."

4. Page 9, footnote 3 - We suggest that the footnote be updated to reflect the fact that *Government Auditing Standards* has been issued in final.

We thank you for the opportunity to comment on this exposure draft. If you have any questions, please call me on (202) 205-7203.

Sincerely,

A handwritten signature in black ink that reads "Peter L. McClintock". The signature is written in a cursive style with a large initial "P" and a long horizontal stroke at the end.

Peter L. McClintock
Assistant Inspector General
for Auditing

EXPOSURE DRAFT

FILE 2357

PROPOSED STATEMENT ON AUDITING STANDARDS

**COMPLIANCE AUDITING CONSIDERATIONS IN AUDITS OF
GOVERNMENTAL ENTITIES AND OTHER RECIPIENTS OF
GOVERNMENTAL FINANCIAL ASSISTANCE**

May 12, 1994

Comment Date: July 29, 1994

Name and Affiliation: *Montana Office of the Legislative Auditor*

Comments: Members of our staff have reviewed this exposure draft. The generic guidance in the proposed statement is, in our opinion, a positive change and we appreciate the Board's efforts in that direction. In that spirit, we offer the following comments and suggestions.

Footnote 1: This footnote references to an exposure draft of the yellow book. This reference should be revised to reflect the issuance of the revised *Government Auditing Standards*.

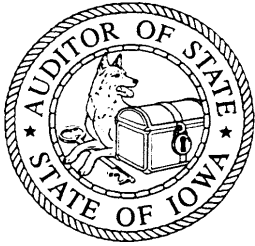
Footnote 5: The structure used in the first sentence is confusing. We offer this alternative: "A subrecipient receives governmental financial assistance initially received by another entity (the primary recipient). The primary recipient distributes the assistance for the government program creating and providing it."

Footnote 6: This footnote introduces the term "federal award" which is not used within the text of the proposed statement. The focus of the footnote should be clarified to explain what "governmental financial assistance" is within the contexts of A-128 and A-133. Are the "federal cost-type contracts" included in the definition of "federal award" subject to the provisions of the proposed statement? Are they excluded because they are separately identified from "financial assistance?"

Paragraphs 14 & 15: Under current OMB Compliance Supplements this information is accurate. However, there has been significant discussion concerning moving the *general* requirements into each federal financial assistance program discussed in the supplements. This change may have an effect on the structure of paragraphs 14 and 15. The compliance supplements also contain suggested audit procedures for each specific requirement listed, yet paragraph 15 does not say that.

The Board may want to consider making modifications to these two paragraphs so they reflect compliance supplement guidance whether modified or not. One suggestion is to not use the term *general*; rather explain that some requirements involve national policy and are applicable to most federal programs.

Please contact Jody Brandt or Vickie Rauser at (406) 444-3122 if you have any questions. Thank you for the opportunity to respond to this exposure draft.



OFFICE OF AUDITOR OF STATE
STATE OF IOWA

Richard D. Johnson, CPA
Auditor of State

State Capitol Building
Des Moines, Iowa 50319-0004
Telephone (515) 281-5834 Facsimile (515) 242-6134

July 21, 1994

A. Louise Williamson, Technical Manager
Auditing Standards Division, File 2357
AICPA
1211 Avenue of the Americas
New York, NY 10036-8775

Dear Ms. Williamson:

RE: "Compliance Auditing Considerations in Audits
of Governmental Entities and Other Recipients
of Governmental Financial Assistance" ED

We agree with the purpose of revising SAS No. 68. Our comments on the ED are as follows:

1. ¶13

This paragraph is from the new audit guide (¶5.11 of the draft). Should there be any cross-referencing?

2. ¶15-18

The details of the OMB specific requirements are well described in SOP 92-7, ¶4.30.

3. ¶22

- a. This topic is separate form ¶19-21.
- b. It could be referenced to A-128.
- c. The details are described SOP 92-7, ¶4.43,4.

4. ¶23-25 Type of Audit Engagement

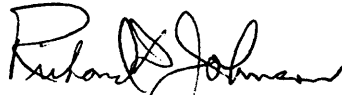
Might it be better to place this after paragraph one?

5. Reporting

One purpose of the revision is to reduce the level of detail but because of the importance of reporting perhaps there should be a brief paragraph stressing its part in auditing governmental financial assistance.

Should you have any questions please write or call me or Don Meadows at 515-281-5538

Very truly yours,


Richard D. Johnson

RDJ/slc

EXPOSURE DRAFT

PROPOSED STATEMENT ON AUDITING STANDARDS

COMPLIANCE AUDITING CONSIDERATIONS IN AUDITS OF GOVERNMENTAL ENTITIES AND
OTHER RECIPIENTS OF GOVERNMENTAL FINANCIAL ASSISTANCE

Dated: May 12, 1994
Comment Date: July 29, 1994
No: 800069

Response Prepared By: Accounting and Auditing standards Committee
Louisiana Society of CPA's
Jon Flair, Chairman
Keith Besson, Member
John Cameron, Member
Daniel Crumb, Member
Larry Johnson, Member
Albert Roevens, Jr., Member
Jimmie Self, Member
Raymond Prince, Technical Consultant
Deborah Zundel, Member

Response Submitted By: Deborah Zundel, Member

Comments:

We have reviewed the board's exposure draft and support the issuance of the draft with the following modifications/suggestions:

In general:

1. It would be helpful to include a Glossary.
2. It would be useful to include an appendix on "Examples of Laws and Regulations that are Generally Recognized by Auditors to have a Direct Effect on a Governmental Entity's Financial Statements", similar to Appendix B in SAS 68.
3. Include specific reporting guidance in the respective audit guide.

Paragraph 1. a. :

Some committee members felt that it should be made more explicit that the content of this paragraph corresponds to the guidance under GAAS mentioned in Paragraph 1.

Accounting and Information
Management Division

July 21, 1994

Ms. A. Louise Williamson
Technical Manager
Auditing Standards Division
File 2357
American Institute of CPAs
1211 Avenue of the Americas
New York, NY 10036-8775

Dear Ms. ^{Louise} ~~Williamson~~:

This letter presents the U.S. General Accounting Office's comments on the proposed Statement on Auditing Standards (SAS), Compliance Auditing Considerations in Audits of Governmental Entities and Other Recipients of Governmental Financial Assistance. This proposed SAS is to supersede SAS No. 68.

First, we believe that this proposed SAS is vague about whether it permits the CPA to report directly on the entity's compliance. The vagueness about direct reporting is compounded by the proposed SAS being ambiguous on the relative authority of Statement on Standards for Attestation Engagements (SSAE) No. 3, Compliance Attestation, and the various AICPA statements of position (SOPs) and audit guides. This SSAE and the various SOPs and audit guides contain much of the guidance on compliance auditing. To resolve this issue, we suggest that the discussion of federal assistance (contained in paragraphs 7 through 11 and 14 through 22) be replaced with the following language:

AICPA has issued statements of position and audit guides prescribing compliance auditing practices that vary from the Statement on Standards for Attestation Engagements No. 3. This SAS permits continued application of those practices. Compliance auditing practices prescribed in subsequent AICPA statements of position and audit guides will also be permitted unless the Auditing Standards Board formally declares otherwise.

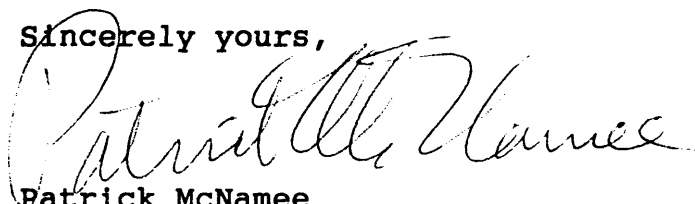
Second, we are disappointed that the proposed SAS appears to undermine the auditors' responsibility for controls over compliance, now required by SAS No. 68. That SAS requires auditors to obtain an understanding of the internal control

structure including knowledge about the design of internal control policies and procedures relevant to financial statement assertions affected by compliance with laws and regulations that have a direct and material effect on the determination of financial statement amounts and about whether those policies and procedures have been placed in operation. (See AU 801.14.)

The proposed SAS does not contain a similar requirement, but instead in paragraph 9 states the auditors' responsibility for controls over compliance varies depending on what federal audit regulations require. The proposed SAS does point out that one element commonly contained in federal audit regulations is to include obtaining an understanding of the accounting and administrative controls established to ensure compliance with the laws and regulations applicable to the federal financial assistance. However, the proposed SAS deletes the explicit statement requiring auditors to understand internal control policies and procedures relevant to financial statement assertions affected by relevant laws and regulations. In addition, the proposed SAS deletes the requirement for auditors to determine whether those policies and procedures have been placed in operation.

Third, the proposed SAS contains guidance that may cause the Auditing Standards Board to once again revise this SAS. For example, paragraph 22 deals with requirements to test non-major program transactions. However, the President's Council on Integrity and Efficiency and GAO studies on the single audit process recommend that this requirement be dropped. The Office of Management and Budget (OMB) officials have proposed to drop this requirement in soon-to-be issued federal regulations revising OMB Circular A-133. We also anticipate other significant changes in the OMB guidelines and in the single audit legislation which will make the proposed SAS inaccurate.

Sincerely yours,



Patrick McNamee
Assistant Director, Legislative
Reviews and Audit Oversight

Linda S. Huneycutt, CPA
7902 Mt. Woodley Place
Alexandria, VA 22306
July 25, 1994

A. Louise Williamson,
Technical Manager,
Auditing Standards Division
File 2357
AICPA
1211 Avenue of the Americas
New York, NY 10036-8775

Dear Ms. Williamson:

I am writing in response to the exposure draft of the proposed statement on auditing standards, "Compliance Auditing Considerations in Audits of Governmental Entities and Other Recipients of Governmental Financial Assistance."


Overall, I think this is a good statement. With the proliferation of governmental regulations, audit and accounting guides, the various SOPs, and other SASs that are applicable to all audits, it is refreshing to see that this proposed SAS incorporates the guidance that is already available and, for the most part, does not duplicate that guidance.

The only change I recommend is at paragraph 1, footnote 3. Since one of the objectives of this proposed SAS is to allow for changes in the accounting and auditing world that will not necessarily entail any changes to this SAS, it seems to me that the last sentence "In July 1993,..." should be eliminated. Perhaps a statement that says "the auditor should be aware that Government Auditing Standards are revised periodically, and should therefore ensure that he is using the most up-to-date version of these Standards."

Thank you for your hard work on this proposed SAS.

If I can be of further assistance, please feel free to call me at 703-548-7200.

Sincerely,



Linda S. Huneycutt



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PENNSYLVANIA INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS

100 Pine Street, Suite 275 · Harrisburg, Pennsylvania 17101-1206 · (717) 232-1821 · FAX (717) 232-7708

July 25, 1994

A. Louise Williamson, Technical Manager
Auditing Standards Division, File 2357, AICPA
1211 Avenue of the Americas
New York, NY 10036-8775

Dear Ms. Williamson:

The Proposed Statement on Auditing Standards adequately addresses compliance auditing considerations in audits of governmental entities and other recipients of governmental financial assistance. As it is stated in the last sentence of the *Why Issued* paragraph of the *Summary*, the proposed Statement would not require frequent revision and updating, which will be helpful to practitioners.

Paragraph 14. *Internal Control Structure* of the Statement on Auditing Standards No. 68 *Compliance Auditing Applicable to Governmental Entities and Other Recipients of Governmental Financial Assistance* contains an excellent discussion of the understanding of the internal control structure required with respect to the financial statement assertions affected by compliance with laws and regulations that have a direct and material effect on the determination of financial statement amounts. Consideration could be given to incorporating this paragraph into the Proposed Statement of Position.

Sincerely yours,

Marcia L. Taylor, CPA
Chairperson



STATE OF TENNESSEE
COMPTROLLER OF THE TREASURY
 DEPARTMENT OF AUDIT
 DIVISION OF STATE AUDIT
 SUITE 1800
 JAMES K. POLK STATE OFFICE BUILDING
 NASHVILLE, TENNESSEE 37243-0204
 PHONE (615) 741-3007

July 27, 1994

Ms. A. Louise Williamson
 Technical Manager, Auditing Standards Division
 American Institute of Certified Public Accountants
 1211 Avenue of the Americas
 New York, NY 10036-8775

Dear Ms. Williamson:

On behalf of the Department of Audit, we appreciate the opportunity to comment on the exposure draft, *Compliance Auditing Considerations in Audits of Governmental Entities and Other Recipients of Governmental Financial Assistance*. We generally support the proposed revision, particularly the concept of providing generic guidance to practitioners engaged to perform compliance audits of governmental entities and other recipients of governmental financial assistance. Eliminating the detailed guidance and example reports included in SAS 68, which are included in other authoritative pronouncements, will reduce the frequency to revise this proposed standard when the other pronouncements are revised.

It may be prudent to delay issuance of this standard until the proposed revisions to federal laws and regulations, such as the Single Audit Act and OMB Circulars A-128 and A-133, are made since these may affect the proposed revision to SAS 68. We offer the following suggestions for your consideration:

INTRODUCTION AND APPLICABILITY

- * Paragraph 1(a) - References to Professional Standards should be omitted, e.g., Volume 1, Section AU 317, if those references might change.
- * Footnote 3 should now refer to the 1994 revision of *Government Auditing Standards*, "Yellow Book."
- * Footnote 4 refers specifically to SOP 92-7 and 92-9. A generic reference to the AICPA Audit Guides and related AICPA SOPs would minimize potential obsolescence when the specified SOPs are revised or incorporated into the ASLGU.

GENERALLY ACCEPTED AUDITING STANDARDS

- * Paragraph 6 - The recently issued Audit and Accounting Guide, *Audits of State and Local Governmental Units* dated July 1, 1994, should be referenced, if necessary.

COMPLIANCE REQUIREMENTS APPLICABLE TO FEDERAL FINANCIAL ASSISTANCE PROGRAMS

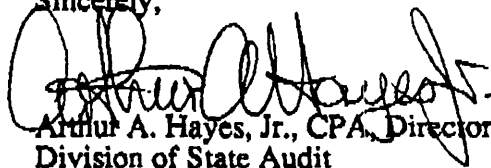
- * Paragraph 14 and Footnote 9 - Considering the revision of the term "general" to "common" in the recent exposure of a part of the Compliance Supplement, the paragraph should refer to "common" and the footnote to "general."
- * Paragraph 16 - It could be incorrectly interpreted that specific requirements for all federal programs are to be obtained from both the OMB's Compliance Supplement and the grant agreement or contract, and that the OMB's Compliance Supplement may be relied upon without review of laws and regulations such as the U.S. Code and the Code of Federal Regulations (Federal Codes). Accordingly, paragraph 16 should be revised as follows, "The auditors should review the applicable Federal Codes for any changes in laws and regulations which might have an impact on the requirements enumerated in the OMB's Compliance Supplements. Specific compliance requirements not included in the OMB's Compliance Supplements may also be enumerated in the applicable Federal Codes and the grant agreement or contract."

EVALUATING RESULTS OF COMPLIANCE AUDIT PROCEDURES ON MAJOR FEDERAL FINANCIAL ASSISTANCE PROGRAMS

- * Paragraph 20 - Same comment as paragraph 1(a), e.g., Volume 1, Section AU 350.
- * Footnote 10 - "A major federal financial assistance program is defined by a federal regulation or law or by the federal grantor agency's audit guide." Do federal grantor agency's audit guides refer to major programs?

Your consideration of our concerns is appreciated. If you have any questions about our comments, please contact Dianne Mitchell of my staff at (615) 741-3697.

Sincerely,


Arthur A. Hayes, Jr., CPA, Director
Division of State Audit

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STATE AUDITOR OF MISSOURI

JEFFERSON CITY, MISSOURI 65102

MARGARET KELLY, CPA
STATE AUDITOR

(314) 751-4824

July 20, 1994

Ms. A. Louise Williamson
Technical Manager
American Institute of Certified
Public Accountants
Auditing Standards Division, File 2357
1211 Avenue of the Americas
New York, NY 10036-8775

Dear Ms. Williamson:

Enclosed are our comments on the proposed Statement on Auditing Standards,
Compliance Auditing Considerations in Audits of Governmental Entities and Other Recipients
of Governmental Financial Assistance.

If you have any questions regarding our comments, please contact Myrana Gibler,
Audit Manager, of my office at (314) 751-4213.

Sincerely,

Margaret Kelly, CPA
State Auditor

MK:sb

Enclosures

**COMMENTS - PROPOSED STATEMENT ON AUDITING STANDARDS,
COMPLIANCE AUDITING CONSIDERATIONS IN AUDITS
OF GOVERNMENTAL ENTITIES AND OTHER RECIPIENTS
OF GOVERNMENTAL FINANCIAL ASSISTANCE**

The Office of Missouri State Auditor appreciates the opportunity to comment on the proposed Statement on Auditing Standards (SAS), Compliance Auditing Considerations in Audits of Governmental Entities and Other Recipients of Governmental Financial Assistance.

GENERAL COMMENTS

Coordination of Revisions

We agree with the Auditing Standards Board's decision to replace SAS No. 68 with the general guidance in the proposed SAS. We believe this change is necessary to reduce the frequency of revisions to the auditing standards and to eliminate duplication of detailed information between the standards and the applicable Audit and Accounting Guides and Statements of Position (SOPs). However, we also suggest the issuance of the proposed SAS be coordinated with revisions to federal documents applicable to single or organization-wide audits; otherwise, the SAS may quickly become dated.

For example, we are aware of the following information that could affect the contents of the SAS:

1. page 13, paragraph 14, and page 14, paragraph 18 - These paragraphs continue to refer to general requirements, noting that the term "common requirements" also may apply. The partial draft of proposed revisions to the Office of Management and Budget (OMB) Compliance Supplement for Single Audits of State and Local Governments, circulated for comment earlier this year, replaces "general" with "common."
2. page 14, paragraph 21 - This paragraph states that federal audit regulations may require the auditor to report any instances of noncompliance found and any resulting questioned costs. The Study on Improving the Single Audit Process issued by the President's Council on Integrity and Efficiency in 1993 (hereafter referred to as the PCIE Single Audit Study) recommends that the auditor be permitted to report minor instances of noncompliance separately in writing [recommendation 5.5(a), page 71]. This recommendation is being considered by the federal government in the revisions to OMB Circular A-133.

3. pages 14-15, paragraph 22 - This paragraph states that transactions selected from other than major federal financial assistance (FFA) programs in connection with the financial statement audit or the consideration of the internal control structure over FFA programs should be tested for compliance with the requirements applicable to the individual transactions. The PCIE Single Audit Study recommends that this compliance testing requirement be removed [recommendation 2.1(d), page 20]. This recommendation also is being considered in the revisions to OMB Circular A-133.

Additional Guidance

As part of our review, we identified the paragraphs of SAS No. 68 that were removed in the proposed SAS and compared those paragraphs with the information in SOPs 92-7 and 92-9. Based on that comparison, we believe the information in the SOPs to be sufficiently detailed to compensate for the removal of most of the SAS No. 68 paragraphs. However, we did identify the following SAS No. 68 paragraphs that appear to include information in addition to the SOPs' information or to discuss certain topics more thoroughly than the SOPs: AU secs. 801.12-.15 (considering risk) and AU sec. 801.19 (written representations from management), relevant to compliance auditing in audits conducted in accordance with generally accepted auditing standards (GAAS). We suggest these paragraphs either be reinserted into the proposed Statement or be considered for future revisions to the SOPs.

SPECIFIC COMMENTS

COMPLIANCE AUDITING

Government Auditing Standards

page 11, paragraphs 7-8 - We suggest these paragraphs summarize the auditor's compliance auditing responsibilities under Government Auditing Standards, to be consistent with the paragraphs on the other three types of audits—audits under GAAS, federal audit requirements, and state and local laws and regulations. Those responsibilities are stated in paragraphs 4.12-4.13 on pages 35-36 of the 1994 revisions to Government Auditing Standards.

Federal Audit Requirements

page 12, paragraph 11 - We believe this paragraph could be omitted since the auditor's responsibility to determine and report on compliance is apparent from paragraph 9.d. and the last sentence of paragraph 10.

COMPLIANCE REQUIREMENTS APPLICABLE TO FEDERAL FINANCIAL ASSISTANCE PROGRAMS

page 13, paragraphs 14-17 - We have three concerns regarding these paragraphs:

1. The second sentence of paragraph 14 does not include three words, “all or most,” before “federal financial assistance programs” that are needed to clearly distinguish between the general and specific requirements. Also, those words currently appear in both OMB Compliance Supplement discussions of the general requirements.
2. Listing the categories of specific requirements in paragraph 15, but not the general requirements in paragraph 14, is inconsistent (unless the general requirements were intentionally not listed because they are currently under revision by the OMB).
3. The paragraphs seem unnecessarily repetitious. For example, the Compliance Supplements as a source of compliance requirements are repeated in paragraphs 14-16, grant agreements or contracts as a source of requirements in paragraphs 16-17, and the Compliance Supplements as a source of suggested audit procedures for compliance requirements in paragraphs 14 and 17.

Accordingly, we suggest the following paragraphs as possible revisions:

Compliance requirements applicable to federal financial assistance programs are usually of two types: general¹ and specific. General requirements involve national policy and apply to all or most federal financial assistance programs. Specific requirements apply to a particular federal program and generally arise from statutory requirements and regulations. The OMB’s Compliance Supplements set forth general and specific requirements for the federal programs awarded to state and local governments and to nonprofit organizations and suggested audit procedures to test for compliance with the requirements.

For program-specific audits, the auditor should consult federal grantor agency audit guides (e.g., for example, the SFA Audit Guide) to identify common requirements that are statutory and regulatory requirements pertaining to certain federal programs, specific

¹ See also our comments on page 1 regarding use of the term “general.”

requirements for a particular program, and suggested audit procedures to test for compliance with the requirements.

In addition to those identified in the OMB's Compliance Supplements or federal grantor agency audit guides, specific requirements may also be enumerated in grant agreements or contracts.

EVALUATING RESULTS OF COMPLIANCE AUDIT PROCEDURES ON MAJOR FEDERAL FINANCIAL ASSISTANCE PROGRAMS

page 14, paragraph 21 - We suggest the second sentence be clarified by including a specific reference from Government Auditing Standards. Paragraph 5.19 on pages 53-54 of the 1994 revisions would appear to apply.

OTHER COMMENTS

On the enclosed draft, we have indicated several suggested editorial changes. Also, during our review we noted two document references for which changes should be considered:

1. page 9, footnote 3 - The last sentence should be removed to reflect the issuance of the 1994 revisions to Government Auditing Standards.
2. page 11, paragraph 6 - If the Audit and Accounting Guide Audits of State and Local Governmental Units is issued before the proposed SAS is finalized, the date in the last sentence should be changed or deleted.

EXPOSURE DRAFT

PROPOSED STATEMENT ON AUDITING STANDARDS

COMPLIANCE AUDITING CONSIDERATIONS IN AUDITS OF GOVERNMENTAL ENTITIES AND OTHER RECIPIENTS OF GOVERNMENTAL FINANCIAL ASSISTANCE

*(To Supersede SAS No. 68, Compliance Auditing Applicable
to Governmental Entities and Other Recipients of
Governmental Financial Assistance)*

MAY 12, 1994

**Prepared by the Auditing Standards Board
American Institute of Certified Public Accountants**

**Comments should be received by July 29, 1994, and addressed to A. Louise Williamson,
Technical Manager, Auditing Standards Division, File 2357
AICPA, 1211 Avenue of the Americas, New York, NY 10036-8775**

800069

This exposure draft has been sent to —

- Members who have asked to receive a copy of every exposure draft issued by one or more components of the AICPA.
 - Members of AICPA Council and technical committees.
 - State society and chapter presidents, directors, and committee chairs, with sufficient copies for the members of the committee that would normally be expected to comment.
 - Organizations concerned with regulatory, supervisory, or other public disclosure of financial activities.
 - Selected industry associations.
 - Members and others who ask to receive a copy.
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AICPA

American
Institute of
Certified
Public
Accountants

1211 Avenue of the Americas
New York, NY 10036-8775

(212) 596-6200
Fax (212) 596-6213

May 12, 1994

Accompanying this letter is an exposure draft, approved by the Auditing Standards Board, of a proposed statement on auditing standards that, when final, would supersede Statement on Auditing Standards No. 68, *Compliance Auditing Applicable to Governmental Entities and Other Recipients of Governmental Financial Assistance*. A summary of the proposed Statement also accompanies this letter.

Comments or suggestions on any aspect of this exposure draft will be appreciated. To facilitate consideration of responses by the Auditing Standards Board, comments should refer to specific paragraphs and include supporting reasons for each suggestion or comment.

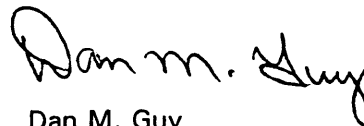
In developing guidance, the Auditing Standards Board considers the relationship between the cost imposed and the benefits reasonably expected to be derived from audit engagements. It also considers the differences an auditor may encounter in an audit engagement involving small entities and, when appropriate, makes special provisions to meet those needs. Thus, the Board would particularly appreciate comments on those matters.

Written comments on the exposure draft will become part of the public record of the AICPA Auditing Standards Division and will be available for public inspection at the offices of the AICPA after August 31, 1994, for one year. Responses should be sent to A. Louise Williamson, Technical Manager, Auditing Standards Division, File 2357, AICPA, 1211 Avenue of the Americas, New York, NY 10036-8775 in time to be received by July 29, 1994.

Sincerely,



John B. Sullivan
Chair
Auditing Standards Board



Dan M. Guy
Vice President
Auditing

SUMMARY

Why Issued

The Auditing Standards Board is issuing this proposed statement on auditing standards to revise the guidance contained in Statement on Auditing Standards (SAS) No. 68, *Compliance Auditing Applicable to Governmental Entities and Other Recipients of Governmental Financial Assistance* (AICPA, *Professional Standards*, vol. 1, AU sec. 801). This proposed Statement would provide generic guidance to practitioners engaged to perform compliance audits of governmental entities and other recipients of governmental financial assistance. In addition, this proposed Statement would not require frequent revision and updating because it does not identify compliance requirements or specify the form of reporting.

What It Does

This proposed Statement —

- a. Recognizes three levels of audits (generally accepted auditing standards, *Government Auditing Standards*, and certain other federal requirements) of recipients of governmental financial assistance.
- b. Reduces the level of detail included in the auditing standards. (Specific performance and reporting guidance would be included, more appropriately, in the applicable audit and accounting guides and statements of position.)

How It Affects Existing Standards

This proposed Statement would supersede SAS No. 68, *Compliance Auditing Applicable to Governmental Entities and Other Recipients of Governmental Financial Assistance*. Furthermore, as a consequence of the foregoing change, the proposed Statement would require conforming changes to and updating of the guidance in related statements of position and audit and accounting guides.

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PROPOSED STATEMENT ON AUDITING STANDARDS

COMPLIANCE AUDITING CONSIDERATIONS IN AUDITS OF GOVERNMENTAL ENTITIES AND OTHER RECIPIENTS OF GOVERNMENTAL FINANCIAL ASSISTANCE

INTRODUCTION AND APPLICABILITY

1. Compliance auditing considerations are applicable to all audits of financial statements of governmental entities and other recipients of governmental financial assistance. This Statement provides guidance for auditors who are engaged to test and report on compliance with laws and regulations in engagements under generally accepted auditing standards (GAAS), *Government Auditing Standards*, and in certain other circumstances,¹ such as single or organization-wide audits or program audits under certain federal audit regulations.² Specifically, this Statement provides guidance on the auditor's responsibility to —

- a. Apply the provisions of Statement on Auditing Standards (SAS) No. 54, *Illegal Acts by Clients* (AICPA, *Professional Standards*, vol. 1, AU sec. 317), relative to detecting misstatements resulting from illegal acts related to laws and regulations that apply to governmental financial assistance or that have a direct and material effect on the determination of financial statement amounts in audits of the financial statements of governmental and certain nongovernmental entities.
- b. Perform an audit in accordance with *Government Auditing Standards*, issued by the Comptroller General of the United States.³
- c. Perform a single or organization-wide audit or a program audit in accordance with federal audit requirements.⁴
- d. Establish an understanding with management regarding the auditor's testing and reporting responsibilities when engaged to test and report on compliance with state or local laws and regulations.

perhaps unnecessary since phrase "test and report" is used later in sentence

¹ Guidance for engagements related to management's written assertion about either (a) an entity's compliance with requirements of specified laws, regulations, rules, contracts, or grants or (b) the effectiveness of an entity's internal control structure over compliance with specified requirements is provided in Statement on Standards for Attestation Engagements No. 3, *Compliance Attestation* (AICPA, *Codification of Statements on Auditing Standards* [Nos. 1–72], AT sec. 500).

² A single or organization-wide audit is an audit of an entity's financial statements and of compliance with federal regulations relating to federal financial assistance. Examples are audits required by the Single Audit Act of 1984 and Office of Management and Budget (OMB) Circular A-128, *Audits of State and Local Governments*, or OMB Circular A-133, *Audits of Institutions of Higher Education and Other Nonprofit Institutions*. A program audit is an audit conducted in accordance with specific federal audit guides, such as the U.S. Department of Education's *Student Financial Assistance Audit Guide* (SFA Audit Guide), or the U.S. Department of Housing and Urban Development's *Consolidated Audit Guide for Audits of HUD Programs* (HUD Audit Guide).

³ In practice, *Government Auditing Standards* is sometimes referred to as *generally accepted government auditing standards* (GAGAS) or the "Yellow Book." *Government Auditing Standards* includes standards for financial and performance audits. The references to *Government Auditing Standards* in this Statement encompass only the standards for financial audits, not the performance audit standards. In July 1993, the General Accounting Office (GAO) issued an exposure draft of proposed changes to *Government Auditing Standards*.

⁴ Certain single or organization-wide audit testing and reporting responsibilities are addressed in AICPA Statements of Position (SOPs) 92-7, *Audits of State and Local Governmental Entities Receiving Federal Financial Assistance*, and 92-9, *Audits of Not-for-Profit Organizations Receiving Federal Awards*, and are, therefore, not addressed by this Statement.

standards

9

Changed to use parallel grammatical structures for references to both types of standards

- e. Communicate with management when the auditor becomes aware that the entity is subject to an audit requirement that may not be encompassed in the terms of his or her engagement.

EFFECTS OF LAWS ON FINANCIAL STATEMENTS

Paranetical phrase probably not needed since Codification is not referred to in remainder of document.

2. The Governmental Accounting Standards Board's *Codification of Governmental Accounting and Financial Reporting Standards* (GASB Codification), section 1200.103, recognizes that governmental entities generally are subject to a variety of laws and regulations that affect their financial statements:

An important aspect of GAAP [generally accepted accounting principles] as applied to governments is the recognition of the variety of legal and contractual considerations typical of the government environment. These considerations underlie and are reflected in the fund structure, bases of accounting, and other principles and methods set forth here, and are a major factor distinguishing governmental accounting from commercial accounting.

Such laws and regulations may deal with funds required by law, regulation, or bond covenant; procurement; debt limitations; and legal authority for transactions.

3. Federal, state, and local governmental entities provide financial assistance to other entities, including not-for-profit organizations and business enterprises that are either primary recipients or subrecipients.⁵ Among the forms of governmental financial assistance are grants of cash and other assets, loans, loan guarantees, and interest-rate subsidies.⁶ By accepting such assistance, both governmental and nongovernmental entities may be subject to laws and regulations that may have a direct and material effect on the determination of amounts in their financial statements.

4. Management is responsible for ensuring that the entity complies with the laws and regulations applicable to its activities. That responsibility encompasses identification of applicable laws and regulations and establishment of internal control policies and procedures designed to provide reasonable assurance that the entity complies with those laws and regulations. The auditor's responsibility for testing and reporting on compliance with laws and regulations varies according to the terms of the engagement.

This word appears in the same SAS No. 68 paragraph structure. All sec. 8c1.02.

⁵ A subrecipient is an entity that receives governmental financial assistance when the assistance is initially received by another entity (the primary recipient) that distributes the assistance for the government program that created and provided the assistance. As used in this Statement, recipient means either a primary recipient or a subrecipient.

⁶ For purposes of this Statement, *financial assistance*, as defined by the Single Audit Act of 1984 and OMB Circular A-128, does not include contracts to provide goods or services to a governmental entity or arrangements in which a nongovernmental entity purchases insurance from the government. Federal awards, as defined by OMB Circular A-133, means financial assistance and federal cost-type contracts used to buy services or goods for the use of the federal government. Federal awards do not include procurement contracts to vendors under grants or contracts used to buy goods or services. For example, financial assistance does not include a contract to design and manufacture aircraft for the U.S. Air Force or the purchase of deposit insurance by a financial institution. In addition, although Medicaid funds paid by the federal government to states constitute financial assistance, most Medicaid arrangements between the states and health-care providers are contracts for services that are not considered to be financial assistance.

COMPLIANCE AUDITING

Generally Accepted Auditing Standards

5. SAS No. 54 describes the auditor's responsibility, in an audit performed in accordance with GAAS, for considering laws and regulations and how they affect the audit.

6. Thus, the auditor should design the audit to provide reasonable assurance that the financial statements are free of material misstatements resulting from violations of laws and regulations that have a direct and material effect on the determination of financial statement amounts. Paragraph 5.5 of the AICPA Audit and Accounting Guide *Audits of State and Local Governmental Units* (as of May 1, 1993) states that for general purpose financial statements "[e]xisting audit practice is that audit scope should be set and materiality evaluations should be applied at the fund type and account group level...."

Government Auditing Standards

Made minor editorial changes based on paragraph 1.1 of 1994 revisions to Government Auditing Standards assistance Contractors,

7. *Government Auditing Standards* contains standards for audits of governmental organizations, programs, activities, and functions and for audits of governmental funds received by nonprofit organizations and other nongovernmental organizations. These standards are to be followed when required by law, regulation, agreement, contract, or policy.⁷

8. For financial audits, *Government Auditing Standards* prescribes fieldwork and reporting standards beyond those required by GAAS. The general standards of *Government Auditing Standards* relate to qualifications of the staff (including continuing education requirements), independence, due professional care, and quality control.

Federal Audit Requirements

9. Although the scope and reporting requirements of an audit of a recipient of federal financial assistance in accordance with federal audit regulations vary, the audits generally have the following elements in common:

Deleted outdated phrase not used in SOP 92-7

- a. The audit is to be conducted in accordance with GAAS and *Government Auditing Standards*.
- b. ~~The auditor's consideration of the internal control structure is to include obtaining an understanding of the accounting and administrative controls established to ensure compliance with the laws and regulations applicable to the federal financial assistance. In some instances, federal audit regulations mandate a "test of controls" to evaluate the effectiveness of the design and operation of the policies and procedures in preventing or detecting material noncompliance.~~ *policies and procedures*
- c. The auditor is to issue a report on the consideration of the internal control structure described above.
- d. The auditor is to determine and report on whether the federal financial assistance has been administered in accordance with applicable laws and regulations (that is, compliance requirements).

⁷ Some states have adopted regulations that require local governments within the states to have their audits conducted in accordance with *Government Auditing Standards*. In addition, some states require that recipients of state financial assistance be audited in accordance with *Government Auditing Standards*.

- e. Review minutes of meetings of the legislative body of the governmental entity being audited for the enactment of laws and regulations that have a direct and material effect on the determination of amounts in the governmental entity's financial statements.
- f. Inquire of the office of the federal, state, or local auditor or other appropriate audit oversight organization about laws and regulations applicable to entities within their jurisdiction, including statutes and uniform reporting requirements.
- g. Review information about compliance requirements, such as the information included in *the Compliance Supplement for Single Audits of State and Local Governments*, and *the Compliance Supplement for Audits of Institutions of Higher Learning and Other Non-Profit Institutions*, issued by the OMB (OMB's Compliance Supplements), and *Catalog of Federal Domestic Assistance*, issued by the Government Printing Office.

the
 (usually see the titles of these publications preceded by "the")

COMPLIANCE REQUIREMENTS APPLICABLE TO FEDERAL FINANCIAL ASSISTANCE PROGRAMS

14. Compliance requirements applicable to federal financial assistance programs are usually of two types: *general*⁹ and *specific*. General requirements are those that involve national policy and are applicable to federal financial assistance programs. General requirements for the federal programs awarded to state and local governments and to nonprofit organizations are set forth in the OMB's Compliance Supplements. Each general requirement is accompanied by suggested audit procedures to test for compliance with the requirement.

15. Specific requirements are those that are applicable to a particular federal program and generally arise from statutory requirements and regulations. The specific requirements in the OMB's Compliance Supplements are generally organized into five categories:

- a. Types of service allowed or unallowed
- b. Eligibility
- c. Matching, level of effort, and/or earmarking requirements
- d. Special reporting requirements
- e. Special tests and provisions

16. In addition to those enumerated in the OMB's Compliance Supplements, specific compliance requirements may also be enumerated in the grant agreement or contract.

17. If a program-specific audit is being performed, the auditor should consider common requirements that are statutory and regulatory requirements pertaining to certain federal programs. The common requirements are set forth in the federal grantor agency's audit guide (for example, the SFA Audit Guide). Specific requirements for program audits are enumerated in a federal grantor agency's audit guide for particular programs, in the grant agreement or contract, or in both. The OMB's Compliance Supplements and the federal grantor agency audit guides provide suggested audit procedures that may be used to test for compliance with a specific requirement.

⁹ General requirements also may be referred to as *common* requirements. (See paragraphs 17 and 18 of this Statement.)

- e. Review minutes of meetings of the legislative body of the governmental entity being audited for the enactment of laws and regulations that have a direct and material effect on the determination of amounts in the governmental entity's financial statements.
- f. Inquire of the office of the federal, state, or local auditor or other appropriate audit oversight organization about laws and regulations applicable to entities within their jurisdiction, including statutes and uniform reporting requirements.
- g. Review information about compliance requirements, such as the information included in *the Compliance Supplement for Single Audits of State and Local Governments*, and *the Compliance Supplement for Audits of Institutions of Higher Learning and Other Non-Profit Institutions*, issued by the OMB (OMB's Compliance Supplements), and *Catalog of Federal Domestic Assistance*, issued by the Government Printing Office.

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programs, the auditor may have selected for testing transactions from federal financial assistance programs other than major programs. If the auditor has selected such transactions, they should be tested for compliance with the requirements that apply to the individual transactions — generally, the requirements relating to the allowability of the program expenditure and the eligibility of the individuals or groups to which the entity provides federal financial assistance. For example, if in the audit of the financial statements an auditor examines a payroll transaction that was charged to a nonmajor program, the auditor should determine whether the position could reasonably be charged to that program and whether the individual's salary was correctly charged to that program.

TYPE OF AUDIT ENGAGEMENT

23. Management is responsible for obtaining audits that satisfy relevant legal, regulatory, or contractual requirements. Auditors should exercise due professional care in ensuring that they and management understand the type of engagement to be performed. When a proposal, contract, or engagement letter is used, an auditor may consider including in it a statement about the type of engagement and whether the engagement is intended to meet specific audit requirements.

24. Generally accepted auditing standards do not require the auditor to perform procedures beyond those he or she considers necessary to obtain sufficient competent evidential matter to form a basis for the opinion on the financial statements. Therefore, if during a GAAS audit of the financial statements the auditor becomes aware that the entity is subject to an audit requirement that may not be encompassed in the terms of the engagement, the auditor should communicate to management and the audit committee, or to others with equivalent authority and responsibility, that an audit in accordance with GAAS may not satisfy the relevant legal, regulatory, or contractual requirements.¹² For example, the auditor will be required to make this communication if an entity engages an auditor to perform an audit of its financial statements in accordance with GAAS and the auditor becomes aware that by law, regulation, or contractual agreement the entity also is required to have an audit performed in accordance with one or more of the following:

- a. *Government Auditing Standards*
- b. The Single Audit Act of 1984 and OMB Circular A-128, *Audits of State and Local Governments*
- c. OMB Circular A-133, *Audits of Institutions of Higher Education and Other Nonprofit Institutions*
- d. Other compliance audit requirements, such as state or local laws or program audits under federal audit guides

Might be deleted since full titles appear in footnote 2, page 9

Audits of State and Local Governments X

Audits of Institutions of Higher Education and Other Nonprofit Institutions |

25. The communication required by paragraph 24 of this Statement may be oral or written. If the communication is oral, the auditor should document the communication in the working papers. The auditor should consider how the client's actions in response to such communication relate to other aspects of the audit, including the potential effect on the financial statements and on the auditor's report on those financial statements. Specifically, the auditor should consider

¹² For entities that do not have an audit committee, "others with equivalent authority or responsibility" may include the board of directors, the board of trustees, the owner in owner-managed entities, the city council, or the legislative standing committee.

programs, the auditor may have selected for testing transactions from federal financial assistance programs other than major programs. If the auditor has selected such transactions, they should be tested for compliance with the requirements that apply to the individual transactions — generally, the requirements relating to the allowability of the program expenditure and the eligibility of the individuals or groups to which the entity provides federal financial assistance. For example, if in the audit of the financial statements an auditor examines a payroll transaction that was charged to a nonmajor program, the auditor should determine whether the position could reasonably be charged to that program and whether the individual's salary was correctly charged to that program.

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ASSOCIATION of GOVERNMENT ACCOUNTANTS

July 28, 1994

Ms. A. Louise Williamson
Technical Manager, Auditing Standards Division
American Institute of Certified Public Accountants
1211 Avenue of the Americas
New York, NY 10036-8775

Dear Ms. Williamson:

On behalf of the Association of Government Accountant's Financial Management Committee, we appreciate the opportunity to comment on the exposure draft, *Compliance Auditing Considerations in Audits of Governmental Entities and Other Recipients of Governmental Financial Assistance*. The following comments represent a simple majority based on responses received from members.

We have reviewed the exposure draft (ED), and we agree with the Auditing Standards Board's decision to replace SAS 68 with generic guidance to practitioners engaged to perform compliance audits of governmental entities and other recipients of governmental financial assistance. We believe this change is necessary to reduce the frequency of revisions to the auditing standards and to eliminate duplication of detailed information between the standards and the applicable Audit and Accounting Guides and Statements of Position (SOPs).

We also suggest that the issuance of the proposed SAS be coordinated with revisions to federal documents applicable to single or organization-wide audits; otherwise, the SAS may quickly become outdated. For example, paragraphs 20 and 21 state that federal audit regulations may require the auditor to report any instances of noncompliance found and any resulting questioned costs. The *Study on Improving the Single Audit Process* issued in 1993 by the President's Council on Integrity and Efficiency (hereafter referred to as the PCIE Single Audit Study) recommends that the auditor be permitted to report minor instances of noncompliance separately in writing (recommendation 5.5(a), page 71). This recommendation is being considered by the federal government in the revisions to OMB Circular A-133. In addition, paragraph 22 states that transactions selected from other than major federal financial assistance (FFA) programs in connection with the financial statement audit or the consideration of the internal control structure over FFA programs should be tested for compliance with the requirements applicable to the individual transactions. The

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July 28, 1994

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July 28, 1994

GENERALLY ACCEPTED AUDITING STANDARDS

- * Paragraph 6 - Since the ASLGU has been revised, the reference in this sentence is most likely obsolete.

FEDERAL AUDIT REQUIREMENTS

- * Paragraph 9(b) - For consistency with Section AU 319.26 of the *Codification of Statements on Auditing Standards*, we suggest that the first sentence be revised slightly to read, "The auditor's consideration of the internal control structure is to include obtaining and documenting an understanding of the accounting and administrative controls . . ." In addition, this paragraph uses the terminology "accounting and administrative controls." Other literature, i.e., SAS 55 and SOP 92-7, no longer uses those terms.

UNDERSTANDING THE EFFECTS OF LAWS AND REGULATIONS

- * Paragraph 13 - The paragraph lists several procedures the auditor should consider performing to assist in assessing management's identification of laws and regulations. First, paragraph 13(e) states, "Review minutes of meetings of the legislative body of the governmental entity . . ." In addition to a legislative body that enacts laws and ordinances (e.g., city council, county commission, state legislature), many governmental entities also have a governing board that establishes rules and regulations (e.g., administrative board, board of trustees). Therefore, to provide more comprehensive guidance to the auditor, we suggest that paragraph 13(e) be expanded to read, "Review minutes of meetings of the legislative body and/or the governing board of the governmental entity . . ." Second, paragraph 13(g) states, "Review information about compliance requirements . . ." It lists three federal documents as examples. Because state governments may also establish compliance requirements, we suggest that paragraph 13(g) be expanded to include ". . . and State policies and procedures."

COMPLIANCE REQUIREMENTS APPLICABLE TO FEDERAL FINANCIAL ASSISTANCE ASSISTANCE PROGRAMS

- * Paragraph 14 and Footnote 9 - Considering the revision of the term "general" to "common" in the recent exposure of a part of the Compliance Supplement, the paragraphs should refer to "common" and the footnote to "general."
- * Paragraph 16 - It could be incorrectly interpreted that specific requirements for all federal programs are to be obtained from both the OMB's Compliance Supplement and the grant agreement or contract, and that the OMB's Compliance Supplement may be relied upon without review of laws and regulations such as the U.S. Code and the Code of Federal Regulations (Federal Codes). Accordingly, paragraph 16 should be revised as follows, "The auditors should review the applicable Federal Codes for any changes in laws and regulations which might have an impact on the requirements enumerated in the OMB's Compliance Supplements. Specific compliance requirements not included in the OMB's Compliance Supplements may also be enumerated in the applicable Federal Codes, applicable federal acts, and the grant agreement or contract."

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Accordingly, we suggest the following paragraphs as possible revisions:

Compliance requirements applicable to federal financial assistance programs are usually of two types: general and specific. General requirements involve national policy and apply to all or most federal financial assistance programs.

Specific requirements apply to a particular federal program and generally arise from statutory requirements and regulations. The OMB's Compliance Supplements set forth general and specific requirements for the federal programs awarded to state and local governments and to nonprofit organizations and suggested audit procedures to test for compliance with the requirements.

For program-specific audits, the auditor should consult federal grantor agency audit guides (e.g., the SFA Audit Guide) to identify common requirements that are statutory and regulatory requirements pertaining to certain federal programs, specific requirements for a particular program, and suggested audit procedures to test for compliance with the requirements.

In addition to those identified in the OMB's Compliance Supplements or federal grantor agency audit guides, specific requirements may also be enumerated in grant agreements or contracts.

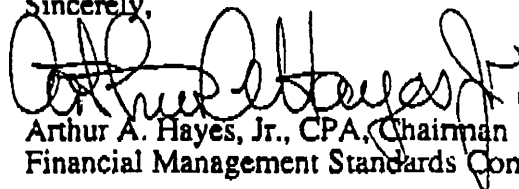
- * Footnote 10 - "A major federal financial assistance program is defined by a federal regulation or law or by the federal grantor agency's audit guide." Do federal grantor agency's audit guides refer to major programs?
- * Footnote 11 states, "Detailed testing and reporting guidance on single or organization-wide audits and program audits is provided in the AICPA Audit and Accounting Guide *Audits of State and Local Governmental Units* and in AICPA SOPs 92-7 and 92-9." Because the AICPA has incorporated SOP 92-7 in the new Guide (as Chapters 5, 20-24 and Appendix A), the footnote is misleading. We suggest revision to the footnote as follows: "Detailed testing and reporting guidance on single or organization-wide audits and program audits is provided in the AICPA Audit and Accounting Guide *Audits of State and Local Governmental Units* and in AICPA SOP 92-9."

EVALUATING RESULTS OF COMPLIANCE AUDIT PROCEDURES ON MAJOR FEDERAL FINANCIAL ASSISTANCE PROGRAMS

- * Paragraph 20 - Same comment as paragraph 1(a), e.g., Volume 1, Section AU 350.

Your consideration of our concerns is appreciated.

Sincerely,



Arthur A. Hayes, Jr., CPA, Chairman
Financial Management Standards Committee

cc: Committee members
Clyde G. McShan, II
Dianne Mitchell
Thomas L. Woods

National State Auditors Association



July 28, 1994

OFFICERS AND EXECUTIVE COMMITTEE

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Delaware

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State Auditor
California

Ms. A. Louise Williamson
Technical Manager, Auditing Standards Division
American Institute of Certified Public Accountants
1211 Avenue of the Americas
New York, NY 10036-8775

Dear Ms. Williamson:

On behalf of the National State Auditors Association (NSAA), we appreciate the opportunity to comment on the exposure draft, *Compliance Auditing Considerations in Audits of Governmental Entities and Other Recipients of Governmental Financial Assistance*. The following comments represent a simple majority based on responses received from members; therefore, some members may not entirely agree with the comments in this letter. Individual state auditors were encouraged to comment separately.

We have reviewed the exposure draft (ED), and we agree with the Auditing Standards Board's decision to replace SAS 68 with generic guidance to practitioners engaged to perform compliance audits of governmental entities and other recipients of governmental financial assistance. We believe this change is necessary to reduce the frequency of revisions to the auditing standards and to eliminate duplication of detailed information between the standards and the applicable Audit and Accounting Guides and Statements of Position (SOPs).

We also suggest that the issuance of the proposed SAS be coordinated with revisions to federal documents applicable to single or organization-wide audits; otherwise, the SAS may quickly become outdated. For example, paragraphs 20 and 21 state that federal audit regulations may require the auditor to report any instances of noncompliance found and any resulting questioned costs. The *Study on Improving the Single Audit Process* issued in 1993 by the President's Council on Integrity and Efficiency (hereafter referred to as the PCIE Single Audit Study) recommends that the auditor be permitted to report minor instances of noncompliance separately in writing (recommendation 5.5(a), page 71). This recommendation is being considered by the federal government in the revisions to OMB Circular A-133. In addition, paragraph 22 states that transactions selected from other than major federal financial assistance (FFA) programs in connection with the financial statement audit or the consideration of the internal control

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structure over FFA programs should be tested for compliance with the requirements applicable to the individual transactions. The PCIE Single Audit Study recommends that this compliance testing requirement be removed (recommendation 2.1(d), page 20). This recommendation also is being considered in the revisions to OMB Circular A-133.

As part of our review, we identified the paragraphs of SAS 68 that were removed from the proposed SAS and compared those paragraphs with the information in SOPs 92-7 and 92-9. Based on that comparison, we believe the information in the SOPs to be sufficiently detailed to compensate for the removal of most of the SAS 68 paragraphs. However, we did identify two SAS 68 paragraphs that appear to include information in addition to that provided in the SOPs to discuss certain topics more thoroughly than is done in the SOPs: AU secs. 801.12-15 (considering risk) and AU sec. 801.19 (written representations from management). We suggest that these paragraphs either be reinserted into the proposed statement or be considered for future revisions to the SOPs.

INTRODUCTION AND APPLICABILITY

- * Footnote 1 refers the auditor to Statement on Standards for Attestation Engagements 3 for guidance on engagements related to management's written assertions. The ED, however, does not also refer the auditor to the guidance on auditing for compliance with aspects of contractual agreements or regulatory requirements related to financial statements, contained in Statement of Auditing Standards (SAS) No. 62, *Special Reports*. It appears that the board intends that all compliance auditing, beyond the scope covered in this ED, be subject to the AICPA's attestation standards. We object to this apparent initiative because most users expect a compliance report in relation to the financial statements or major federal programs and because the attestation standards lack materiality criteria users can understand. Therefore, we suggest that the board expand footnote 1 to also refer the auditor to SAS 62 for guidance on compliance reports.
- * The last sentence of footnote 3 states, "In July 1993, the General Accounting Office (GAO) issued an exposure draft of proposed changes to *Government Auditing Standards*." To properly reflect the developments that have occurred since the issuance of this ED, we suggest that this sentence be revised to read, "In June 1994, the General Accounting Office (GAO) revised its *Government Auditing Standards*, effective for financial audits of periods ending on or after January 1, 1995, and this statement incorporates those applicable revisions."

In addition, references to the *Government Auditing Standards* are limited to the chapters relating to financial audits, although *Government Auditing Standards* also provides guidance on performance/program audits. Paragraph 10 of the ED refers to a program audit, but it does not define the term. The term has a separate definition from that in the *Government Auditing Standards*, and it should be clearly defined in the context of federal audit requirements.

GENERALLY ACCEPTED AUDITING STANDARDS

- * Paragraph 6 - The recently issued Audit and Accounting Guide *Audits of State and Local Governmental Units* dated July 1, 1994, should be referenced.

Page Three
July 28, 1994

GOVERNMENT AUDITING STANDARDS

- * Paragraph 8 - We suggest that these paragraphs summarize the auditor's compliance auditing responsibilities under *Government Auditing Standards* to be consistent with the paragraphs on the other three types of audits - audits under GAAS, federal audit requirements, and state and local laws and regulations. Those responsibilities are stated in paragraphs 4.12-4.13 on pages 35-36 of the 1994 revision to the *Government Auditing Standards*.

FEDERAL AUDIT REQUIREMENTS

- * Paragraph 9(b) - For consistency with Section AU 319.26 of the *Codification of Statements on Auditing Standards*, we suggest that the first sentence be revised slightly to read, "The auditor's consideration of the internal control structure is to include obtaining and documenting an understanding of the accounting and administrative controls . . ." In addition, this paragraph uses the terminology "accounting and administrative controls." Other literature, i.e., SAS 55 and SOP 92-7, no longer uses those terms.
- * Paragraph 11 - We believe this paragraph could be omitted since the auditor's responsibility to determine and report on compliance is apparent from paragraph 9(d) and the last sentence of paragraph 10.

STATE AND LOCAL LAWS AND REGULATIONS

- * Paragraph 13 - The paragraph lists several procedures the auditor should consider performing to assist in assessing management's identification of laws and regulations. First, paragraph 13(e) states, "Review minutes of meetings of the legislative body of the governmental entity . . ." In addition to a legislative body that enacts laws and ordinances (e.g., city council, county commission, state legislature), many governmental entities also have a governing board that establishes rules and regulations (e.g., administrative board, board of trustees). Therefore, to provide more comprehensive guidance to the auditor, we suggest that paragraph 13(e) be expanded to read, "Review minutes of meetings of the legislative body and/or the governing board of the governmental entity . . ." Second, paragraph 13(g) states, "Review information about compliance requirements . . ." It lists three federal documents as examples. Because state governments may also establish compliance requirements, we suggest that paragraph 13(g) be expanded to include ". . . and State policies and procedures."

COMPLIANCE REQUIREMENTS APPLICABLE TO FEDERAL FINANCIAL ASSISTANCE PROGRAMS

- * Paragraphs 14 and 18 - These paragraphs continue to refer to general requirements, noting that the term "common requirements" also may apply. The partial draft of proposed revisions to the Office of Management and Budget's (OMB's) *Compliance Supplement for Single Audits of State and Local Governments*, circulated for comment earlier this year, replaces "general" with "common." In addition, the paragraphs seem unnecessarily repetitious. For example, the Compliance Supplements as a source of compliance requirements are repeated in paragraphs 14-16, grant agreements or contracts as a source of requirements in paragraphs 16-17, and the Compliance Supplements as a source of suggested audit procedures for compliance requirements in paragraphs 14 and 17.

Page Four
July 28, 1994

The second sentence in paragraph 14 does not include three words, "all or most," before "federal financial assistance" that are needed to clearly distinguish between the general and specific requirements. Also, those words currently appear in both OMB Compliance Supplement discussions of the general requirements.

Listing the categories of specific requirements in paragraph 15, but not the general requirements in paragraph 14, is inconsistent (unless the general requirements were intentionally not listed because they are currently under revision by the OMB).

- * Paragraph 16 - It could be incorrectly interpreted that specific requirements for all federal programs are to be obtained from both the OMB's Compliance Supplement and the grant agreement or contract, and that the OMB's Compliance Supplement may be relied upon without review of laws and regulations such as the U.S. Code and the Code of Federal Regulations (Federal Codes). Accordingly, paragraph 16 should be revised as follows, "The auditors should review the applicable Federal Codes for any changes in laws and regulations which might have an impact on the requirements enumerated in the OMB's Compliance Supplements. Specific compliance requirements not included in the OMB's Compliance Supplements may also be enumerated in the applicable Federal Codes, applicable federal acts, and the grant agreement or contract."

Accordingly, we suggest the following paragraphs as possible revisions:

Compliance requirements applicable to federal financial assistance programs are usually of two types: general and specific. General requirements involve national policy and apply to all or most federal financial assistance programs. Specific requirements apply to a particular federal program and generally arise from statutory requirements and regulations. The OMB's Compliance Supplements set forth general and specific requirements for the federal programs awarded to state and local governments and to nonprofit organizations and suggested audit procedures to test for compliance with the requirements.

For program-specific audits, the auditor should consult federal grantor agency audit guides (e.g., the SFA Audit Guide) to identify common requirements that are statutory and regulatory requirements pertaining to certain federal programs, specific requirements for a particular program, and suggested audit procedures to test for compliance with the requirements.

In addition to those identified in the OMB's Compliance Supplements or federal grantor agency audit guides, specific requirements may also be enumerated in grant agreements or contracts.

- * Footnote 11 states, "Detailed testing and reporting guidance on single or organization-wide audits and program audits is provided in the AICPA Audit and Accounting Guide *Audits of State and Local Governmental Units* and in AICPA SOPs 92-7 and 92-9." Because the AICPA has incorporated SOP 92-7 in the new Guide (as Chapters 5, 20-24 and Appendix A), the footnote is misleading. We suggest revision to the footnote as follows: "Detailed testing and reporting guidance on single or organization-wide audits and program audits is provided in the AICPA Audit and Accounting Guide *Audits of State and Local Governmental Units* and in AICPA SOP 92-9."

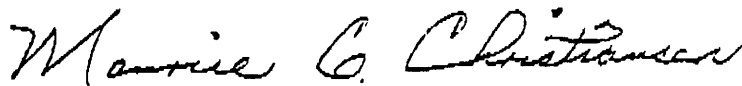
Page Five
July 28, 1994

**EVALUATING RESULTS OF COMPLIANCE AUDIT PROCEDURES ON MAJOR
FEDERAL FINANCIAL ASSISTANCE PROGRAMS**

- * Paragraphs 19 through 22 - We suggest that the word "major" be eliminated in the section title. Also, "major programs" should be added as a subtitle above paragraph 19, and "nonmajor programs" should be added as a subtitle above paragraph 22. This will clarify the information included in these sections.

Your consideration of our concerns is appreciated. If you have any questions about our comments, please contact Arthur Hayes, Chairman, NSAA Audit Standards and Reporting Committee, at (615) 741-2985.

Sincerely,



Maurice C. Christiansen, CPA
President

EXPOSURE DRAFT

FILE 2357

PROPOSED STATEMENT ON AUDITING STANDARDS

**COMPLIANCE AUDITING CONSIDERATIONS IN AUDITS OF
GOVERNMENTAL ENTITIES AND OTHER RECIPIENTS OF
GOVERNMENTAL FINANCIAL ASSISTANCE**

May 12, 1994

Comment Date: July 29, 1994

Name and Affiliation: MACPA

Comments:

Paragraph #1 - We feel that the word "generic" should be inserted on Line 3 after "provides". The sentence would be "This statement provides generic guidance for the auditors....". We feel this additional word helps set the tone for the standard - as explained in the Summary - Why Issued.

Footnote #3 - We feel the last sentence should be deleted because the new Government Auditing Standards have been issued.

Paragraph #2 - We feel the last sentence should have the change as follows: "Such laws and regulations may deal with the fund structures required by law, regulation"

This will then use the same terminology as the second paragraph.

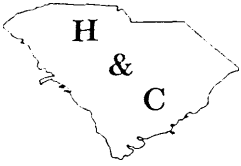
Paragraph #7 - We feel the first sentence, second line, should be changed to read "and for audits of government financial assistance received by"

This will use the same terminology as the title of the document. Confusing as currently stated with the use of the word "funds", or define "funds" as in Footnote #6.

Paragraph #7 - We feel the last sentence should be changed as follows: "These standards which include detecting material misstatement arising from violations of contracts and grant agreements are to be followed when"

This wording will be consistent with the new Government Auditing Standards.

Paragraph #9 - We feel consideration should be given to noting the emphasis of materiality measurement has been shifted from the financial statement to each major federal financial assistance program.



Hobbs and Corley, P.A.
Certified Public Accountants
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Mark T. Hobbs, CPA
Wayne D. Corley, CPA

Members
Private Companies Practice Section
of the American Institute of
Certified Public Accountants
South Carolina Association of
Certified Public Accountants

July 21, 1994

A. Louise Williamson, Technical Manager
Auditing Standards Division, File 2357
AICPA
1211 Avenue of the Americas
New York, New York 10036-8775

Gentlemen:

The Technical Standards Committee of the South Carolina Association of Certified Public Accountants has reviewed the Exposure Draft entitled "Compliance Auditing Considerations in Audits of Governmental Entities and Other Recipients of Governmental Financial Assistance". We offer the following comments for your consideration:

1. Generally, we concur with the approach in the Exposure Draft as it relates to the reduction of the level of detail in the auditing standards. However, since the SAS would be more authoritative than audit and accounting guides or statements of position, all areas of compliance auditing should be addressed or referenced to another source.
2. The study and evaluation of internal controls is a significant part of compliance auditing. The Exposure Draft should consider expanding the discussion concerning requirements of studying and understanding internal controls over compliance. The expanded guidance could supplement the discussion in paragraphs 9b and 9c.
3. SAS 68 addressed management representation letters regarding compliance with laws and regulations in detail. The Exposure Draft briefly addresses management representation letters in paragraph 13(c), but does not address the additional representation that would be made regarding compliance with laws and regulations. The Exposure Draft should address management representation in more detail or contain a footnote referencing these requirements.

Thank you for the opportunity to comment.

Very truly yours,

Mark T. Hobbs
Chairman, Technical Standards Committee
South Carolina Association of
Certified Public Accountants

CC: John Wentzell, SCACPA President
Lollie Coward, SCACPA Executive Director
Debra Turner, CPA

**The University
of Alabama
System**



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MEMORANDUM

TO: A. Louise Williamson, Technical Manager
AICPA Auditing Standards Division

FROM: Sylvia L. Ayers, CPA *S. Ayers*
Director of Internal Auditing, UAH

SUBJECT: Response to Exposure Draft of Proposed SAS
"Compliance Auditing Considerations in Audits of Governmental Entities and
Other Recipients of Governmental Financial Assistance"

FILE 2357

DATE: July 25, 1994

I concur with the "housekeeping" task of eliminating specific compliance, fieldwork, and reporting requirements and providing generic guidance for auditors engaged to perform compliance audits of governmental entities and other recipients of governmental financial assistance.

These types of audit engagements occur in a somewhat dynamic environment. For instance, the Yellow Book summarizing Government Auditing Standards was revised recently. The Office of Management and Budget plans to revise OMB Circulars A-21, A-128 and A-133 sometime later this year. The deletion of specific requirements should reduce the number of revisions needed to reflect changes made by the various federal audit officials.

The effective date of transition appears reasonable since this revision is a housekeeping task instead of new audit requirements. Concur that the related audit and accounting guides and SOPs will need revision to reflect this new SAS.

EXPOSURE DRAFT

FILE 2357

PROPOSED STATEMENT ON AUDITING STANDARDS

COMPLIANCE AUDITING CONSIDERATIONS IN AUDITS OF GOVERNMENTAL ENTITIES AND OTHER RECIPIENTS OF GOVERNMENTAL FINANCIAL ASSISTANCE

May 12, 1994

Comment Date: July 29, 1994

Name and Affiliation: Mark Sleasman, CPA, Sub-Committee Chair of Oregon Society of CPA's Audit and Accounting Committee

We agree with the Exposure Draft to the extent that it reduces the level of detail included in the auditing Standards and places more reliance for detail guidance in the applicable AICPA Audit and Accounting Guides.

We suggest that transitional guidance, or a transitional rule, be issued for the guidance that the Exposure Draft drops that has not yet been adopted or nullified by the AICPA Audit and Accounting Guides. The guidance in SAS No. 68 that is not in the new Exposure Draft (new SAS) should be applicable until the time the guidance is superceded by the AICPA Audit and Accounting Guides.

Thank you for the opportunity to respond to this Exposure Draft.

Mark Sleasman
Sub-Committee Chair
OSCPA Audit + Accounting Committee

Instructions for Response Form

This form may be used for comments or suggestions relating to any aspect of the exposure draft that is of concern or interest to you. Return this response form to the address indicated on the reverse side by the comment date.



STATE OF MICHIGAN
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201 N. WASHINGTON SQUARE
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(517) 334-8050
FAX (517) 334-8079

28

THOMAS H. MCTAVISH, C.P.A.
AUDITOR GENERAL

July 25, 1994

Ms. A. Louise Williamson
Technical Manager, Auditing Standards Division
American Institute of Certified Public Accountants
1211 Avenue of the Americas
New York, New York 10036-8775

Dear Ms. Williamson:

We have reviewed the Exposure Draft (ED) of the proposed Statement on Auditing Standards (File 2357), entitled Compliance Auditing Considerations in Audits of Governmental Entities and Other Recipients of Governmental Financial Assistance, and submit the following comments for consideration by the Auditing Standards Board. We have presented our comments in paragraph and/or page sequence to simplify your review process.

1. Footnote 1, on Page 9, refers the auditor to Statement on Standards for Attestation Engagements No. 3 for guidance on engagements related to management's written assertions. However, the ED does not also refer the auditor to the guidance on auditing for compliance with aspects of contractual agreements or regulatory requirements related to financial statements, contained in Statement on Auditing Standards (SAS) No. 62, entitled Special Reports. It appears that the Board intends that all compliance auditing, beyond the scope covered in this ED, be subject to the AICPA's attestation standards. We object to this apparent initiative for several reasons, including the fact that most users expect a compliance report in relation to the financial statements or major federal programs, and that the attestation standards lack materiality criteria that users can understand. Therefore, we suggest that the Board expand Footnote 1 to also refer the auditor to SAS No. 62 for guidance on compliance reports.
2. The last sentence of Footnote 3, on Page 9, states that "In July 1993, the General Accounting Office (GAO) issued an exposure draft of proposed changes to *Government Auditing Standards*." To properly reflect the developments that have occurred since the issuance of this ED, we suggest that this sentence be revised to read "In June 1994, the General Accounting Office (GAO) revised its *Government Auditing Standards*, effective for financial audits of periods ending on or after January 1, 1995, and this Statement incorporates those applicable revisions."

3. For consistency with Section AU 319.26 of the Codification of Statements on Auditing Standards (Codification), we suggest that the first sentence of Paragraph 9.b. be revised slightly to read "The auditor's consideration of the internal control structure is to include obtaining and documenting an understanding of the accounting and administrative controls...."
4. Paragraph 13 lists several procedures that the auditor should consider performing to assist in assessing management's identification of laws and regulations. We have two comments on these procedures. First, Paragraph 13.e. states "Review minutes of meetings of the legislative body of the governmental entity..." In addition to a legislative body that enacts laws and ordinances (e.g., city council, county commission, state legislature), many governmental entities also have a governing board that establishes rules and regulations (e.g., administrative board, board of trustees). Therefore, to provide more comprehensive guidance to the auditor, we suggest that Paragraph 13.e. be expanded to read "Review minutes of meetings of the legislative body and/or the governing board of the governmental entity..." Second, Paragraph 13.g. states "Review information about compliance requirements,..." and lists three federal documents as examples. Because state governments may also establish compliance requirements, we suggest that Paragraph 13.g. be expanded to include "...and State policies and procedures."
5. Paragraph 16 states "In addition to those enumerated in the OMB's Compliance Supplements, specific compliance requirements may also be enumerated in the grant agreement or contract." This sentence implies that the auditor should review grant agreements and contracts for compliance requirements in all programs. Based on our interpretation of the guidance in both the Compliance Supplement and federal Circular A-128, we believe that the auditor should review the grant agreements and contracts for compliance requirements only for those specific programs not listed in the Compliance Supplement. Also, for those programs not listed in the Supplement, the auditor should consult the Code of Federal Regulations and applicable federal acts. Therefore, we suggest that Paragraph 16 be revised to read "For those federal programs not included in the OMB's Compliance Supplement, specific compliance requirements may be included in the grant agreement or contract. The auditor should also consult the Code of Federal Regulations and applicable federal acts."
6. Footnote 11, on Page 14, states "Detailed testing and reporting guidance on single or organization-wide audits and program audits is provided in the AICPA Audit and Accounting Guide *Audits of State and Local Governmental Units* and in

Ms. A. Louise Williamson
Page 3
July 25, 1994

AICPA SOP's 92-7 and 92-9." We have two comments on this footnote. First, we believe the information in the footnote is far too important to the reader to locate it near the end of the ED. Second, because the AICPA has incorporated SOP 92-7 in the new Guide (as Chapters 5, 20-24, and Appendix A), the footnote is misleading. For these reasons, we suggest that Footnote 11 be relocated within Paragraph 1 (Introduction and Applicability) of the final document and revised to read "Detailed testing and reporting guidance on single or organization-wide audits and program audits is provided in the AICPA Audit and Accounting Guide *Audits of State and Local Governmental Units* and in AICPA SOP 92-9. Therefore, this guidance is not included in this Statement."

Also, the 1994 revision of *Government Auditing Standards* eliminated the previous requirement for the auditor to provide statements of positive and negative assurance on compliance items tested. Although we understand that the new Guide will be revised in early 1995 to reflect the 1994 revisions to professional standards, we believe that the elimination of this particular reporting requirement is far too important to defer mentioning in the literature until 1995. Therefore, we suggest that the Board alert the auditor to the elimination of the previously required statements of positive and negative assurance, either in Paragraph 1 or in a footnote to the Statement.

7. Section AU 801.19 of the Codification states that, in accordance with generally accepted auditing standards, the auditor is required to obtain written representations from management regarding its compliance with laws and regulations. This paragraph was not retained in the ED. We realize that this guidance will be incorporated in Chapter 5 of the new Guide; however, we believe the importance of written representations also warrants inclusion of this paragraph in the Statement. Therefore, we suggest that Section AU 801.19, as revised in the new Guide, be included verbatim in this Statement.

We appreciate the opportunity to comment on the Exposure Draft. Should you have any questions, or desire further details on our comments, please contact me or Jon A. Wise, C.P.A., Director of Professional Practice.

Sincerely,



Thomas H. McTavish, C.P.A.
Auditor General

OFFICE OF THE STATE AUDITOR

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LAWRENCE F. ALWIN, CPA
State Auditor

SHARON W. COBB, CPA
First Assistant

July 27, 1994

A. Louise Williamson, Technical Manager
Auditing Standards Division, File 2357
American Institute of Certified Public Accountants
1211 Avenue of the Americas
New York, NY 10036-8775

Dear Ms. Williamson:

Thank you for allowing us to comment on the AICPA's Proposed Statement on Auditing Standards, *Compliance Auditing Considerations in Audits of Governmental Entities and Other Recipients of Governmental Financial Assistance*.

We agree with the proposed statement's generic guidance for compliance audits of recipients of governmental financial assistance and plans to include specific performance and reporting guidance in the applicable audit and accounting guides and statements of position. We believe this is an improved approach and agree with the content and guidance in the proposal.

Two other minor comments we have are:

- Footnote 3 should now refer to the 1994 revision of *Government Auditing Standards*, since it has been issued by the General Accounting Office.
- Paragraph 8 should clarify that the general standards of *Government Auditing Standards* relating to staff qualifications vary from those of GAAS, although similar topics are covered in both sets of standards.

Again, thank you for the opportunity to comment on the proposed statement.

Sincerely,

Dennis O. Teinert

Dennis O. Teinert, CPA
Federal Coordinator Assistant

DOT/rmn



30

COMMONWEALTH OF PENNSYLVANIA
GOVERNOR'S OFFICE
HARRISBURG

HARVEY C. ECKERT
DEPUTY SECRETARY FOR COMPTROLLER OPERATIONS
OFFICE OF THE BUDGET

July 28, 1994

Ms. A. Louise Williamson
Technical Manager
Auditing Standards Division, File 2357
American Institute of Certified Public
Accountants
1211 Avenue of the Americas
New York, NY 10036-8775

Dear Ms. Williamson:

We have reviewed the Exposure Draft (ED) on the Proposed Statement on Auditing Standards entitled "Compliance Auditing Considerations in Audits of Government Entities and Other Recipients of Governmental Financial Assistance." We provide the following comments for your consideration:

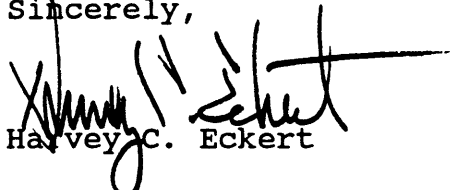
1. The reporting examples in SAS 68 have been removed in the ED. Footnote 4 references SOPs 92-7 and 92-9 for guidance on audit testing and reporting for single and organization-wide audits. As written in the ED, we believe that reference only covers single or organization-wide audits. We believe that item 1.b. should also reference Footnote 4 and that Footnote 4 include other audits done in accordance with Government Auditing Standards (GAS) since such guidance is provided in the SOPs.

Also, the SOPs need to be updated for guidance on compliance reporting based on an audit of the financial statements conducted in accordance with GAS as a result of the 1994 revision to GAS.

2. In addition to the recent changes to GAS, there is much discussion on proposed revisions to the Single Audit Act and OMB Circulars A-128 and A-133. We believe this proposed statement should not be issued until such revisions are completed and can be incorporated into the proposed statement.

Thank you for the opportunity to comment. If you have any questions, please contact me at 717-787-6496.

Sincerely,



Harvey C. Eckert

cc: J. Terry Kostoff

July 29, 1994

Ms. A. Louise Williamson
Technical Manager
Auditing Standards Division, File 2357
American Institute of Certified Public Accountants
1211 Avenue of the Americas
New York, NY 10036-8775

Dear Ms. Williamson:

We support the issuance of the proposed Statement on Auditing Standards, "Compliance Auditing Considerations in Audits of Governmental Entities and Other Recipients of Governmental Financial Assistance" as a replacement for SAS No. 68. In particular, we agree with the concept of shifting the detailed guidance on compliance with the various governmental rules and regulations to audit and accounting guides.

We have the following comments on the proposal:

Paragraph 11 - This paragraph essentially repeats paragraph 9(d), and could be eliminated.

Paragraph 13 - This paragraph is structured somewhat differently than SAS No. 54 in that there is an expectation, in these circumstances, that management will identify the laws and regulations that have a direct and material effect; we agree with this structure. Therefore, we believe that the concept of "laws and regulations that are generally recognized by auditors..." is not necessary. We suggest that the first two sentences of this paragraph be combined to read as follows:

The auditor should assess whether management has identified laws and regulations that have a direct and material effect on the determination of amounts in the entity's financial statements, and obtain an understanding of the possible effects on the financial statements of these laws and regulations.

Paragraphs 14 and 17 - In both of these paragraphs there are references to the suggested audit procedures contained in the Compliance Supplements and, in paragraph 17, to the federal grantor agency audit guides. In November 1987, OMB issued a series of Questions and Answers that essentially provided a "safe harbor" for the auditor who applies the suggested audit procedures contained in Compliance Supplement A-128. (See Question 10 in Appendix D of the new Audit and Accounting Guide, Audits of State and Local Governmental Units.) In practice, this "safe harbor" has been applied to Compliance Supplement A-133 as well. A footnote making this point would be helpful to practitioners.

Ms. A. Louise Williamson

Page 2 of 2

July 29, 1994

Paragraph 16 - It is highly unlikely that specific requirements would be addressed in both a Compliance Supplement and in the specific grant agreement or contract. Generally, specific requirements are only addressed in the grant agreement or contract when the Compliance Supplement does not address the program. Therefore, we suggest that this paragraph be revised as follows:

For those programs not covered in the OMB's Compliance Supplements, specific compliance requirements may be enumerated in the grant agreement or contract.

We appreciate the opportunity to express our views. If you have any questions regarding our comments, please contact A.J. Lorie at 212-536-2119.

Very truly yours,

Coopers + Lybrand

**Colorado Society of
Certified Public Accountants**

July 25, 1994

Ms. A. Louise Williamson, Technical Manager
Auditing Standards Division
File 2357
AICPA
1211 Avenue of the Americas
New York, New York 10036-88775

Re: Exposure Draft - Proposed Statement
on Auditing Standards - Compliance
Auditing Considerations in Audits of
Governmental Entities and Other
Recipients of Governmental Financial
Assistance

The following are the Colorado Society of CPA's Governmental Issues Committee comments with regard to the above document:

1. It appears that changes will be made to A-128, A-133 and the *Compliance Supplement* which may effect paragraphs 14 through 22 (see June 1994 *Journal of Accountancy* Article "*Change the Single Audit Requirements*"). Therefore, consideration should be given to delaying this document.
2. Paragraph 1 - We recommend the Board clarify the term governmental financial assistance. We presume this applies to both federal and nonfederal financial assistance. Does the Board still intend for the auditor to examine nonfederal financial assistance for material noncompliance that may give rise to a contingent liability? If so, we recommend the term be defined in the footnotes in the same manner as "subrecipient" on page 10.
3. Throughout the document, wherever laws and regulations are referred to, we recommend using "are subject to the laws and regulations as referred to in the grant agreement or *Compliance Supplement*". Two specific examples are referred to in numbers 4 and 5 below.
4. Paragraph 11 - We recommend adding to the last sentence in the paragraph to read, "complied with applicable federal laws or regulations as defined in the compliance supplement and/or grant agreement (referred to as "compliance requirements")."



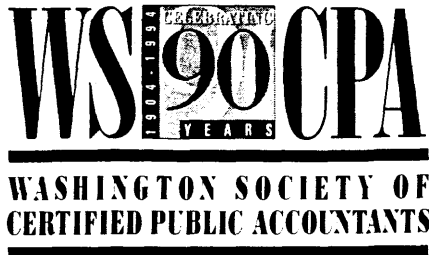
Page Two
Ms. A. Louise Williamson
July 25, 1994

5. Paragraph 17 - We recommend to remove everything after the first sentence and replace with the following, Testing should consist of procedures defined in the compliance supplement and/or grant agreement or procedures as defined by and agreed to by the client; grantor or pass through agency and the auditor.
6. Paragraph 21 - In the first sentence, we recommend to change "report any instances of noncompliance found and any resulting questioned costs" to read, "Regardless of the auditor's opinion on compliance, federal audit regulations may require him or her to report any material instances of noncompliance found and any material questioned costs as reflected in the new Yellow Book and the Single Audit Act of 1984. In reporting instances of noncompliance,..." The AICPA should encourage the OMB to conform to A-133 standards when reporting findings and questioned costs.

Very truly yours,



Colorado Society of CPA's
Governmental Issue Committee



July 27, 1994

A. Louise Williamson
AICPA
Technical Manager
Auditing Standards Division - File 2357
1211 Avenue of the Americas
New York, New York 10036-8775

The Government Accounting and Auditing Committee of the Washington Society of Certified Public Accountants appreciates the opportunity to respond to the AICPA Exposure Draft: *Compliance Auditing Considerations in Audits of Governmental Entities and other Recipients of Governmental Financial Assistance.*

The committee supports the proposed statement on auditing standards. Specifically, we appreciate the reduction in level by detail included in the auditing standards. We agree that other authoritative literature, such as Audit Guides and Statements of Position, serves as a source of detailed audit procedures; this statement as written, appropriately serves as a framework with which to apply the other guidance.

Thank you for the opportunity to comment.

Very truly yours,

Michael L. Cheney
Chairman
Government Accounting and Auditing Committee

MLC:em

July 29, 1994

Ms. A. Louise Williamson, Technical Manager
Auditing Standards Division, File 2357
American Institute of CPAs
1211 Avenue of the Americas
New York, New York 10036-8775

Arthur Andersen & Co.

Suite 2700
500 Woodward Avenue
Detroit MI 48226-3424
313 596 9000

Dear Louise:

This letter is in response to the exposure draft of a proposed Statement on Auditing Standards entitled Compliance Auditing Considerations in Audits of Governmental Entities and Other Recipients of Governmental Financial Assistance.

I support the proposed standard, and offer the following comments for your consideration:

- Paragraph 1 refers to program audits, and footnote 2 to that paragraph cites two examples of specific federal audit guides which utilize program audits. However, SSAE No. 3 (according to paragraph 2d) applies to all program-specific audits, pursuant to federal audit guides issued after June 15, 1994. The interaction between this footnote and paragraph 2d of SSAE No. 3 should be reviewed and resolved by the Board.
- The last sentence of footnote 3 should be deleted.
- Although I recognize that the last sentence of paragraph 6 simply repeats what is currently in footnote 4 of SAS No. 68, I recommend that this sentence be deleted or reworded. If the thought is necessary (and I'm not sure that it is), it should be so stated, and not by incorporating a quotation from an audit guide.
- Paragraph 8 includes a parenthetical reference to continuing education requirements, but I fail to see why this particular requirement is singled out, and suggest it be deleted.
- Paragraph 12 incorporates the existing guidance in paragraphs 98 - 99 of SAS No. 68. Doesn't SSAE No. 3 replace the guidance in these two paragraphs? (Note that the paragraphs were not exempted in paragraph 2 of SSAE No. 3.) Since all such compliance engagements must now presumably be performed as SSAE No. 3 engagements, I don't understand the need for, nor the applicability of, this paragraph.

ARTHUR
ANDERSEN

ARTHUR ANDERSEN & CO. SC

Ms. A. Louise Williamson, Technical Manager

Page 2

July 29, 1994

- In paragraph 14 and footnote 9, the term "common requirements" is relegated to a footnote, and the term "general requirements" is used in the standard. For consistency, the term "general requirements" should also be used in paragraphs 17 and 18.
- In paragraph 23, the term "may consider including" seems too weak. At a minimum, this should be "should consider including."
- In paragraph 24, the second sentence should probably begin with the word, "However."

Very truly yours,



Timothy E. Durbin



COMMONWEALTH of VIRGINIA
Auditor of Public Accounts

WALTER J. KUCHARSKI
AUDITOR

POST OFFICE BOX 1295
RICHMOND, VIRGINIA 23210
(804) 225-3350

July 29, 1994

American Institute of Certified Public Accountants
A. Louise Williamson, Technical Manager
Auditing Standards Division, File 2357
1211 Avenue of the Americas
New York, NY 10036-8775

Dear Ms. Williamson:

Thank you for the opportunity to comment on the Exposure Draft (ED) of the Statement on Auditing Standards, *Compliance Auditing Considerations in Audits of Governmental Entities and Other Recipients of Governmental Financial Assistance*. Overall, we endorse the Board's approach of reducing the level of detail in this standard, and instead having the detail in the applicable accounting and auditing guides and statements of position.

Our main concern about this ED is, as drafted, the document fails to incorporate several imminent changes in the body of guidance on which it is based. Specifically, the ED refers to the *1988 Government Auditing Standards*, although the Federal government has already issued the 1994 revision of GAS. As you are probably aware, OMB is revising Circular A-133 to incorporate many of the recommendations made in several studies of the Single Audit process. It is our understanding that OMB contemplates the revisions to Circular A-133 will apply to audits currently conducted under Circular A-128 as well. Also, OMB is revising the Compliance Supplement, including an overhaul of the Common (general) Requirements. Therefore, we encourage the Board to consider whether the immediate need for this standard outweighs the risk that its contents may very quickly become out-dated as the federal government changes these requirements.

Should the Board opt to issue its final statement before the conclusion of these projects, we offer the following comments on specific sections of the ED.

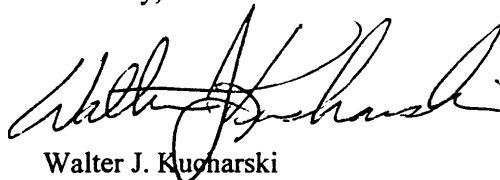
- 1) Footnote 3 should refer to the *1994 Government Auditing Standards* rather than the 1988 GAS and the July, 1993 exposure draft.
- 2) We recommend eliminating the references to AICPA SOPs 92-7 and 92-9 throughout the proposed standard as SOPs are subject to more frequent change. Instead, the Board references should be made to the applicable accounting and auditing guides and *related* SOPs.

A. Louise Williamson, Technical Manager
July 29, 1994
Page 2

- 3) Paragraphs 16 should clarify that while the OMB Compliance Supplements contain descriptions and suggested audit procedures for the specific requirements of many federal programs to state and local governments and non-profit organizations, the auditor has responsibility for changes in requirements that have occurred since the last revision to the Supplements as well as specific requirements of programs not in the Supplements. These requirements may be enumerated in the grant agreement or contract or in applicable regulations relating to the administration of the program.
- 4) Paragraph 20 should include a discussion of the distinction between known and likely questioned costs and their effect on the auditor's opinion on the financial statements, opinion or report on compliance and the schedule of findings and questioned costs required by the Single Audit Act.
- 5) As discussed in our opening comments, considering the changes contemplated by OMB and recommended by the several studies of the Single Audit process, we believe paragraph 22 should not contain detail guidance related to testing of nonmajor program transactions or refer to the guidance in the applicable OMB circulars. Guidance in other areas covered in the ED are referenced to their sources rather than restated. This change would reduce the need for an immediate revision of the standard when the changes being proposed by OMB are adopted. Also, delete the word "Major" from the current section title since it discusses both major and nonmajor programs are discussed.

Your consideration of these concerns is appreciated. Should you have questions regarding these comments please contact Cynthia J. Hartley, Director, Systems and Quality Control, at (804) 225-3350.

Sincerely,



Walter J. Kuonarski
Auditor of Public Accounts

WJK/CJH:jj

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July 28, 1994



A. Louise Williamson
Technical Manager
Auditing Standards Division
File 2357
AICPA
1211 Avenue of the Americas
New York, NY 10036-8775

RE: Proposed Statement on Auditing Standards - Compliance Auditing Applicable to Government Entities and other Recipients of Governmental Financial Assistance (Superceeds SAS No. 68)

Dear Ms. Williamson:

We are enclosing the comments of the New York State Society of Certified Public Accountants in response to the above Proposed Statement on Auditing Standards. These comments were prepared by the Society's Auditing Standards and Procedures Committee.

If you have any questions regarding the comments, please call us and we will arrange for someone from the committee to contact you.

Thank you for your consideration.

Very truly yours,

John J. O'Leary
John J. O'Leary

Chairman, Auditing Standards and
Procedures Committee

Walter M. Primoff
Walter M. Primoff, CPA

Director, Professional Programs

JJO/WMP:dr
Enclosure

cc: Accounting & Auditing Committee Chairmen

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nysscpa

The Auditing Standards and Procedures Committee of the New York State Society of CPAs is pleased to offer the following comments on the Proposed Statement on Auditing Standards.

The Committee agrees with the Board's decision to issue the proposed statement, and considers it a significant addition to existing guidance in this area of practice. While the Committee agrees, in general, with the proposed statement, some members believe that additional clarification or guidance is needed in the following areas.

Reduced Level of Guidance in Statements on Auditing Standards

The Committee in general is concerned with the planned reduction in the level of detail guidance to be included in the proposed statement. While the Committee agrees with the proposal to issue an audit and accounting guide to provide specific performance and reporting guidance, it is concerned that such guidance is being intentionally transferred from a primary source of guidance to auditors to one that is secondary. The Committee is also concerned that delays in issuing the audit and accounting guide would be a disservice to practitioners who audit governmental entities and other recipients of governmental financial assistance. The Committee, therefore, requests that the Board reconsider its decision to reduce the level of guidance in the proposed statement. Alternatively, the Committee suggests that the Board consider adding appendixes to the proposed statement to illustrate the applications of the proposed guidance.

Small Entities Consideration

Paragraph 4 of the proposed statement indicates management is responsible for ensuring that entities receiving federal financial assistance for specific governmental programs comply with the laws and regulations applicable to the activities, and that responsibility encompasses identification of those applicable laws and regulations and establishment of internal control policies and procedures designed to provide the entity with reasonable assurance of compliance with all applicable laws and regulations. Paragraphs 14-16 identify two types of compliance requirements; general and specific. General requirements are those that involve national policies and are applicable to federal financial assistance programs set forth in the OMB's Compliance Supplements. Specific requirements are those applicable to a particular federal program set forth in the applicable federal grantor agency audit guide.

The Committee believes many small entities that are recipients of federal financial assistance do not maintain adequate internal control policies and procedures that would enable them to monitor compliance with general requirements. The Committee also believes auditors of these small entities who perform compliance tests, often expand their procedures because of the frequency of noncompliance with those requirements.

The Committee therefore suggests the proposed statement exempt small entities from compliance with general requirements. The Committee believes compliance with program-specific procedures stated in federal program audit guides would not significantly undermine the general requirements of the national programs. The Committee defines small entities as those equal to or less than a "subrecipient" as that term is used in note 5 to paragraph 3 of the proposed statement.

Undue Emphasis to SAS No. 54

The Committee believes the proposed statement makes too many references to SAS No. 54, "Illegal Acts by Clients," and such emphasis on SAS No. 54 seems to imply auditors frequently encounter such matters when auditing recipients of federal financial assistance. For example, paragraph 1 of the proposed statement states that the proposed statement provides guidance on the auditor's responsibility to "...apply the provisions of SAS No. 54, Illegal Acts by Clients (AICPA, Professional Standards, Vol. 1, AU sec. 317) relative to detecting misstatements resulting from illegal acts related to laws and regulations that apply to governmental financial assistance or that have a direct and material effect on the determination of financial statement amounts in audits of governmental and certain nongovernmental entities." Paragraph 5 states that "SAS No. 54 describes the auditor's responsibility, in an audit performed in accordance with GAAS, for considering laws and regulations and how they affect the audit." Finally, paragraph 25 of the proposed statement reminds the auditor of the requirement to advise a client if he or she becomes aware that the entity is subject to an audit requirement that may not be encompassed in the terms of the current engagement, and the auditor should consider management's actions in relation to the guidance in SAS No. 54.

The Committee believes that these references to SAS No. 54 may be placed in a single paragraph stating:

- a. The auditor's responsibility to test compliance with laws and regulations that pertain to the program activity being audited.
- b. The requirement to follow the guidance in SAS No. 54 if the auditor becomes aware of violations of laws and regulations that relate to the (general or specific) federal financial assistance program activity.

The Committee also believes the proposed statement should make reference to SAS No. 53, "The Auditor's Responsibility to Detect and Report Errors and Irregularities."

Government Auditing Standards

Footnote 3 on page 9 of the proposed statement indicates that in July 1993 the General Accounting Office (GAO) issued an exposure draft of proposed changes to Government Auditing Standards. The footnote should be changed to indicate that in June 1994, the General Accounting Office issued Government Auditing Standards, 1994 Revision.

Generally Accepted Auditing Standards

The last sentence of paragraph 6 on page 11 of the proposed statement quotes the AICPA Audit and Accounting Guide, "Audits of State and Local Governmental Units" as indicating that materiality evaluations should be applied at the fund type and account group level. While it is true materiality evaluations in governmental units are applied at the fund type and account group level, the Committee believes materiality evaluations in a not-for-profit organization are made on an entity-wide basis, rather than on a fund type and account group level basis. Accordingly, the Committee recommends the last sentence of paragraph 6 on page 11 be deleted.

September 13, 1994

File Ref. No. 1120

To the Auditing Standards Board:

Re: Exposure Draft on Compliance Auditing Considerations in Audits
of Governmental Entities and Other Recipients of Governmental
Financial AssistanceHere are additional comment letters received to date on the
exposure draft on Compliance Auditing Considerations in Audits of
Governmental Entities and Other Recipients of Governmental
Financial Assistance.**Name/Affiliation****Location**

42. KPMG Peat Marwick	New York, NY
43. Michael C. Moreland Governmental Accounting and Auditing Committee of the California Society of CPAs	Sacramento, CA
44. Ian A. Mackay American Institute of CPAs	Washington, DC
45. Mary M. Foelster American Institute of CPAs (for the Government Accounting and Auditing Committee)	Washington, DC
46. Robert O. Dale PCPS Technical Issues Committee	New York, NY

Sincerely,

A. Louise Williamson, CPA
Technical Manager
Auditing Standards Division

ALW/jw

cc: SAS 68 Revision Task Force

599 Lexington Avenue
New York, NY 10022

Telephone 212 909 5400

Telefax 212 909 5699

August 24, 1994

Ms. A. Louise Williamson, Technical Manager
Auditing Standards Division, File 2357
1211 Avenue of the Americas
New York, NY 10036-8775

**Re: Exposure Draft - Proposed Statement on Auditing Standards
Compliance Auditing Considerations in Audits of
Governmental Entities and Other Recipients of
Governmental Financial Assistance**

Dear Ms. Williamson:

We support the issuance of a final statement based on the Exposure Draft. However, the following comments on the Exposure Draft are enclosed for your consideration.

- As you know, the United States General Accounting Office issued a 1994 Revision to *Government Auditing Standards*, the "Yellow Book", after the Exposure Draft was issued. Accordingly, the ASB or its designee should consider what changes should be made to the Exposure Draft as a result of changes to the Yellow Book.
- The proposed SAS is not clear regarding whether auditors should report on compliance using the model set forth in existing SAS No. 68 or the attestation model set forth in Statement on Standards for Attestation Engagements (SSAE) No. 3, *Compliance Attestation*. We recommend that the Board clarify which method of reporting is appropriate.

SSAE No. 3, in paragraph 2.d. indicates that it does not apply to program-specific audits, as addressed in paragraph 96 of SAS No. 68, performed in accordance with federal audit guides issued prior to the effective date of SSAE No. 3. We assume that some type of conforming change will be made to SSAE No. 3; however, the Exposure Draft does not separately address federal audit guides as SAS No. 68 does. Furthermore, paragraph 2.d. of SSAE No. 3 has caused confusion in practice. Accordingly, consistent with our recommendation above, we suggest that the Board clarify which standard is appropriate with respect to this specific matter. We are willing to work with the Board's SAS No. 68 task force to develop the necessary clarification on these applicability issues.

- Paragraph 5.10 of the revised Yellow Book indicates that in certain situations, "some reasonable needs of report users . . . may be unmet." The paragraph further states that "auditors may meet these needs by performing further tests of internal controls and compliance with laws and regulations." We recommend that paragraph 4 of the Exposure Draft be expanded or footnoted to clarify that it is management's (or other users') responsibility to engage auditors to perform supplemental tests when considered necessary.



Ms. A. Louise Williamson
August 24, 1994

Page 2

- The illustrative internal control report in existing SAS No. 68 includes the following language: "In planning and performing our audit of the financial statements of XYZ Co. for the year ended June 30 19X1, we considered its internal control structure in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control structure." This statement is untrue when the auditor has also performed an examination of a management assertion regarding the internal control structure over financial reporting in addition to the financial statement audit. We recognize that the Exposure Draft does not contain an illustrative internal control report; however, we believe this is the appropriate time to address how the internal control report should be modified if an SSAE No. 2 examination has been performed. Any such guidance could be included in the appropriate audit and accounting guides.
- Paragraph 1, footnote 3 refers to Statements of Position 92-7 and 92-9. Since one of the objectives of this proposed standard is to eliminate the need for frequent revision, we suggest that these specific references be eliminated and replaced with a reference to applicable AICPA audit and accounting guides.
- Paragraph 6. The last sentence of this paragraph is a quotation from the AICPA Audit and Accounting Guide, *Audits of State and Local Governments*. Consistent with our comment on paragraph 1, and because this sentence does not appear to add substance to this paragraph, we recommend that the quotation be eliminated.
- Paragraph 18, footnote 11 refers to Statements of Position 92-7 and 92-9. See our related comment on paragraph 1, footnote 3.
- Based on discussions within our firm regarding pending Office of Management and Budget regulatory changes, it appears likely that the proposed SAS may need to be revised in the future to reflect such changes. One of the primary reasons for this proposed SAS is to eliminate the need for frequent revision and updating of this standard. Accordingly, we recommend that the ASB consider whether the proposed SAS should be made even more generic in contemplation of additional regulatory changes.

We appreciate the opportunity to comment on the Exposure Draft. If you have any questions regarding our comments, please contact E.R. Noonan at (212) 909-5448.

Very truly yours,

KPMG Peat Marwick LLP



California
Society
Certified
Public
Accountants

August 19, 1994

A. Louise Williamson
Technical Manager, Auditing Standards Division
American Institute of Certified Public Accountants
1211 Avenue of the Americas
New York, NY 10036-8775

The Governmental Accounting and Auditing Committee of the California Society of Certified Public Accountants appreciates the opportunity to present comments on the Exposure Draft relating to compliance auditing considerations in audits of governmental entities and other recipients of governmental financial assistance.

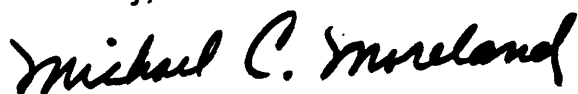
While the committee supports the requirements in the Exposure Draft on compliance auditing, we offer the following comments:

1. We believe that the Exposure Draft will provide a significant improvement over the approach to guidance embodied in Statement on Auditing Standards (SAS) No. 68. Reporting requirements have changed over the years and reporting guidance has frequently been inconsistent with each update. After the appropriate reporting guidance was developed in the related statements of position and audit and accounting guides, the guidance in SAS 68 became duplicative, adding confusion to the already complex reporting process for governmental assistance.
2. In revising the SAS to be very specific towards governmental assistance, information which was included in the previous SAS in paragraphs 12-14 has been omitted. We believe the Exposure Draft could be strengthened by retaining some reference to the basic audit requirements in SAS 53 and SAS 55 and including a statement that the requirements for governmental assistance go beyond these requirements. These references could be included in paragraph 5 of the Exposure Draft.

A. Louise Williamson
August 19, 1994
Page 2

We thank you again for allowing the Committee the opportunity to offer our comments on the Exposure Draft.

Sincerely,

A handwritten signature in black ink that reads "Michael C. Moreland". The signature is written in a cursive, slightly slanted style.

Michael C. Moreland, Chair
Governmental Accounting and Auditing Committee

MCM:MM/MH:hk

cc: S. Thomas Cleveland, President
Gale L. Case, First Vice President
Members, Governmental Accounting and Auditing Committee
James R. Kurtz, Executive Director
Bruce C. Allen, Director, Government Relations
Mike Flanigan, Director, Professional Regulation
Maxine Hosaka, Associate Director, Regulation

Date: August 10, 1994

Reply:

To: Louise Williamson

File No. J-1-402

From: Ian MacKay *IWM*

Subject: **Exposure Draft - Proposed Revised SAS No. 68**

Here are my comments on the exposure draft:

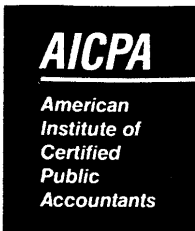
- Need for future revisions - One of the stated intents of the proposed revisions is that the proposed statement would not require frequent revision and updating. The ASB should be aware that the OMB is currently revising OMB Circular A-133 (expected to be exposed for comment in August 1994) and eventually plans to combine OMB Circular A-128 into Circular A-133 once changes to the Single Audit Act are made to make the Act apply to not-for-profit entities as well. Also, the OMB staff has indicated that it would like to move towards an attestation standards approach for compliance auditing under A-128 and A-133. We may want to get input from the OMB on how and when its proposed revisions could affect the revised SAS 68 to avoid the need for future revisions in the near term.
- Emphasis on governmental entities? - The reference to "audits of *governmental entities* and *other* recipients..." in the title and throughout the ED seems to overemphasize the application of the statement to governmental entities receiving governmental financial assistance as compared to not-for-profits and other entities. If my information is correct, there are more A-133 audits than A-128 audits. Also, there are many for-profit entities that would be covered under the standard (HUD and SFA audits). Perhaps the title should read something like "Compliance Auditing Considerations in Audits of Entities Receiving Governmental Financial Assistance," and similar changes be made throughout the ED.
- Form of reporting - The summary to the ED states that the proposed statement would not specify the form of reporting and that specific reporting guidance would be more appropriately included in the applicable audit and accounting guides and statements of position. I agree that the standard should not illustrate compliance reports that would need regular revision. However, where does guidance exist on the form of compliance reporting for for-profit entities not covered by audit guides and SOPs (other than in federal program

guides)? My experience has been that auditors of for-profit entities generally do not understand A-128 and A-133 compliance reporting. The ASB may wish to consider developing a reporting "model" to be used that would identify basic elements to be included in compliance reports. This would help practitioners who audit federal and state financial assistance programs where no guide exists. It would also promote consistency in compliance reporting.

- Paragraph 1b - This paragraph notes that the proposed standard provides guidance on the auditor's responsibility to perform an *audit* in accordance with Government Auditing Standards. Because the new (1994) Yellow Book also incorporates other AICPA standards that address specific types of financial-related audits (including SAS Nos. 35, 62, 68, 70, and SSAE Nos. 1, 2, and 3), perhaps this paragraph should clarify that this standard applies to "financial statement audits" and for certain financial-related audits other applicable AICPA standards may apply. Also, the reference in footnote 3 to paragraph 1b to SOP 92-7 should be deleted because SOP 92-7 will be superseded by the revised state and local government audit guide, and the reference to the July 1993 GAO exposure draft should be deleted.
- Paragraph 13 - This paragraph should get to the point (and purpose of the standard) to say that recipients of governmental financial assistance may have additional considerations under SAS 54 relative to financial statement audits because such laws and regulations governing financial assistance may have a direct and material effect on the financial statements. As written, the standard appears to recite SAS 54 in terms of its broad application to *all* laws and regulations that have a direct and material effect. Is this really necessary?
- Paragraph 13g - Why does this include a reference to the Catalog of Federal Domestic Assistance? I'm not aware that it provides information about compliance requirements.
- Paragraph 17 - The reference to "common requirements" in the first sentence may lead to confusion (see footnote 9 to paragraph 14.). Also, what if the specific requirements for program audits are not enumerated in a federal grantor agency's audit guide or in the grant agreement or contract. What is the auditor's responsibility then?
- Paragraph 18 - Delete the reference in footnote 11 to SOP 92-7.

#

cc: Mary Foelster
Dan Guy
Jeanne Summo



INTERNAL MEMORANDUM

Date: August 31, 1994

Reply:

File No. J-1-402

To: Louise Williamson

From: Mary M. Foelster *MMF*

Subject: **Exposure Draft - Proposed Revised SAS No. 68**

The AICPA's Government Accounting and Auditing Committee has reviewed the exposure draft (ED) of the proposed Statement on Auditing Standards entitled, *Compliance Auditing Considerations in Audits of Governmental Entities and Other Recipients of Governmental Financial Assistance*. The committee asked me to submit their comments to you for consideration. Call me if you have any questions at extension 259.

Major Concern

Applicability to Program-Specific Audits. We believe that the Auditing Standards Board (ASB) needs to clarify the applicability of this proposed standard versus Statement on Standards for Attestation Engagements No. 3, *Compliance Auditing*, (SSAE3) relative to program-specific audits. There is already confusion among practitioners about the applicability of SSAE3 to program-specific audits, and this proposed standard will only add to the confusion.

Paragraph 1.c. indicates that this proposed standard is applicable to program-specific audits. Footnote 1 acknowledges that SSAE3 applies to engagements related to management's assertion about compliance or the control system to assure compliance. However, paragraph 2.d. of SSAE3 infers that SSAE3 applies to program-specific audits except those that have federal guides issued prior to its effective date. SSAE3 also contains certain conditions that must be met in order for a practitioner to perform an engagement related to management's written assertion about compliance or controls over compliance (SSAE3, paragraphs 9 through 13).

One interpretation of the above is that this proposed standard would apply to program-specific audit engagements that do not meet the conditions for engagement performance of SSAE3. Another interpretation is that this proposed standard only applies to program-specific audits that meet the exemption in paragraph 2.d. of SSAE3 and that AICPA members would be precluded from performing other program-specific audits unless they met the conditions for engagement performance of SSAE3. In addition, it is not clear which standard applies to program-specific audits that have an audit guide issued prior to the effective date of SSAE3, but such guide is revised after that date. There are also certain programs that have no federal audit guide; which standards apply to these programs? Finally, another area that is not clear is the applicability of standards for program-specific audits that are required to be performed in accordance with Government Auditing Standards (GAS).

August 31, 1994

Page 2

We strongly recommend that SSAE3 not be interpreted to preclude program-specific audits in situations where the conditions for an SSAE3 engagement are not met. While we agree that the management assertion/auditor attestation model may be the future of compliance auditing, we do not believe the structure is in place to require it now. The current structure of federal audit requirements is such that many existing potential program-specific audit engagements do not have federal audit guides issued before the effective date of SSAE3, nor do they meet the conditions for performance of paragraphs 9 through 13 of that Statement. Not allowing program-specific audits in these cases would result in the practitioner having to violate standards in order to help his or her clients to satisfy their federal audit requirement in the most cost effective way, or lose that business to non-AICPA members who can legitimately provide the service under GAS.

Over time, the AICPA should work with federal and other governmental agencies as they amend existing or develop new audit requirements to help them move toward the management assertion/auditor attestation type of engagement. In the meantime, however, the ASB should issue some specific guidance to clarify which standards apply to program-specific audits. This guidance could be issued as part of this revision to SAS No. 68 and/or as a revision to the scope section of SSAE3.

Other Program-Specific Audit Issues.

- Footnote 1 appears to be out of place and should be clarified to address the issues discussed in the above section of this letter.
- The third sentence of footnote 2 equates a program-specific audit with an audit conducted in accordance with a federal audit guide. This is not always true as detailed in the above section of this letter.

General Comments

Deleted Guidance. We are also unsure as to why certain sections of SAS No. 68, *Compliance Auditing Applicable to Governmental Entities and Other Recipients of Governmental Financial Assistance*, that were relatively generic were deleted. While we understand that much of the information that was deleted is included in the Audit and Accounting Guide, *Audits of State and Local Governmental Units* (the Guide), we believe that certain of the deletions should be left at the standards level. Therefore, we recommend adding back the following deletions from SAS No. 68:

- Paragraphs 12 through 14. We believe that these paragraphs provide good generic guidance on implementing SAS No. 53, *The Auditor's Responsibility to Detect and Report Errors and Irregularities*, and SAS No. 55, *Consideration of the Internal Control Structure in a Financial Statement Audit*, in a compliance environment.

- Paragraph 19. The representations that management is responsible for the entity's compliance with laws and regulations and that management has identified and disclosed to the auditor all laws and regulations were useful guidance for the client representation letter.
- Paragraph 91. The representations from management relating to single audits are good generic guidance. We believe this guidance is sufficiently important to be included in the final standard.

Need for Future Revisions. The ED still contains many references that will require future revision. The following are the areas that we noted during our review:

- Footnotes 4 and 11 refer to SOPs 92-7, *Audits of State and Local Governmental Entities Receiving Federal Financial Assistance*, and 92-9, *Audits of Not-for-Profit Organizations Receiving Federal Awards*. SOP 92-7 has recently been superseded. Its guidance is now incorporated in the body of the recent revision to the Guide. We are unsure as to whether there are similar plans for SOP 92-9.
- Paragraph 13.g. refers to the OMB Compliance Supplements by name. OMB eventually plans to replace the two Compliance Supplements with a single document to cover all entities. We recommend adding a parenthetical phrase such as, "or any future documents that are issued to replace them" when referring to documents that may be replaced. This also would apply to references to Circulars A-128, *Audits of State and Local Governments*, and A-133, *Audits of Institutions of Higher Education and Other Nonprofit Institutions*, since OMB eventually plans to combine those Circulars also.
- The discussion in Paragraphs 14, 15, and 17 of general, specific, and common compliance requirements is likely to change based upon recommendations in the PCIE Single Audit Study and what we understand will be contained in the revised A-128 Compliance Supplement. For purposes of this standard, it probably isn't important to refer to the types of compliance requirements by name (e.g., general, common, or specific), but merely to recognize that some requirements cover many programs and some are specific to individual programs. We recommend these paragraphs be rewritten to provide a more generic discussion of compliance requirements.
- Some program-specific audit guides may not use the word "major" to refer to the program being audited. Also, it is possible that the concept of major and nonmajor programs may change in future revisions to Circulars A-128 and A-133. To keep the guidance generic, we recommend revising the last sentence in paragraph 18 to read, "...the auditor may be required to express an opinion on whether the recipient has complied with the requirements applicable to one or more of its federal financial assistance programs." We also recommend deleting footnote 10.

- The paragraph 22 discussion of testing transactions of federal financial assistance programs other than major programs is likely to change based on recommendations of the PCIE Single Audit Study and current working drafts of a revision to OMB Circular A-133. We recommend that it be deleted.

Specific Comments

<u>Paragraph</u>	<u>Comment</u>
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- | | |
|---------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 1, footnote 3 | <p>The third sentence could be misinterpreted to indicate that references to GAS refer only to Chapters 4 and 5 of GAS, and not to Chapter 3 as well. Also, technically the GAS financial audit standards incorporate by reference some of the performance audit standards. We recommend that the third sentence be amended to indicate that the references to GAS refer to the standards that <u>apply to financial audits</u> to avoid misinterpretation.</p> <p>The last sentence states that “In July 1993, the General Accounting Office (GAO) issued an exposure draft of proposed changes to GAS.” This sentence should be rewritten to properly reflect the recent issuance of the 1994 revision of GAS.</p> |
| 9.b. | <p>For consistency with Section AU 319.26 of the <u>Codification of Statements on Auditing Standards</u>, we suggest that the first sentence be revised slightly to read “The auditor’s consideration of the internal control structure is to include obtaining and documenting an understanding of the accounting and administrative controls...”</p> |
| 11 | <p>The second sentence should be clarified for what “in all material respects” is relative to. For example, in a single audit materiality is relative to <u>each</u> major program.</p> |
| 13 | <p>This paragraph lists several procedures that the auditor should consider performing to assist in assessing management’s identification of laws and regulations. We have two comments on these procedures. First, paragraph 13.e. states “Review minutes of meetings of the legislative body of the governmental entity...” In addition to a legislative body that enacts laws and ordinances (e.g., city council, county commission, state legislature), many governmental entities also have a governing board that establishes rules and regulations (e.g., administrative board, board of trustees). Therefore, to provide more comprehensive guidance to the auditor, we suggest that paragraph 13.e. be expanded to read “Review minutes of meetings of the legislative body and/or the governing board of the governmental entity...” Second, paragraph</p> |

August 31, 1994

Page 5

13.g. states "Review information about compliance requirements,..." and lists three federal documents as examples. Because state governments may also establish compliance requirements, we suggest that paragraph 13.g. be expanded to include "...and State policies and procedures."

13-22 We do not believe that readers of this proposed standard will be clear as to what context these paragraphs are written. For example, do these paragraphs refer to the auditors responsibilities under generally accepted auditing standards, GAS, single audit requirements, program-specific audit requirements or all of these.

21 The last sentence may not always be true, or may not be true in the future. The next version of the Student Financial Aid (SFA) guide and the audit guide for SFA lenders is likely to require the projection of and reporting of "likely questioned costs." Also, a recent draft of revisions to OMB Circular A-133 also requires reporting of these "likely questioned costs." We recommend that the guidance be revised to reflect this.

MMF:jw

cc: Deborah A. Koebele
George A. Scott



46

September 12, 1994

Ms. A. Louise Williamson, Technical Manager
Auditing Standards Division, File 2357
American Institute of CPAs
1211 Avenue of the Americas
New York, NY 10036-8775

**Re: Exposure Draft on Proposed Statement on Auditing
Standards "Compliance Auditing Considerations in Audits
of Governmental Entities and Other Recipients of
Governmental Financial Assistance"**

Dear Ms. Williamson:

One of the objectives that Council of the American Institute of CPAs established for the Private Companies Practice Executive Committee is to act as an advocate for all local and regional firms and represent those firms' interests on professional issues, primarily through the Technical Issues Committee ("TIC"). This communication is in accordance with that objective.

TIC has reviewed the proposed guidance contained in the above referenced exposure draft related to compliance audits of governmental entities and other recipients of governmental financial assistance. Our comments and suggestions follow.

Introduction and Applicability

The title of the proposed Statement and the introductory portion of paragraph 1 seem to suggest the guidance only affects practitioners engaged to perform audits of financial statements of governmental entities and other recipients of governmental financial assistance. Although item e. briefly discusses the applicability of the Statement to auditors who become aware the entity is subject to additional audit requirements, we are concerned that practitioners performing a cursory reading of the document may not entirely understand how the Statement affects a GAAS audit of the financial statements. Therefore, it would be helpful if the introductory portion of paragraph 1 clearly described how this Statement impacts auditors who, during the conduct of a GAAS audit, determine the entity has been a recipient of governmental financial assistance.

Compliance Auditing

Paragraph 6 contains a quotation from paragraph 5.5 of the AICPA Audit and Accounting Guide, "Audits of State and Local Governmental Units." Consequently, it is confusing as to whether that guidance now applies to all recipients of governmental financial assistance, including not-for-profit organizations, hospitals, colleges and universities. Such reference also appears inconsistent with the stated purpose of the Statement, which, according to the Summary, is designed to "provide **generic** guidance to practitioners." Furthermore, from an administrative perspective, such approach could require revision of the Statement every time that guide is updated. Accordingly, we do not believe it is advisable to issue auditing standards with direct quotations from industry audit and accounting guides. If information from the guides is needed to help clarify a particular point, we believe it should be provided through general commentary. For example, if the quoted material in paragraph 6 applies only to audits of state and local governments, it could be written as follows, "In audits of general purpose financial statements of state and local governmental units, existing practice sets audit scope and applies materiality evaluations at the fund type and account group level."

Understanding the Effects of Laws and Regulations

Paragraph 13 provides procedures the auditor could consider performing to obtain an understanding of the laws and regulations that have a direct and material effect on amounts in the financial statements. Item b. lists the entity's legal counsel, among others, as a possible source of such information. In some instances, the auditor might be able to obtain written confirmation from outside legal counsel regarding the applicable laws and regulations. Accordingly, this procedure could also be listed as an available option.

Type of Audit Engagement

When the auditor becomes aware the entity is subject to an audit requirement that may not be encompassed in the terms of the engagement, paragraph 24 provides that management and the audit committee should be informed that a GAAS audit may not satisfy the relevant legal, regulatory or contractual requirements. This provision may be read to suggest that an auditor engaged to perform a GAAS audit has an obligation to apply further audit procedures whenever any information comes to his or her attention indicating the entity could be subject to additional audit requirements, whether or not that information could have a material effect on the financial statements. We believe it would be appropriate for the auditor to establish a materiality limitation for the purpose of determining whether such information warrants additional audit procedures.

Paragraph 25 provides guidance to the auditor when considering client actions in response to a communication required by paragraph 24. Although it advises the auditor to consider the potential effect on the financial statements and the auditor's report, we believe this section should also contain information on the specific actions that should be taken by the auditor (e.g., expression of a qualified or an adverse opinion, possible communication with parties outside the client) when management fails to arrange for an audit that meets the relevant requirements within the designated time period.

*

*

*

We appreciate the opportunity to present these comments on behalf of the Private Companies Practice Section. We would be pleased to discuss our comments with you at your convenience.

Sincerely,



Robert O. Dale, Chair
PCPS Technical Issues Committee

ROD:al
File 2221

cc: PCP Executive and PCPS Technical Issues Committees

June 19, 1991

File Ref. No. 1120

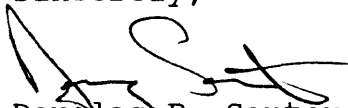
To the Auditing Standards Board:

Re: Exposure Draft of proposed SAS, Compliance Auditing Applicable to Governmental Entities and Other Recipients of Governmental Financial Assistance

Here are additional comment letters received to date on the proposed SAS, Compliance Auditing Applicable to Governmental Entities and Other Recipients of Governmental Financial Assistance.

<u>Name/Affiliation</u>	<u>Location</u>
9. Karl Denton Denton, Netherton & Co.	Englewood, Colorado
10. Douglas L. Blensly Accounting Principles & Auditing Principles State Committee	Glendale, California
11. Robert D. Hammond, CPA Clifton, Gunderson & Co.	Denver, Colorado
12. L. Michael Howard Committee on Accounting, Auditing and Financial Reporting	Chicago, Illinois
13. Unknown	
14. Michael J. Dean Harper, Van Scoik & Co.	Clearwater, Florida
15. Douglas R. Norton Auditor General	Phoenix, Arizona

Sincerely,



Douglas P. Sauter
Technical Manager
Auditing Standards Division

DPS/lf
Attachments

EXPOSURE DRAFT

FILE 2353

PROPOSED STATEMENT ON AUDITING STANDARDS COMPLIANCE AUDITING APPLICABLE TO GOVERNMENTAL ENTITIES AND OTHER RECIPIENTS OF GOVERNMENTAL FINANCIAL ASSISTANCE

April 9, 1991

Comment date: July 1, 1991

Name and Affiliation:

Karl Denton Denton, Wharton Ho, PC

Comments:

This draft certainly clears up a lot of wording problems.

The real problem is that the HUD housing authority audits are not SGAAP but some state boards in their reviews are calling them sub-standard because they don't follow SAAAS or SAAP.

Our firm has done housing authorities for 20 years and we don't have and have not had any problems with HUD. I hope you can solve this problem.

Instructions for Response Form

This response form may be used for comments or suggestions relating to any aspect of the exposure draft that is of concern or interest to you. For convenience, the most significant points have been identified in the summary that accompanies this exposure draft.

Return this response form to the address indicated on the reverse side by the comment date.



June 3, 1991

California
Society
Certified
Public
Accountants

Douglas P. Sauter, Technical manager
AICPA Auditing Standards Division
1211 Avenue of the Americas
New York, New York 10036-8775

Re: File 2353

Dear Mr. Sauter:

The state Accounting Principles and Auditing Standards Committee (AP/AS) and the Governmental Accounting and Auditing Committee (GAA) of the California Society of CPAs have reviewed the exposure draft of the proposed statement on "Compliance Auditing Applicable To Governmental Entities and Other Recipients of Governmental Financial Assistance."

Both committees agree that the proposed statement should be issued as soon as possible in the form that it was exposed.

While we do not take exception to the issuance of this statement, both committees would like to urge the Auditing Standards Board to revisit the matter of compliance auditing with a view to issuing a statement of a more generic nature so that it does not have to be amended or reissued every time the government changes rules and regulations.

Douglas L. Blensly, Chair
Accounting Principles and Auditing
Principles State Committee

(11)

June 5, 1991

Douglas P. Sauter,
Technical Manager
AICPA Auditing Standards Division
File 2353
1211 Avenue of the Americas
New York, NY 10036-8775

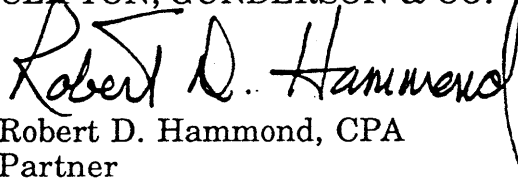
**Re: Exposure Draft
Compliance Auditing Applicable to Governmental
Entities and Other Recipients of Governmental
Financial Assistance**

Gentlemen:

We are pleased to have this opportunity to respond to the exposure draft cited above. Our comments are attached, and pertain primarily to one aspect of the draft which added a requirement for compliance auditing when there are no major Federal financial assistance programs involved. We feel very strongly about that aspect, and have included our comments at this time. We are continuing a careful review of the balance of the Draft, and may make additional comments prior to the deadline for comments.

If you have questions about the attached comments, please contact Robert D. Hammond, telephone (303) 452-2008, or at the address shown on this letterhead.

Cordially,
CLIFTON, GUNDERSON & CO.


Robert D. Hammond, CPA
Partner

MEMBERS OF
IAA INTERNATIONAL

A Worldwide Association
of Independent Accounting Firms

MEMBERS OF AMERICAN
INSTITUTE OF CERTIFIED
PUBLIC ACCOUNTANTS

Comments On
Exposure Draft

Proposed Statement on Auditing Standards
Compliance Auditing Applicable to Governmental Entities and Other
Recipients of Governmental Financial Assistance

We endorse the majority of this draft designed to clear up any misunderstanding in SAS 63, and to expand its coverage to include OMB Circular A-133. There is however one small section of the revisions which I do not feel is supported by the inclusion of Circular A-133 or any other Federal regulation that has been issued or implemented since the adoption of the Single Audit Act of 1984. We object in the strongest terms to the additions that those revisions attempt to make to the performance of a Single Audit.

Page 18, paragraph 45, titled "Compliance Auditing-General Requirements" begins with a reference to "The OMB's Compliance Supplement for Single Audits of State and Local Governments". It should be pointed out that the use of the Compliance Supplement **by direction of the Congress of the United States** is not mandated for use in Single Audits. Accordingly to quote that publication as support for adding significant auditing requirements is improper. That reference goes on to say that the general requirements are matters of significant national policy, and that failure to comply could have a material impact.... Two significant terms are used here--"could", not "does" or "will", and material impact. I offer that materiality is a decision that can only be made by the auditor, given the specific conditions in each audit.

Our strongest objection is to paragraph 48, page 19 which states: "The auditor should issue a report on compliance with the general requirements regardless of whether the government being audited has major programs.", and "If the tests of controls do not provide sufficient evidence to support a report on compliance, additional testing on the general requirements would need to be performed."

The requirement to perform additional testing to prepare a report not called for by the law or the related regulations would impose an unreasonable and unnecessary cost upon those receiving Federal financial assistance, and upon those who must perform the audits and historically have not been able to pass additional audit costs on to their clients.

Footnote 21 at the bottom of page 19 of the draft makes reference to Statement of Position 90-9, however that reference is to the consideration of internal control structure. We do not object to the requirement that General Compliance features be included in the evaluation of the internal control structure, and believe that that evaluation and report will provide the Federal agencies with sufficient information, to the extent intended by the Single Audit Act, to assess the financial management of Federal financial assistance.

Paragraph 93. b. Lists a requirement that is not contained in OMB Circular A-133, particularly as written in this statement. I have reviewed all of the elements of Circular A-133 and can find no statement in that document that states the the auditor must test and report on "Compliance with the general requirments applicable to the federal award programs." To the contrary all such references are to major programs.

We believe that this position is not supported by The Single Audit Act of 1984, OMB Circular A-128, or A-133, and would in fact impose a level of auditing on recipients of Federal financial assistance that clearly was opposed by the Congress of the United States when the Single Audit Act was passed. We offer the following citations in support of this position:

The Single Audit Act of 1984

Paragraph 7502 (d)(1)(2)(c) "...the government , department, agency, or establishment has complied with laws and regulations that may have a material effect upon each major Federal assistance program." The reference here is clearly to major Federal financial assistance program. The congressional hearings that accompanied the passage of the Single Audit Act contained substantial discussion on avoiding imposing a level of auditing which would be burdensome to those receiving small amounts of Federal financial assistance.

OMB Circular A-128

Paragraph 8. b. "Compliance review. The law also requires the auditor to determine whether the organization has complied with laws and regulations that may have a material effect on each major Federal financial assistance program."

Paragraph 8.b.(3) "Transactions related to other Federal assistance programs that are selected in connection with examinations of financial statements and evaluations of internal controls shall be tested for compliance with Federal laws and regulations that apply to such transactions."

OMB Circular A-133

Paragraph 12.b.(3) "The institution has complied with laws and regulations that may have a direct and material effect on its financial statements and on each major Federal assistance program."

Paragraph 13 c. (1) "In addition, transactions selected for non-major programs shall be tested for compliance with Federal laws and regulations that apply to such transactions."

AICPA Audits of State and Local Government Units

Page 182, para. 22.21 "However, such tests need only relate to the previously identified specific program compliance matters and need not address the general compliance identified."

Page 183, para. 22.22 "In the event that an entity has no major federal financial assistance programs...the only compliance testing required...is that previously described."

The audit guide was developed based upon the existing regulations which have not changed, and a review and understanding of the directions from congress in adopting the law that specifically discussed limiting to an absolute minimum the amount of additional auditing that would be imposed upon governments receiving non-major program assistance.

In conclusion, we urge that the wording in paragraph 45 be changed to leave it up to the auditor's discretion whether or not to perform a compliance audit sufficient to render a compliance report covering general requirements when only non major programs are present. We also urge the elimination, in paragraph 48, of reference to requirements for compliance auditing of general requirements where there are no major programs. We also urge that the wording in paragraph 93 b. conform to the actual wording in OMB Circular A-133 and not include, as fact, a statement that is not contained in the Circular.



**GOVERNMENT FINANCE
OFFICERS ASSOCIATION**

180 North Michigan Avenue, Suite 800, Chicago, Illinois 60601
312/977-9700 • Fax: 312/977-4806

June 2, 1991

Mr. Douglas P. Sauter
Technical Manager
Auditing Standards Division
American Institute of Certified
Public Accountants
1211 Avenue of the Americas
New York, NY 10036-8775

Dear Mr. Sauter:

On behalf of the Government Finance Officers Association (GFOA), the Committee on Accounting, Auditing and Financial Reporting (CAAFR) wishes to submit the following response to the American Institute of Certified Public Accountants' (AICPA) proposed statement on auditing standards (PSAS) Compliance Auditing Applicable to Governmental Entities and Other Recipients of Governmental Financial Assistance.

The CAAFR is one of five standing committees of the GFOA. Each committee may recommend positions to the GFOA's Executive Board or act on its own behalf within the confines of established GFOA policy and subject to the Executive Board's review in responding to exposure drafts, discussion memoranda, and proposed regulations and guidelines.

Members of the CAAFR are active finance officers involved in government at either the state or local level. The committee is advised by members of the public accounting profession and academics. For major responses to groups such as the AICPA, a task force is appointed from the membership of the committee to develop a response. A list of the members of the committee's auditing task force is attached.

The GFOA has three principal concerns with the amendments being proposed to Statement on Auditing Standards (SAS) No. 63:

1. Paragraph 3 of the PSAS appears to place the entire responsibility on management for obtaining audits that satisfy relevant legal, regulatory or contractual

WASHINGTON OFFICE

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202/429-2750 • Fax: 202/429-2755

Mr. Douglas P. Sauter
June 2, 1991
Page 2

requirements. Given the pervasiveness of such requirements in audits of recipients of governmental assistance, we believe auditors should assume greater responsibility for the adequacy of audit scope prior to accepting an engagement. Accordingly, the GFOA suggests that the first sentence of paragraph 3 be altered to read as follows:

Although management is responsible for obtaining audits that satisfy relevant legal, regulatory, or contractual requirements, the auditor should inquire of management as to the nature and extent of these requirements before agreeing to perform a GAAS audit.

2. Paragraph 79k suggests that language be added to the auditor's report on compliance for major federal programs to limit the intended audience for this report. Such language is appropriate in situations where auditors have not done enough work to render an opinion (e.g., "positive and negative assurance") because such reports could be open to misinterpretation by uninformed parties. In the case of major federal financial assistance programs, however, the auditor has performed the work needed to render an opinion. Therefore, in our view, a limitation on the distribution of this report is not appropriate.
3. Paragraph 95a is potentially misleading because the description of a major federal award program under OMB Circular A-133 (i.e., "federal expenditures total the larger of 3 percent of total federal funds expended or \$100,000") neglects to mention that this dollar threshold applies, not only to individual award programs, but also to categories of programs. Accordingly, paragraph 95a should be amended to reflect this fact, perhaps using the language found in the glossary entry "major federal award program" on page 38 of the PSAS.

In addition to these three issues, there are several minor technical issues that we also wish to raise:

- The language in note 3 to paragraph 3 should be modified so that it can apply to governmental entities as well as to nongovernmental recipients of financial assistance.

Mr. Douglas P. Sauter
June 2, 1991
Page 3

- The alteration to the first portion of paragraph 90 would create the false impression that materiality is judged in terms of each federal financial assistance program, regardless of whether a program is "major." In our view, it would be more appropriate to amend the language to refer to "a material effect on the entity's financial statements or a major federal financial assistance program."
- The description of the common rule furnished in the glossary should be incorporated within the text of the PSAS for the benefit of those unfamiliar with the common rule.

The GFOA appreciates being afforded the opportunity to respond to the AICPA's PSAS. If you have any questions, please feel free to call me (614\466-4971) or Stephen Gauthier, the GFOA's Director of Technical Services. Thank you.

Yours very truly,



L. Michael Howard
Task Force Chair
Committee on Accounting, Auditing and
Financial Reporting

EXPOSURE DRAFT

PROPOSED STATEMENT ON AUDITING STANDARDS

COMPLIANCE AUDITING APPLICABLE TO GOVERNMENTAL ENTITIES AND OTHER RECIPIENTS OF GOVERNMENTAL FINANCIAL ASSISTANCE

April 9, 1991

Comment date: July 1, 1991

Name and Affiliation:

Comments: Certain portions of Paragraphs 48 and 92 appear contradictory. Paragraph 48 states in part " The auditor should issue a report on compliance with the general requirements regardless of whether the government being audited has major programs." Paragraph 92 states in part, "... Nonprofit institutions that receive less than \$ 25,000 a year in federal awards are exempt from federal audit requirements..."

The SAS should clarify if the auditor for institutions receiving \$1. to \$ 25,000 of federal funds, should issue a compliance report on general requirements.

Instructions for Response Form

This response form may be used for comments or suggestions relating to any aspect of the exposure draft that is of concern or interest to you. For convenience, the most significant points have been identified in the summary that accompanies this exposure draft. Return this response form to the address indicated on the reverse side by the comment date.

14

HARPER, VAN SCOIK & COMPANY
Certified Public Accountants

REX E. HARPER, C.P.A.
WILBER G. VANSOIK, C.P.A.
JOHN H. GRAHAM, JR., C.P.A.
DAVID D. BURTON, JR., C.P.A.
RICHARD A. CRISTINI, C.P.A.
CHARLES W. WHETSTONE, C.P.A.
FRANK J. MANCOCK, C.P.A.
CHARLES D. RIGGS, III, C.P.A.
LAURA KRUEGER BROCK, C.P.A.
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MEMBERS
FLORIDA INSTITUTE OF
CERTIFIED PUBLIC ACCOUNTANTS
AMERICAN INSTITUTE OF
CERTIFIED PUBLIC ACCOUNTANTS
SEC AND
PRIVATE COMPANIES
PRACTICE SECTION

June 14, 1991

AICPA
Mr. Douglas P. Sauter, Technical Manager
Auditing Standards Division
1211 Avenue of the Americas
New York, New York 10036-8775

Dear Mr. Sauter:

We have enclosed for your review and use, a comment on the Exposure Draft,
Compliance Auditing Applicable to Governmental Entities and other recipients
of Governmental Financial Assistance.

Please contact us if you have any questions on this matter.

Very truly yours,

HARPER, VAN SCOIK & COMPANY



Michael J. Dean

MJD/bjr

Enclosure

15



STATE OF ARIZONA
OFFICE OF THE
AUDITOR GENERAL
June 13, 1991

DOUGLAS R. NORTON, CPA
AUDITOR GENERAL

Mr. Douglas P. Sauter, Technical Manager
AICPA Auditing Standards Division
AICPA File 2353
1211 Avenue of the Americas
New York, New York 10036-8775

RE: Exposure Draft - Proposed Statement on Auditing
Standards - Compliance Auditing Applicable to
Governmental Entities and Other Recipients of
Governmental Financial Assistance

Dear Mr. Sauter:

We have reviewed subject exposure draft and are in general agreement with its contents. However, we do have the following specific comments concerning it for your consideration.

1. For three of the required reports, there are no examples of the appropriate language to use when material weaknesses or material instances of noncompliance are identified.
 - For the report on internal control structure-related matters based solely on an assessment of control risk made as part of the audit of the financial statements in accordance with Government Auditing Standards, paragraph 39.k requires "a statement about whether the auditor believes any of the reportable conditions described in the report are material weaknesses and, if they are, identifies the material weaknesses noted." The example report in paragraph 40 illustrates the language when none of the reportable conditions are considered material, but there is no example of the language to be used when material weaknesses exist.
 - For the report on compliance with specific requirements applicable to nonmajor program transactions, paragraph 88.f requires "a statement of positive assurance that, with respect to the items tested, the results of those procedures disclosed no material instances of noncompliance with the specific requirements identified." However, neither the report requirements in paragraph 88 nor the illustrative report in paragraph 89 discusses how to report material instances of noncompliance.

Mr. Douglas P. Sauter
June 13, 1991
Page two

- For the report on compliance with general requirements, paragraph 50.e requires a similar "statement of positive assurance that, with respect to the items tested, the results of those procedures disclosed no material instances of noncompliance with the general requirements." Again, there is no guidance as to how to report material instances of noncompliance.
2. There is no clear definition of material instances of noncompliance as the term relates to general requirements. The Glossary defines general requirements as "those requirements that involve significant national policy and of which failure to comply could have a material impact on an organization's financial statements." This implies that noncompliance with any of the general requirements could be considered material. However, Appendix B, example 1.g refers only to noncompliance that would have a direct effect on the determination of cost-related amounts in the entity's financial statements. The Statement should clarify in what instances noncompliance with any of the general requirements would be considered material.
 3. Is it really necessary to describe any departure from the auditor's standard report in the required reports referred to in ¶23, ¶39, ¶50, ¶79, and ¶88? Since the auditor's report is issued in conjunction with the required reports and is referred to in them, the reader has the information readily available. Because the required reports are numerous and individually lengthy, we think there should be an effort made to lessen their content rather than unnecessarily expand it.

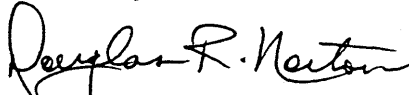
We also have the following comments of a more minor nature for your consideration.

1. Page 12, ¶22 - Suggest defining "direct-effect illegal acts." The Glossary does not define this term.
2. The definition of Common Rule in the Glossary should be expanded to describe its several major provisions and how it relates to Circular A-102.
3. Page 33, Appendix A, item number 5, first bullet under Report Issued heading - To be consistent with descriptions in the text, Appendix C, and with other report titles in this appendix, description should read "Report on compliance with specific requirements applicable to nonmajor federal financial assistance program transactions tested."

Mr. Douglas P. Sauter
June 13, 1991
Page three

4. In several paragraphs of Appendix B and in the Glossary definition of the Single Audit Act of 1984, "general-purpose" is hyphenated, but in previous pronouncements it hasn't been. Also, the statement in the Glossary definition of the Single Audit Act of 1984 that the Act requires an audit of the general purpose financial statements is incorrect. According to OMB's Questions and Answers on the Single Audit Process of OMB Circular A-128 "The Circular does not require the preparation of general purpose financial statements in accordance with GAAP. However, financial statements are required. The Circular requires an audit of financial statements that are prepared by the recipient to meet its needs and the needs of other statement users. However, if these statements are not prepared in accordance with generally accepted accounting principles, the audit report should state the nature of the variances therefrom and follow professional guidance for reporting on financial statements which have not been prepared in accordance with GAAP." Nowhere in the Single Audit Act of 1984 or OMB Circular A-128 is the modifier "general purpose" used in conjunction with "financial statements."

Sincerely,



Douglas R. Norton
Auditor General

DRN/DIW/gf

cc: Kinney Poynter
National State Auditors Association

July 15, 1991

File Ref. No. 1120

To the Auditing Standards Board:

**Re: Exposure Draft of proposed SAS, Compliance Auditing
Applicable to Governmental Entities and Other Recipients of
Governmental Financial Assistance**

Here are additional comment letters received to date on the proposed SAS, Compliance Auditing Applicable to Governmental Entities and Other Recipients of Governmental Financial Assistance. Please disregard the previous letter sent to you dated July 1.

<u>Name/Affiliation</u>	<u>Location</u>
16. James E. Bodtke	Peoria, Illinois
17. Terry D. Hill U.S. Department of Labor	Dallas, Texas
18. W. R. Snodgrass Comptroller of the Treasury	Nashville, Tennessee
19. Dave DePean PA Dept. of Health	Harrisburg, Pennsylvania
20. James M. Holloway, CPA South Carolina of CPAs	West Columbia, South Carolina
21. Gary Holstrum, Ph.D, CPA Florida Institute of CPAs	Tampa, Florida
22. Grover C. Austin, CPA Legislative Auditor	Baton Rouge, Louisiana

<u>Name/Affiliation</u>	<u>Location</u>
23. Gary E. Thornton, CPA Office of the State Auditor	Jackson, Mississippi
24. Joseph G. Eisele, CPA	Edmond, Oklahoma
25. Lawrence M. Wagner, CPA Public Health & Employment Services	Harrisburg, Pennsylvania

Sincerely,

Doug (et)

Douglas P. Sauter
Technical Manager
Auditing Standards Divison

DPS/lf

Enclosures

JAMES E. BODTKE, CHARTERED
CERTIFIED PUBLIC ACCOUNTANTS

8919 NORTH KNOXVILLE AVENUE
PEORIA, ILLINOIS 61615-1409
OFFICE (309) 691-7414
MODEM SECURED
FAX: (309) 692-8287

June 20, 1991

Douglas P. Sauter, Technical Manager
Auditing Standards Division
AICPA
1211 Avenue of the Americas
New York, Ny 10036-8775

Re: Exposure draft on Compliance Auditing dated April 9, 1991

Dear Mr. Sauter:

With respect to the above mentioned draft, we have the following comments:

PARAGRAPH 23

The topic sentence states we are to perform positive assurances on items tested and negative assurances on those items not tested, however, (f) states we are to place a scope limitation on the overall compliance of provisions, and disclaim an opinion on compliance with laws, regulation, contracts, and grants.

In the audit objectives to test management assertions, the auditor is required to design audit procedures to assure the completeness of the nature, timing and extent of testing sufficient to achieve the audit objectives. However, paragraph 23 is unclear as to what the auditor is attempting to achieve. Three scenarios could be derived from this paragraph:

We are expressing a piecemeal opinion in the form of positive assurances on those items tested. If this is the case, should not we disclose what we tested, as in an agreed upon procedure scope.

We are expressing a piecemeal opinion in the form of negative assurance on items we did not test. This is ludicrous. How can we give assurance on items we did not test!

We are claiming a scope limitation on the overall compliance and inserting the appropriate disclaimer. If this is the case, what is the purpose of the exercise. Let's leave out testing with laws, regs, and contracts altogether, eliminating the requirement, or let us test them and report them.

Auditing Standards Division
Page 2 of 2
June 20, 1991

We need to have clear language which is not contradictory in terms. Are we testing completely, giving assurance on items not tested, or simply inserting the scope limitation.

PARAGRAPH 30

The second sentence describes "the auditor ordinarily does not possess the expertise to form a conclusion about whether an illegal act or possible illegal act could result in criminal prosecution". In practice, we seriously doubt whether an auditor has the expertise to form a conclusion about whether an act is an illegal act, without the advice of counsel, trial, or ultimately the decision of the court. Our comment is not directed to the repeal of SAS 54 however, it is our opinion the procedures for illegal acts should follow the steps of the joint AICPA / ABA policy on lawyer's letters.

Upon discovery of the a potential violation or illegal act, the auditor should immediately inform the proper officials.

The auditor should request those officials to specifically obtain the advice of counsel to determine the disclosures necessary under FASB 5, or to reach a conclusion a disclosure is unnecessary.

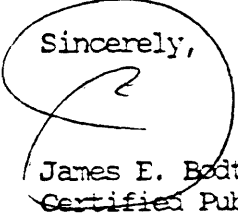
The auditor should then determine the appropriate disclosure in the basic financial statement or consider disclaiming an opinion in the report based upon a scope limitation of limited or untimely response.

We believe these requirements make much more sense, result in less liability, and provide for better service to the public. The requirements noted in paragraph 31, set forth in Government Auditing Standards, of releasing reports omitting such acts, or somehow conveying information in separate [secret?] reports not released to the public, is not something our profession should be condoning or abetting.

As evidence to the above I submit to you today's Wall Street Journal as an attachment. Will the "expectation gap" lead to the "credibility gap"?

We thank you for hearing our comments.

Sincerely,


James E. Bötke
Certified Public Accountant

Price Waterhouse Affiliate Omitted Concerns Over Lending in BCCI Audit

By PETER TRUPELL
And LEE BERTON

Staff Reporters of THE WALL STREET JOURNAL

When Price Waterhouse's British affiliate signed BCCI Holdings (Luxembourg) S.A.'s consolidated 1989 accounts, it said they gave a "true and fair" view of the company's business.

But those public accounts, dated April 30, 1990, didn't tell the full story. In January 1990, the Price Waterhouse affiliate privately made available to BCCI management a special audit that pointed to massive shortcomings in the bank's lending policies and internal controls. The audit found that huge loans were far too concentrated among a few individual borrowers, weren't checked by appropriate credit units of the bank, and frequently were made to close associates of top BCCI managers. At least some of the borrowers failed to make timely interest and principal payments. The bank also had violated foreign currency laws in Pakistan.

The discrepancy between Price Waterhouse's public and private assessments may taint the accounting firm's reputation. The sixth biggest U.S. accounting firm—with a lion's share of big bank and company audits—Price Waterhouse long has been considered the Mr. Clean of major accounting firms.

Since 1987, Price Waterhouse has been the sole auditor of BCCI, or Bank of Credit & Commerce International, the international institution that now is under investigation by government attorneys in New York, Florida and Washington, D.C. In that period, BCCI, because of continued faulty—and possibly fraudulent—lending and banking practices, as well as a lack of record-keeping, has lost several billion dollars, according to investigators and bank regulators.

New York-based Price Waterhouse and its British affiliate of the same name are legally separate but affiliated partnerships. Although Price Waterhouse's U.K. affiliate headed the BCCI audit team, the U.S. firm did some audit work on BCCI's U.S. units starting in 1987.

Shaun O'Malley, chairman of Price Waterhouse in New York, said a U.S. grand jury in New York a few months ago subpoenaed records of the U.S. affiliate related to BCCI. "We're fully cooperating with regulatory authorities in this investigation," he said.

But parties close to the investigation say that Robert Morgenthau, the Manhattan district attorney, has been highly frustrated in his attempts to get the work papers of Price Waterhouse's British affiliate regarding audits of BCCI units overseas.

The U.K. firm has told its U.S. partners that it believes nothing irregular occurred in its auditing of BCCI. "I have been assured by the senior partner of the U.K. firm," says Mr. O'Malley, "that it believes that its prior audits were performed by competent professionals in accordance with professional standards." A spokeswoman for the British unit declined to

chaotic lending relationships, including its loans to shareholders in Credit & Commerce International Holdings N.V., the parent company of First American Bankshares Inc.; to the Gokals, a Pakistani shipping family; to Saudi investor Ghaith Pharaon; to the Saigols, a family of Pakistani merchants; and to London's Cromwell Hospital.

Describing \$838 million of BCCI bank loans secured by shares in the parent company of First American Bankshares, the report says that there were "no loan agreements on many of these loans," "no third party evidence," "no prior appraisals" for the lending, and "loans in

Please Turn to Page A4, Column 2

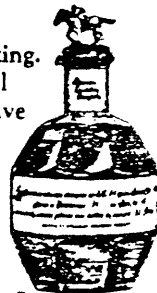
BLANTON'S RATED NUMBER ONE IN BOURBON TASTING.

Here are the results of a blind tasting conducted by Washingtonian magazine. As you see, Blanton's finished first,* and by a wide margin. For unlike other Bourbons, Blanton's is never blended. Each bottle is hand-filled from a single barrel just as the Bourbon has matured to perfection.

Rating Bourbons

Points	Brand	Proof	Age	Price	Distiller
43	Blanton	93	8	\$32.79	Blanton
32	Old Fitzgerald's 1849	98	8	11.99	Old F
30	Jim Beam	90	7	15.99	Jimm
28	George Dickel No. 12	90	8	14.49	Geo
23	Wild Turkey	101	12	31.95	Aut
21	Wild Turkey 12	94	12	8.99	ET
19	Elija Craig	94.6	21	21.49	D
16	Collector's Edition	114	—	17.99	C
16	Old Grand-Dad 114	88	—	7.49	E
14	Jim Beam	107	7	15.99	
12	Old Weller	90	7	7.49	
7	Evon Williams	80	—	19.95	
7	Gentleman Jack	90	—	12.99	
7	Maker's Mark	101	10	14.69	
5	Eagle Rare	—	—	10.99	
5	Jack Daniel's Black Label	86	—	—	

Conduct your own tasting. We believe you too will elect to drink — and give — Blanton's. To find out where to purchase Blanton's, please call 1-800-654-8471.

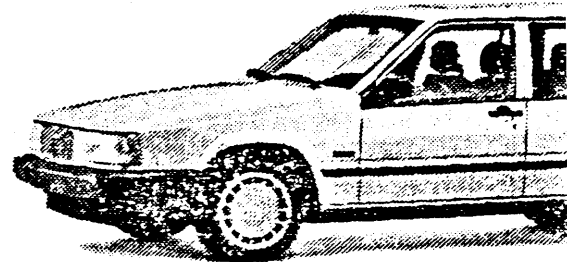


Blanton's



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*Offered by participating Volvo dealers to qualified and a take delivery by July 5, 1991. Prices may vary based on dea lease of the 744 sunroof automatic sedan with metallic pa monthly payments of \$379 for the 745 sunroof automatic w 944 SE sunroof automatic sedan or the 945 SE sunroof at signing for first monthly payment of \$359 for the 744 SA s insurance, taxes, title and registration fees. 15 cents per m abnormal wear and tear. Option to purchase at end of lease Finance North America, Inc. Finance Program: The follo shown include dealer contributions; dealer contributions; and selling price of \$23,487. \$379 per month for 1991 745 SA for 60 months, based on APR of 7.50% and selling price of Insurance, taxes, title and registration fees extra. **Which for complete details and limitations of this lease or financ

SEE VA

U. S. Department of Labor

Employment and Training Administration
Federal Building
525 Griffin Street
Dallas, Texas 75202



Reply to the Attention of: 6TGB

June 21, 1991

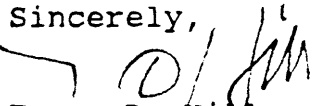
Mr. Douglas P. Sauter, Technical Manager
AICPA Auditing Standards Division
File 2353
1211 Avenue of the Americas
New York, NY 10036-8775

Dear Mr. Suater:

Enclosed are my comments concerning the Exposure Draft on the Proposed Statement on Auditing Standards - Compliance Auditing Applicable to Governmental Entities and Other Recipients of Governmental Financial Assistance.

If you have any questions, please call me at 214-767-4970.

Sincerely,


Terry D. Hill
System Accountant

Enclosures

EXPOSURE DRAFT

FILE 2353

PROPOSED STATEMENT ON AUDITING STANDARDS

COMPLIANCE AUDITING APPLICABLE TO GOVERNMENTAL ENTITIES AND OTHER RECIPIENTS OF GOVERNMENTAL FINANCIAL ASSISTANCE

April 9, 1991

Comment date: July 1, 1991

Name and Affiliation: Terry D. Hill Member #01507995
U.S. Dept of Labor - Employment & Training Administration

Comments: Pages 10 & 11 (Item 15)

I suggest addition of item e in describing laws and regulations that may have a direct and material effect on the determination of amounts in financial statements.

Item e would read:

"Uniform Administrative Requirements - administrative requirements applicable to federal financial assistance programs"

This would incorporate OMB Circulars A-102 and A-110 which includes standards, including those for financial management systems, which should be considered in audit of the financial statements.

Instructions for Response Form

This response form may be used for comments or suggestions relating to any aspect of the exposure draft that is of concern or interest to you. For convenience, the most significant points have been identified in the summary that accompanies this exposure draft. Return this response form to the address indicated on the reverse side by the comment date.



18

STATE OF TENNESSEE

William R. Snodgrass

COMPTROLLER OF THE TREASURY

Comptroller

STATE CAPITOL

NASHVILLE, TENNESSEE 37243-0260

PHONE (615) 741-2501

June 21, 1991

Mr. Douglas P. Sauter, Technical Manager
Auditing Standards Division, File 2353
AICPA
1211 Avenue of the Americas
New York, New York 10036-8775

Dear Mr. Sauter:

I appreciate the opportunity to comment on the proposed Statement on Auditing Standards (SAS) "Compliance Auditing Applicable to Governmental Entities and Other Recipients of Governmental Financial Assistance."

1. The reporting requirements include "a reference to the auditor's report on the financial statements, including a description of any departure from the standard report," for each of the reports issued (e.g., paragraphs 23a, 39a, 50a, 79a, and 88a). When these reports are issued in a single document with the financial statements and auditor's opinion letter, it should not be necessary for each report to include a description of any departure from the standard report.
2. Regarding testing compliance (specific and general) requirements on nonmajor federal financial assistance programs, OMB Circular A-128, 8.b.(3), states:

Transactions related to other Federal assistance programs that are selected in connection with examinations of financial statements and evaluations of internal controls shall be tested for compliance with Federal laws and regulations that apply to such transactions.

Paragraphs 45 through 51 indicate that reports should be issued on general requirements regardless of whether nonmajor program transactions are selected in the audit process. Does this mean that the auditor will be expected to test general requirements applicable to each program whether transactions related to those programs are selected in the sampling process? This question relates to the government that has both major and nonmajor programs. Would the answer be different for governments without major programs? For example, if a government has eight nonmajor programs (in addition to

major programs) and transactions are selected (through the sampling process) that are applicable to three of those nonmajor programs, should the auditor test

- general requirements applicable to the selected transactions of the nonmajor programs?
- all of the general requirements applicable to the three nonmajor programs?
- all of the general requirements applicable to each of the eight programs?

This section should be clarified to make these distinctions.

3. Paragraph 90 relates materiality to federal financial assistance programs. Typically materiality for major programs relates to the major program, and materiality for nonmajor programs relates to the financial statements.

Consideration of my concerns would be appreciated.

Very truly yours,



W. R. Snodgrass
Comptroller of the Treasury

WRS/jr

EXPOSURE DRAFT

FILE 2353

PROPOSED STATEMENT ON AUDITING STANDARDS

COMPLIANCE AUDITING APPLICABLE TO GOVERNMENTAL ENTITIES AND OTHER RECIPIENTS OF GOVERNMENTAL FINANCIAL ASSISTANCE

April 9, 1991

Comment date: July 1, 1991

Name and Affiliation: Dave DeFau, Audit Coordinator, PA Dept. of Health.

Comments: 1. The guidance provided in Paragraph 4 is too vague.

At the least, it should specify the applicable guidance in SAS No. 54; i.e., Paragraphs 22-23. If the engagement is accepted, it should be disclosed in the auditor's report that a GAAS audit of the financial statements does not satisfy all relevant legal, regulatory, or contractual requirements and specify the reasons therefor. Failure to do so could be considered a violation of AICPA Ethics Interpretation 501-3, "Failure to Follow Standards and/or Procedures or Other Requirements in Governmental Audits." It could also leave the auditor vulnerable to legal and regulatory action.

Per the above discussion, the Statement should be amended to include a statement such as the following:

If the client refuses to arrange for an audit that meets the applicable require-

Instructions for Response Form

This response form may be used for comments or suggestions relating to any aspect of the exposure draft that is of concern or interest to you. For convenience, the most significant points have been identified in the summary that accompanies this exposure draft. Return this response form to the address indicated on the reverse side by the comment date.

CUT ALONG LINE

Comments (continued):

ment, the auditor should withdraw from the engagement and indicate the reasons for withdrawal in writing to the audit committee or board of directors.

2. Paragraph 100 should be amended to make the following mandatory:

- Use of a proposal, contract, or engagement letter.
- Inclusion of a statement in the proposal, contract or engagement letter as to the type of engagement and whether the engagement is intended to meet a governmental oversight agency's audit requirements.

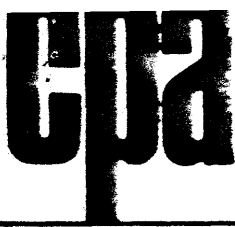
Return responses to:

AICPA

Douglas P. Sauter, Tech. Mgr.
Auditing Standards Division
1211 Avenue of the Americas
New York, NY 10036-8775

Please send 2 copies of the final Statement (and 1 or 2 copies of any further Exposure Drafts of this Statement) to the following address:

Commonwealth of Pa/Dept. of
Health
Audit Coordinator
Bureau of Financial Mgmt.
P.O. Box 90
Rm 933/Health and Welfare Build
Harrisburg, Pa 17108



South Carolina Association
of Certified Public Accountants
570 Chris Drive
West Columbia, SC 29169
(803) 791-4181



June 25, 1991

Mr. Douglas P. Sauter
Technical Manager
AICPA Auditing Standards Division, File 2353
AICPA
1211 Avenue of the Americas
New York, New York 10036-8775

Dear Mr. Sauter:

The Technical Standards Committee of the South Carolina Association of Certified Public Accountants has reviewed the Exposure Draft of the proposed statement on auditing standards "Compliance Auditing Applicable to Governmental Entities and Other Recipients of Governmental Financial Assistance". We believe the proposed statement will provide a useful revision to SAS No. 63.

Our specific comment to the Exposure Draft (the ED) is in the following area:

We concur with the ED as presently written. We observe that the ED will necessitate communications with client entities regarding reporting expectations, scope and fee considerations. Further, practitioners must react to the final document through personnel training and engagement administration considerations. We recommend the effective date be delayed one year to fiscal periods ending after December 15, 1992.

Thank you for the opportunity to comment.

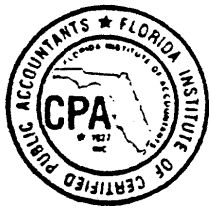
Very truly,

A handwritten signature in cursive script that reads "James M. Holloway".

James M. Holloway, CPA
Chairman, Technical Standards Committee
South Carolina Association of
Certified Public Accountants

cc: Members of the Committee
C. John Wentzell, CPA
Lollie B. Coward, SCACPA

28



FLORIDA INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS

325 WEST COLLEGE AVENUE • P.O. BOX 5437 • TALLAHASSEE, FLORIDA 32314
TELEPHONE (904) 224-2727 • FAX (904) 222-8190

June 17, 1991

Mr. Douglas P. Sauter, Technical Manager
AICPA Auditing Standards Division
File 2353
AICPA
1211 Avenue of the Americas
New York, NY 10036-8775

We are pleased to respond to the Auditing Standards Board's (ASB's) exposure draft of a proposed statement on auditing standards entitled "Compliance Auditing Applicable to Governmental Entities and Other Recipients of Governmental Financial Assistance."

Overall, the committee agrees that the ASB has done a good job of incorporating the requirements of OMB 133 into the proposed SAS. However, members of the committee also believe that the ASB should consider other alternatives in addressing these types of issues. Many members of the committee believe that the SAS should be more of a "core" document and the specifics of the applicable OMBs (as well as other subsequent documents which may impact this field of auditing) being addressed in other medium such as Guides or SOPs. This is particularly germane since the AICPA's looseleaf service makes many of these other types of documents available to practicing CPAs in a much more timely fashion than can be accomplished by having to undergo the due process associated with amending a SAS.

Another concern voiced by members of the committee is that this approach leaves the ASB in a position of being reactive rather than proactive in its standard-setting activities. Additionally, when the ASB is incorporating other documents into an SAS as is the case here, it is imperative that the SAS very clearly delineate the circumstances in which the guidance would be applicable.

In addition to these general comments, the committee has specific comments directed towards paragraphs in the exposure draft.

Paragraph 3

The committee agrees with the assertion that it is the responsibility of management to report to applicable regulatory bodies or other authoritative entities. However, the committee believes that it is important for this paragraph to contain a cross-reference to SAS 61 to underscore the auditor's responsibilities for reporting to the audit committee if one exists.

Paragraph 45

The committee is concerned with the wording change in the first sentence of this paragraph: "The OMB's Compliance Supplement for Single Audits of State and Local Governments, which implements . . ." The supplement does not implement. We suggest that more appropriate wording might be "provides guidance for implementing" or similar wording.

Paragraph 48

It should be made clear that this paragraph is intended to address the new requirements of the OMB.

Paragraph 92 - 95

Clarification needs to be provided as to whether this constitutes auditor's responsibilities under OMB 133. Particularly, paragraph 95(b) accomplishes essentially the same as OMB 128.

Paragraph 97

It is not clear whether this paragraph is intended to take the general guidance of SAS 63 and overlay specific requirements which may be mandated by a certain program (such as for many HUD audits) or whether this is intended to be general guidance for all circumstances to which the proposed SAS would apply. While the majority of the committee read paragraph 97 as meaning the former, there were members of the committee who felt the latter interpretation could be gleaned from the paragraph.

We appreciate the opportunity to provide comments in response to this exposure draft. Representatives of our committee are available to discuss these comments with the Board or its representatives at their convenience.

Sincerely,

Gary Holstrum FIC

Gary Holstrum, PhD, CPA
Chairman

Committee on Accounting Principles and Auditing Standards
Florida Institute of Certified Public Accountants

Task Force to Respond to Exposure Draft:

Paul Munter, DBA, CPA
Steve Kattell, CPA
Ed Leonard, CPA



DANIEL G. KYLE, Ph.D., CPA
LEGISLATIVE AUDITOR

OFFICE OF
LEGISLATIVE AUDITOR
STATE OF LOUISIANA
BATON ROUGE, LOUISIANA 70804-9397

June 24, 1991

1600 RIVERSIDE N.
P.O. BOX 94397
TEL. (504) 342-7237
FAX (504) 342-7144

Mr. Douglas P. Sauter, Technical Manager
Auditing Standards Division, File 2353
American Institute of Certified
Public Accountants
1211 Avenue of the Americas
New York, New York 10036-8775

Dear Mr. Sauter:

I have reviewed the Exposure Draft of the proposed amendment to SAS No. 63. In general, I concur with the proposed amendment; however, I believe that paragraph number 3 should be revised as indicated below (language to be deleted is shown with a line drawn through and new language is shown in italics).

....Therefore, if during a GAAS audit of the financial statements the auditor becomes aware that the entity is subject to an audit requirement that is not encompassed in the terms of the engagement, the auditor should communicate to management *and* the audit committee, or others with ~~equivalent~~ authority and responsibility³ *equivalent to that of an audit committee*, that an audit in accordance with generally accepted auditing standards may not satisfy the relevant legal, regulatory, or

As written in the proposed revision, paragraph 3 indicates that an auditor may satisfy the standard by notifying management, but not other appropriate parties, about deficiencies in an audit engagement. However, reporting such matters solely to management does not ensure that all appropriate parties are informed. Furthermore, if an audit committee or other equivalent authority was involved in preparing the request for proposal, selecting the auditor, and/or signing the engagement agreement, et cetera, all matters affecting the propriety of the engagement agreement should be communicated to that party.

In another matter, if the board is unable to issue the revised statement soon after the close of the comment period, consideration should be given to extending the effective date of implementation. It is important to understand that some entities will engage their audit for the

Mr. Douglas P. Sauter
June 24, 1991
Page 2

year ending December 31, 1991, as much as six months before the year-end. The auditor, as well as the entity, should know which auditing standards are applicable to an audit at the time the audit engagement is signed.

If you have any questions concerning these comments, please feel free to call me.

Sincerely,



Grover C. Austin, CPA
Assistant Legislative Auditor

GCA/db

cc: Mr. Kinney Poynter
NSAA

SAS63



STATE OF MISSISSIPPI
OFFICE OF THE STATE AUDITOR

PETE JOHNSON
STATE AUDITOR

POST OFFICE BOX 956
JACKSON, MISSISSIPPI 39205-0956
(601) 359-3561
FAX: (601) 359-1490

MEMORANDUM

TO: Douglas P. Sauter, Technical Manager, AICPA Auditing Standards Division, File 2353
FROM: Gary Thornton, CPA, Manager, School District Audits
DATE: June 24, 1991
SUBJECT: Comments regarding exposure draft of proposed statement on auditing standards titled "Compliance Auditing Applicable to Governmental Entities and Other Recipients of Governmental Financial Assistance"

Para. #	Comments
41	The second sentence should not mention "reportable" since the term "reportable condition" is not defined due to the deletion of paragraph 7 of the example report. See AU section 9325.04 for a correct example.
43(b)	The Single Audit Act of 1984 and OMB Circular A-128 only require the auditor to consider compliance with "laws and regulations that may have a material effect on its (the entity's) financial statements and on each major Federal assistance program." Paragraph 45 of this proposed SAS states that "The general requirements may or may not be laws and regulations that have a direct and material effect on the determination of financial statement amounts." Only page 2-3 of the <u>Compliance Supplement</u> states that the general requirements "shall be included as part of every audit ... whether or not the government has a major program." Since neither the Single Audit Act of 1984 or OMB Circular A-128 appears to give the OMB the authority to expand the requirements placed upon the auditor by them with regards to testing for compliance with laws and regulations, it appears reasonable to conclude that the requirement contained in the <u>Compliance Supplement</u> must refer only to testing in the context of materiality to the financial statements rather than in terms of testing nonmajor programs per se. It appears reasonable to require a report on general requirements even when there are no major programs since to do otherwise might lead the auditor to believe that he is justified in omitting disclosure of noted noncompliance with the general requirements when there are no major programs.

However, the reporting requirements should be changed, not the auditor's responsibility to test nonmajor programs for compliance with the general requirements that are not required to be tested as part of the audit of the financial statements due to them not having a material effect.

48 This paragraph should be changed to be consistent with the comments reflected above and below regarding the auditor's responsibilities for testing compliance with general requirements related to nonmajor programs.

51 Consistent with comments above, the example report should be changed to reflect that procedures were applied to major programs only and that negative assurance regarding nonmajor programs is based on the results of other procedures rather than procedures applied expressly to test compliance with the general requirements applicable to nonmajor programs.

Sincerely,

Gary E. Thornton

Gary E. Thornton, CPA

Note - These comments are personal and may not reflect the position of my employer, co-workers and/or any professional organizations or committees with which I am associated.

(24)

Joseph G. Eisele CPA

6600 Applewood Drive
Edmond, Oklahoma 73034
(405) 340-6695

June 26, 1991

David P. Sauter, Technical Manager
AICPA Auditing Standards Division
1211 Avenue of the Americas
New York, NY 10036-8775

Re; File No. 2353

Dear Mr. Sauter:

I am in general agreement with the above referenced proposed Statement.

The proposed paragraphs No. 3 and 4, however, are inappropriate and should not be included in the auditing standards. I believe the responsibility discussed in paragraph No. 3 is too general. Possible non-compliance with a contractual obligation is a frequent discovery in an audit engagement. The Board should not select this possibility for prominence in a Statement on Auditing Standards. If guidance is needed on contract compliance, a separate Statement should be proposed.

I appreciate the opportunity to share my view.

Sincerely,



Joseph G. Eisele

EXPOSURE DRAFT

File 2353

PROPOSED STATEMENT ON AUDITING STANDARDS

COMPLIANCE AUDITING APPLICABLE TO GOVERNMENTAL ENTITIES AND OTHER RECIPIENTS OF GOVERNMENTAL FINANCIAL ASSISTANCE

April 9, 1991
Comment Date: July 1, 1991

Name and Affiliation: Lawrence M. Wagner, Audit Manager
Public Health and Employment Services
Comptroller's Office - Audits Division
P.O. Box 3652
Harrisburg, Pennsylvania 17105

Comments:

1. Comments as it pertains to Paragraph 3 in conjunction with Paragraph 99 are the following:

The auditor's responsibility for testing and reporting on compliance with laws and regulations varies according to the engagement. The auditor should perform certain procedures to exercise due to professional care in understanding the type of engagement that the auditor is to perform versus what is required by regulatory agencies. The auditor should perform certain procedures to determine what the scope of the audit should be. These procedures may include:

- Determining the entity's programs, functions and activities; and
- Obtaining an understanding of the entity's organizational structure.

The auditor should also be alert for possible violations of audit requirements.

2. The comment as it pertains to Paragraph 4 is the following:

If management does not agree with the auditor's conclusion, it should be referenced in the audit report. Restrictions on the scope of the audit may require the auditor to qualify the opinion. The reason for such qualification should be described in the report.

EXPOSURE DRAFT
(Page 2)

3. The comment as it pertains to Paragraph 15 is the following:

Both governmental and nongovernmental entities may be subject to laws and regulations that may have a direct and material effect on the determination of amounts in their financial statements. Such laws and regulations may deal with the following matters:

- Cost Allocation. In order to recover indirect costs, the recipient must develop a cost allocation plan that provides the basis for the indirect cost rate. The plan must consider all indirect costs of the department administering the grant and other agencies' costs that will be charged against the grant. Additionally, the auditor should be aware that federal grants may be subject to laws that limit the amount of indirect costs that may be allowed; and
- Monitoring Subrecipients. Subrecipients should be monitored to determine whether the subrecipient spent federal assistance provided in accordance with applicable laws and regulations.

4. The comment as it pertains to the "Glossary" is the following:

The definition for specific requirements should include cost allocation and monitoring subrecipients.

July 16, 1991

File Ref. No. 1120
2353

To the Auditing Standards Board:

**Re: Exposure Draft of proposed SAS, Compliance Auditing
Applicable to Governmental Entities and Other Recipients of
Governmental Financial Assistance**


Here are additional comment letters received to date on the proposed SAS, Compliance Auditing Applicable to Governmental Entities and Other Recipients of Governmental Financial Assistance.

<u>Name/Affiliation</u>	<u>Location</u>
26. Brant Hardy, CPA NH Society of CPAs	Bedford, New Hampshire
27. Daniel R. Janet Fangmeyer & Fangmeyer	Silver Spring, Maryland
28. Joseph Scansaroli, CPA	Johnstown, Pennsylvania
29. J. David Barba, CPA Office of State Auditor	Denver, Colorado
30. Kathryn M. Howard Anderson Associates	Baltimore, Maryland
31. Coopers & Lybrand	New York, New York
32. Joseph Delaney, CPA Office of State Auditor	Olympia, Washington
33. Thomas H. McTavish, CPA Office of the Auditor General	Lansing, Michigan

Auditing Standards Board
July 16, 1991
Page two

- | | |
|------------------------------------------------------------------|--------------------------|
| 34. J. Dwight Hadley
Office of the State
Comptroller | Albany, New York |
| 35. J. Dwight Hadley
Association of Government
Accountants | Alexandria, Virginia |
| 36. Joseph Delaney, CPA
Office of State Auditor | Olympia, Washington |
| 37. Vickie Rauser
Office of the Legislative
Auditor | Helena, Montana |
| 38. Hugh J. Posner
Society of Louisiana CPAs | Kenner, Louisiana |
| 39. Ernst & Young | Cleveland, Ohio |
| 40. Margaret Kelley, CPA
State Auditor of Missouri | Jefferson City, Missouri |

Sincerely,



Douglas P. Sauter
Technical Manager
Auditing Standards Division

DPS/lf
Enclosure



NEW HAMPSHIRE SOCIETY OF CERTIFIED PUBLIC ACCOUNTANTS
3 EXECUTIVE PARK DRIVE • BEDFORD, NEW HAMPSHIRE 03102-2137
TEL. (603) 622-1999 • FAX (603) 626-0204

June 14, 1991

Mr. Douglas P. Sauter
Technical Manager
AICPA Auditing Standards Division
1211 Avenue of the Americas
New York, NY 10036-8775

File #2353

Dear Mr. Sauter:

On behalf of the Auditing and Accounting Committee of the New Hampshire of CPAs, I am pleased to comment on the Proposed Statement on Auditing Standards Exposure Draft " Compliance Auditing Applicable to Governmental Entities and to Other Recipients of Governmental Financial Assistance".

General

We welcome the boards efforts to bring compliance auditing for "non-profit organizations" up to the same standards already achieved by "states and local governmental units". We feel that the board has achieved this with the new proposed statement on auditing standards.

Additional Guidance Requested

Until recently, non-profit organizations receiving federal financial assistance were required to render three reports namely:

- . Report on Financial Statements
- . Report on Internal Control
- . Report on Compliance with Laws and Regulations

These three reports were relatively easy to explain to the users of financial statements.

Since the introduction of SAS #63 and now with the proposed changes to incorporate OMB Circular A-133, the auditors' reports have been changed as follows:

- . The report on internal control has been replaced with two separate reports on internal control.
- . The report on compliance has been replaced with four separate reports on compliance.

It will be difficult to explain to the users of financial statements the purpose of these separate reports. We would prefer to see a return to the "three report" concept. We believe that this can be accomplished by combining the two reports on internal control into one and combining the four reports on compliance into one.

We believe that it is important for the Auditing Standards Board to give examples how these combined reports may be drafted by practitioners.

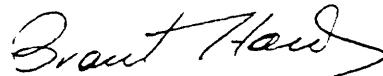
We note with great interest that SOP 90-9 "The Auditors Consideration of the Internal Control Structure Used in Administering Federal Financial Assistance Programs Under the Single Audit Act" has already combined the internal controls reports for state and local governmental units.

We, therefore, urge the board to consider incorporating into the proposed new statement on auditing standards examples of a "combined internal control report" and a "combined compliance report". We believe that this will reduce the level of confusion amongst the readers of the financial statements.

The above comments are the opinions of the Auditing and Accounting Committee of the New Hampshire Society of CPAs and do not necessarily reflect the views of the Society as a whole, nor of its Board of Directors, nor of the individual members of the Board.

Should you have any questions concerning the above, please contact Brant Hardy at (508)632-3050.

Yours truly,



Brant Hardy, CPA
Chairman
Auditing and Accounting Committee
New Hampshire Society of CPAs

EXPOSURE DRAFT

FILE 2353

PROPOSED STATEMENT ON AUDITING STANDARDS

COMPLIANCE AUDITING APPLICABLE TO GOVERNMENTAL ENTITIES AND OTHER RECIPIENTS OF GOVERNMENTAL FINANCIAL ASSISTANCE

April 9, 1991

Comment date: July 1, 1991

Name and Affiliation:

Comments:

1. you people have nothing to do but make constant changes. The accounting and auditing rules are more complex than the IRS Code.

2. why do you not send the membership copies of the final version? we never know what your people are going to do next. The AICPA has become a retail organization selling documents and Cont. Education.

3. why does the accounting profession let the Govt. push us around? No one else can do their work.

4. I suggest that your technical people go work for a living to see what is involved.

Joe Scanavolo - C.F.A.
430 Main St
Johnstown Pa 15901

Instructions for Response Form

This response form may be used for comments or suggestions relating to any aspect of the exposure draft that is of concern or interest to you. For convenience, the most significant points have been identified in the summary that accompanies this exposure draft. Return this response form to the address indicated on the reverse side by the comment date.

CUT ALONG LINE



STATE OF COLORADO

OFFICE OF STATE AUDITOR
(303) 866-2051
FAX (303) 866-2060

TIMOTHY M. O'BRIEN, C.P.A.
State Auditor

Legislative Services Building
200 East 14th Avenue
Denver, Colorado 80203-2211

June 25, 1991

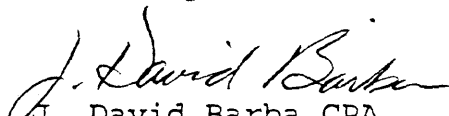
Douglas P. Sauter
Technical Manager
AICPA Auditing
1211 Avenue of the Americas
New York, NY 10036-8775

Dear Mr. Sauter:

Attached is the Colorado State Auditor's comments regarding the exposure draft of changes to SAS #63.

If you have any questions, contact me at (303) 866-2051.

Sincerely,


J. David Barba CPA
Deputy State Auditor

JDB/naf

Enclosure

RC 6/20/91
NY 6/20/91

EXPOSURE DRAFT

File 2353

Proposed Statement on Auditing Standards
Compliance Auditing Applicable to Governmental
Entities and Other Recipients of Governmental
Financial Assistance

April 9, 1991
Comment Date: July 1, 1991

Name and Affiliation: Colorado State Auditor's Office

Comments:

The changes made to SAS #63 to incorporate the issuance of OMB Circular A-133 and the requirement to issue a report on compliance with general grant requirements when no major programs exist appear to be all encompassing. We would offer the following comments on the changes made:

1. We agree with the new requirement to test general grant requirements compliance whenever an A-128 audit is being performed and not just when major grants are involved.
2. The addition, to the compliance reports, of a paragraph which references the audit of the financial statements provides more complete information on the scope of the audit being performed.
3. The addition to footnote #9 on page 10 is difficult to understand. Re-wording of the definition of "federal awards" may help clarify what is considered to be a federal award or financial assistance.

EXPOSURE DRAFT PROPOSED STATEMENT ON AUDITING STANDARDS COMPLIANCE AUDITING APPLICABLE TO GOVERNMENTAL ENTITIES AND OTHER RECIPIENTS OF GOVERNMENTAL FINANCIAL ASSISTANCE

April 9, 1991
Comment date: July 1, 1991

Name and Affiliation: MACPA Auditing Standards Committee

Comments: The members of the committee focused on the auditor's ability and appropriateness of testing for completeness of the nonfinancial aspects of Federal laws and regulations.

Some members expressed concern that cpa's are being asked to be "watch dogs" for the government. They feel that we should only be responsible for reporting on the financial aspects of these engagements.

Respectively submitted,
Kathryn M. HOWard, Chairman

Instructions for Response Form

This response form may be used for comments or suggestions relating to any aspect of the exposure draft that is of concern or interest to you. For convenience, the most significant points have been identified in the summary that accompanies this exposure draft. Return this response form to the address indicated on the reverse side by the comment date.

June 27, 1991

Mr. Douglas P. Sauter
Technical Manager
American Institute of Certified
Public Accountants
Auditing Standards Division
1211 Avenue of the Americas
New York, NY 10036-8775

Dear Mr. Sauter:

We are pleased to submit our comments on the exposure draft, Compliance Auditing Applicable to Governmental Entities and Other Recipients of Governmental Financial Assistance. We support the issuance of this statement, and offer the following suggestions:

Paragraph 15

In addition to the laws and regulations that the exposure draft has listed, OMB Circular A-133 also deals with Financial Reports and Other Special Tests and Conditions. We suggest these be included in the list.

Paragraph 48

We believe the fourth sentence implies that the auditor must perform test of controls over compliance with general requirements. Based on our understanding of OMB Circular A-128 and A-133 this is not the case. We suggest the following:

"If the government being audited has no major programs, the auditor should consider whether his or her tests of controls, **if any**, over compliance with general requirements provide evidence that would also support a report on compliance."

Paragraph 80

In the first paragraph of the sample report in paragraph 80, the references to "claims for advances and reimbursements" and "amounts claimed or used for matching" have been deleted. We believe that paragraphs 58 and 59 requires the independent auditor to report on compliance with these requirements and suggest the reference remain in the sample report.

Appendix A

We suggest the following addition to the third performed procedure:

"Obtain an understanding, **perform tests of controls** and assess control risk of the internal control structure over federal financial assistance.

If you have any questions regarding our comments, please contact James S. Gerson (212-536-2243) or A.J. Lorie (212-536-2119) in our National office.

Very truly yours,

Coopers + Lybrand

(32)



Office of State Auditor

ROBERT V. GRAHAM
STATE AUDITOR

JACK HEINRICH
ASSISTANT STATE AUDITOR

LEGISLATIVE BUILDING AS-21
OLYMPIA, WASHINGTON 98504-0421
(206) 753-5277

June 26, 1991

6379
472

Mr Douglas P. Sauter, Technical Manager
AICPA Auditing Standards Division, File 2353
AICPA
1211 Avenue of the Americas
New York, New York 10036-8775

AICPA
TEXT PROCESSING DEPT.
91 JUL -2 AM 9:17

Dear Mr Sauter:

Thank you for the opportunity to respond to the exposure draft (ED) Compliance Auditing Applicable To Governmental Entities And Other Recipients Of Governmental Financial Assistance. The Committee responsible for the ED is to be commended for their perseverance in promulgating reasonable standards in an environment dominated by capricious Federal Interpretation. While I agree with the substance of the proposed standard, the following comments are submitted for consideration by the Committee.

Item 1.

Title of the Proposed Standard - The purpose of SAS 63 as originally issued was to satisfy the recommendation of the Steinberg Committee for a SAS on compliance auditing. As written, that SAS was a compendium of existing guidance of what was required in the audit of a governmental unit receiving federal financial assistance. Revision of said standard is attributable to changes in the audit requirements and expectations of the Federal community. Therefore I propose the title of the proposed standard be changed to read, "Compliance Auditing Applicable To Governmental Entities And Other Recipients Of Federal Financial Assistance".

Item 2.

Compliance Reporting-General Requirements (para 45-51) - It would appear that the Committee has agreed to promulgate a standard which will satisfy Federal expectations, rather than issue a standard which is consistent with legislative intent of the Single Audit Act of 1984. This is not meant as a criticism of the Committee, however failure to reconcile the intent with practice may cause confusion to the practitioner. Appendix F of SAS 63 was consistent with former requirements and legislative intent. While the requirements contained within the revised compliance supplement renders the prior SAS 63 guidance obsolete in respect to federal requirements, the prior guidance is still consistent with the legislated intent.

Senator Durenburger's remarks about the Single Audit Act to the Senate on October 3, 1984 can be found on pages S13286-13289 of the Congressional Record. Herein we find that the legislated intent of general compliance requirement testing would be limited to those audits wherein noncompliance would "negatively impact the overall financial position of the government" or "... have a material effect upon each major Federal assistance program".

Be that as it may, the new compliance supplement requires testing of these requirements in all single audits whether or not the government has any major programs (para 45). Unfortunately, the guidance contained within para 47 regarding the scope of compliance testing applicable to the general requirements is wholly inadequate. I recognize that by stating this, others may accuse me of hypocrisy, insofar as the same congressional record I cite contains the exact same wording as para 47 regarding the use of professional judgement in determining the extent of procedures for testing compliance. However, I believe the Committee has a responsibility to provide practical guidance in this area. In the absence of general guidelines we will continue to see audits rejected as inadequate based on the whim of a federal reviewer's "rule of thumb". When I speak to people such as Bert Edwards and Harold Monk I have been given wonderful advice as to what the current expectation is, however without this being documented, the sufficiency of an auditor's procedures will always be subject to challenge.

Before I move on to another topic allow to reinforce my overall objection to this section by quoting from the congressional record:

"...we believe that no specific testing should be conducted on a pool of non-major programs and certainly that no Federal policy or regulation should be crafted as such to require State and local government testing of these programs...This is a very important point to understand, Mr President, because a misunderstanding of this paragraph could result in an undue amount of work for State and local governments... The auditor would not test for general compliance with civil rights, Davis-Bacon, or other so-called cross-cutting provisions".

Item 3

Report Wording (para 51) - I agree with the proposal to delete from the final paragraph of the compliance report (s) the word "restriction". My observation herein is that this same change should probably be affected for the reports on internal controls contained in SOP 90-9.

Item 4

Footnote 28 page 22 - The "old" compliance supplement was considered to be a safe harbor under the OMB Q & A of Nov. 87 publication. It is my understanding the new supplement is not to be considered a safe harbor. If my understanding is accurate, this footnote should be deleted.

page 3

Item 5

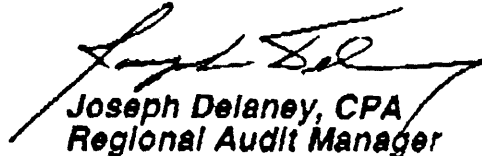
Footnote 32 and Appendix C - Both the flowchart in Appendix C (pg 36) and footnote 32 (pg 29) are an area of potential confusion for a practitioner when evaluated against the guidance contained in the publication State and Local Governmental Developments - 1990. On page 11 of said publication there is guidance on reporting on compliance with laws and regulations in a nonmajor program environment. That information contradicts both of the references cited above for the proposed standard. Furthermore, it is my understanding that in a nonmajor program environment, submission of a single audit report without a report on nonmajor programs will be grounds for the Federal community to reject the report. I would request that the Committee provide additional clarification of this area or delete footnote 32 and modify the flowchart in Appendix C.

Item 6

Para 95 (b) - The reporting of immaterial findings has always been a source of irritation to auditors who conduct A-128 audits. A-133 eliminated this requirement for associated audits. My only comment regarding this is what purpose is served by management being required to report the immaterial compliance to the appropriate federal agency? Is this to suggest that the federal agency (s) are still going to pursue immaterial items? What is the benefit to the taxpayer?

Once again, thank you for the opportunity to respond to this ED. If you have any questions regarding my response, I may be contacted at (509) 456 2700.

Respectfully submitted,


**Joseph Delaney, CPA
Regional Audit Manager**



STATE OF MICHIGAN
OFFICE OF THE AUDITOR GENERAL
201 N. WASHINGTON SQUARE
LANSING, MICHIGAN 48913
(517) 334-8050
FAX (517) 334-8079

33

THOMAS H. MCTAVISH, C.P.A.
AUDITOR GENERAL

June 25, 1991

Mr. Douglas P. Sauter, Technical Manager
Auditing Standards Division, File 2353
American Institute of Certified Public Accountants
1211 Avenue of the Americas
New York, New York 10036-8775

Dear Mr. Sauter:

We have reviewed the Exposure Draft of the proposed Statement on Auditing Standards, entitled Compliance Auditing Applicable to Governmental Entities and Other Recipients of Governmental Financial Assistance, dated April 9, 1991, and submit the following comments for consideration by the Auditing Standards Board. Although some are more significant than others, we have presented our comments in paragraph and page-number sequence to simplify your review process.

1. Paragraph 23a. on Page 12 (as well as Paragraphs 39a., 50a., 79a., and 88a.) states that the auditor's report on compliance shall include a reference to the auditor's report on the financial statements, "...including a description of any departure from the standard report." The term 'description' is ambiguous and may be interpreted by the reader in many different ways. Therefore, we suggest that the final Statement clearly indicate that the description to be included in the auditor's report on compliance is intended to be a summary or paraphrased version of the departure, not the departure repeated verbatim from the auditor's report on the financial statements.
2. Paragraph 23f. on Page 12 states that a basic element of the auditor's report expressing positive and negative assurance on compliance is "...a disclaimer of opinion on compliance with laws, regulations, contracts, and grants." There is currently some confusion in the profession whether the term 'contracts' refers broadly to all contracts (including vendor contracts for custodial services, office rental, etc.) or specifically to federal contracts. Within the context of the proposed Statement, we interpret the term to refer only to federal contracts. Therefore, for purposes of clarity, we suggest that the term "federal contracts" be used consistently throughout the document.



Office of State Auditor

ROBERT V. GRAHAM
STATE AUDITOR

JACK HEINRICHER
ASSISTANT STATE AUDITOR

LEGISLATIVE BUILDING AS-21
OLYMPIA, WASHINGTON 98504-0421
(206) 753-5277

June 26, 1991

Mr Douglas P. Sauter, Technical Manager
AICPA Auditing Standards Division, File 2353
AICPA
1211 Avenue of the Americas
New York, New York 10036-8775

Dear Mr Sauter:

Thank you for the opportunity to respond to the exposure draft (ED) Compliance Auditing Applicable To Governmental Entities And Other Recipients Of Governmental Financial Assistance. The Committee responsible for the ED is to be commended for their perseverance in promulgating reasonable standards in an environment dominated by capricious Federal interpretation. While I agree with the substance of the proposed standard, the following comments are submitted for consideration by the Committee.

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Senator Durenburger's remarks about the Single Audit Act to the Senate on October 3, 1984 can be found on pages S13286-13289 of the Congressional Record. Herein we find that the legislated intent of general compliance requirement testing would be limited to those audits wherein noncompliance would "negatively impact the overall financial position of the government" or "... have a material effect upon each major Federal assistance program".

Be that as it may, the new compliance supplement requires testing of these requirements in all single audits whether or not the government has any major programs (para 45). Unfortunately, the guidance contained within para 47 regarding the scope of compliance testing applicable to the general requirements is wholly inadequate. I recognize that by stating this, others may accuse me of hypocrisy, insofar as the same congressional record I cite contains the exact same wording as para 47 regarding the use of professional judgement in determining the extent of procedures for testing compliance. However, I believe the Committee has a responsibility to provide practical guidance in this area. In the absence of general guidelines we will continue to see audits rejected as inadequate based on the whim of a federal reviewer's "rule of thumb". When I speak to people such as Bert Edwards and Harold Monk I have been given wonderful advise as to what the current expectation is, however without this being documented, the sufficiency of an auditor's procedures will always be subject to challenge.

Before I move on to another topic allow to reinforce my overall objection to this section by quoting from the congressional record:

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page 3

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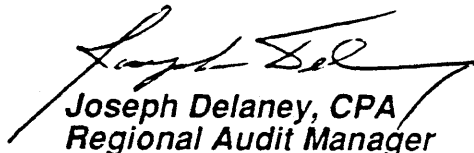
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Once again, thank you for the opportunity to respond to this ED. If you have any questions regarding my response, I may be contacted at (509) 456 2700.

Respectfully submitted,


**Joseph Delaney, CPA
Regional Audit Manager**

Office of the Legislative Auditor



STATE CAPITOL
HELENA, MONTANA 59620
406/444-3122

DEPUTY LEGISLATIVE AUDITORS:

- MARY BRYSON
Operations and EDP Audit
- JAMES GILLET
Financial-Compliance Audit
- JIM PELLEGRINI
Performance Audit

LEGISLATIVE AUDITOR:
SCOTT A. SEACAT

LEGAL COUNSEL:
JOHN W. NORTHEY

July 3, 1991

Douglas P. Sauter, Technical Manager
AICPA Auditing Standards Division, File 2353
AICPA
1211 Avenue of the Americas
New York, N.Y. 10036-8775

Dear Mr. Sauter:

Thank you for the opportunity to respond to the Proposed Statement on Auditing Standards, "Compliance Auditing Applicable to Governmental Entities and Other Recipients of Governmental Financial Assistance." We have reviewed the exposure draft and have summarized our comments as follows.

Paragraph 1, line 3: The sentence structure would be more correct as ". . . Single Audit Act of 1984; Office of Management and Budget (OMB) Circular A-128. . . ." As currently written, OMB Circular A-133 is placed at a higher level of authority than OMB Circular A-128. We do not believe this to be the case.

Paragraph 1.c and 1.d: Paragraph 1.c refers to "federal financial assistance programs" and paragraph 1.d refers to "federal award programs." The terminology should be consistent between the two to prevent misunderstanding.

Paragraph 23.f: We do not believe a "disclaimer of opinion on compliance with laws, regulations, contracts, and grants" is necessary in a non-opinion report. The current report language makes it clear the auditor is not opining.

Paragraph 25: We question the propriety of the phrase "In rare circumstances" as we do not believe the AICPA Auditing Standards Board has the knowledge of whether this occurs or should occur rarely. How does the auditor decide whether the current circumstance falls into the "rare" category. In addition, we do not believe the word "any" is needed in the first sentence.

Paragraphs 45-51: This section, as revised, may add audit work to address the General Requirements over nonmajor programs. However, this is a potential gap in audit coverage that should probably be addressed. The first sentence in

paragraph 45 states there are nine general requirements. This is obvious with the listing in paragraph 46; therefore, the word "nine" is unnecessary.

Paragraph 48: The portion of the first sentence, ". . .regardless of whether the government being audited has major programs" is unnecessary as the requirement is to issue a report on compliance. The second sentence, regarding professional judgment is unnecessary as this is assumed to always be true. Deleting these two items will require editing the balance of the paragraph to make it flow.

Paragraph 80: The deleted items are helpful as reminders of what is necessary for the report. We would suggest these be included within the brackets as examples. For example: ". . .[list requirements tested--types of services allowed or unallowed; eligibility; matching, level of effort, or earmarking; reporting; special tests and provisions; claims for advances and reimbursements; and amounts claimed or used for matching]. . ."

Paragraph 86: Deleting ". . .the auditor need not address the general requirements or the specific requirements that apply to the program as a whole, such as matching and reporting requirements" removes guidance on the extent of testing of nonmajor programs. Paragraph 87 provides some guidance, but auditors may believe they are now supposed to complete testing at the program level.


Paragraph 92: This paragraph should make it clear to auditors that they have the option to perform a Single Audit in accordance with OMB Circular A-128 in lieu of OMB Circular A-133.

Paragraph 93: This paragraph does not address testing and reporting on compliance with nonmajor programs. See paragraph 43.d.

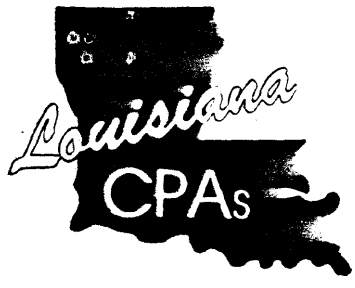
Glossary: The categories within the definition of "Specific requirements do not include "cost allocation" or "monitoring subrecipients." The definition should include all categories to be complete and to avoid misunderstanding.

The format of the exposure draft was helpful in analyzing the proposed changes to SAS No. 63. Please contact us at (406) 444-3122 if you have any questions or need further information.

Sincerely,



Vickie Rauser
Senior Auditor



June 28, 1991

Mr. Douglas P. Sauter, Technical Manager
AICPA Auditing Standards Division, File 2371
AICPA, 1211 Avenue of the Americas
New York, New York 10036-8775

BOARD OF DIRECTORS

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Executive Director
Barry C. Melancon

Dear Mr. Sauter:

The Society of Louisiana Certified Public Accountants appreciates the opportunity to comment on the exposure draft entitled Proposed Statement on Auditing Standards - Compliance Auditing Applicable to Governmental Entities and Other Recipients of Governmental Financial Assistance dated April 9, 1991.

The exposure draft, as written, is acceptable except for the following comments received from members of the Committee.

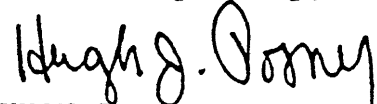
1. It would appear as if the exposure draft would mandate additional compliance auditing for those institutions receiving at least \$25,000 per year but less than \$100,000 per year from the federal government. These additional requirements could make it unnecessarily costly for those institutions receiving at least \$25,000 but less than \$100,000 in federal assistance.
2. Page 17, Section 40, last sentence - The sentence is confusing and probably grammatically incorrect. It is vague as to what "this" refers. I suggest that the last sentence be changed to read, "However, this report is a matter of public record and its distribution is not limited."
3. Page 18, Section 43b, first line - Change "over" to "governing." (The suggested change results in clearer communication and, further, agrees with the wording in the second paragraph of the report example on page 26, section 80.)

**Society of Louisiana
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Mr. Douglas P. Sauter, Technical Manager
June 28, 1991
Page 2

4. Paragraph 1 establishes the scope of this proposed SAS, and includes guidance on reporting on the internal control structure under Government Auditing Standards. However, there is no guidance on reporting on the internal control structure applicable to federal financial assistance, although this report is required by Circular A-128 and A-133. I believe this proposed statement is incomplete without such guidance; this proposed statement should uniformly address all the auditing and reporting requirements imposed by the receipt of governmental financial assistance. Most of this guidance could be lifted from SOP 90-9.

Yours very truly,



HUGH J. POSNER, CHAIRMAN
ACCOUNTING & AUDITING
STANDARDS COMMITTEE

HJP/ebc
Enclosure

cc: Edward Conway

July 8, 1991

Auditing Standards Board
American Institute of Certified Public Accountants
1211 Avenue of the Americas
New York, New York 10036-8775

Compliance Auditing Applicable to Governmental Entities
and Other Recipients of Governmental Financial Assistance

Ernst & Young supports the above-captioned proposed statement. We believe the proposed statement provides appropriate updated guidance to auditors about testing and reporting on compliance with applicable laws and regulations in engagements performed in accordance with GAAS, Government Auditing Standards, the Single Audit Act of 1984 and OMB Circular A-128, *Audits of State and Local Governments*, and OMB Circular A-133, *Audits of Institutions of Higher Education and Other Nonprofit Institutions*. Specifically, the proposed requirement to issue a report on the "general requirements" in all audits conducted in accordance with Circular A-128 and Circular A-133 gives recognition to the reporting being requested in practice by agencies providing federal financial assistance.

Very truly yours,





STATE AUDITOR OF MISSOURI
JEFFERSON CITY, MISSOURI 65102

MARGARET KELLY, CPA
STATE AUDITOR

(314) 751-4824

July 3, 1991

Mr. Douglas P. Sauter
Technical Manager
Auditing Standards Division, File 2353
American Institute of Certified
Public Accountants
1211 Avenue of the Americas
New York, New York 10036-8775

Dear Mr. Sauter:

Enclosed are our comments on the AICPA's exposure draft of a proposed Statement on Auditing Standards, "Compliance Auditing Applicable to Governmental Entities and Other Recipients of Governmental Financial Assistance."

If you have any questions regarding our comments, please contact Myrana Gibler, Audit Manager, of my staff at (314) 751-4213.

Sincerely,

Margaret Kelly, CPA
State Auditor

Enclosures

**COMMENTS - AICPA EXPOSURE DRAFT
PROPOSED STATEMENT ON AUDITING STANDARDS
"COMPLIANCE AUDITING APPLICABLE TO GOVERNMENTAL ENTITIES
AND OTHER RECIPIENTS OF GOVERNMENTAL FINANCIAL ASSISTANCE"**

The Missouri State Auditor's Office appreciates the opportunity to comment on the AICPA exposure draft.

We believe a number of the changes in the draft are desirable, for example:

1. The addition of paragraphs 3 and 4 to provide guidance on the auditor's responsibility when, during an audit in accordance with generally accepted auditing standards, the auditor becomes aware that the entity is subject to an audit requirement not encompassed by the terms of the engagement - These paragraphs appear to be consistent with the AICPA's efforts in recent documents to clearly distinguish between management and auditor responsibilities.
2. The modification of paragraphs 45-51 to require a report on compliance with the general requirements whether or not an entity has major federal financial assistance (FFA) programs - This approach is reasonable since general compliance requirements such as political activity, civil rights, and allowable costs/cost principles apply to numerous programs (major or nonmajor).

Also, in many instances, the tests of compliance with the general requirements are closely related to the tests the auditor performs to evaluate the effectiveness of control structure policies and procedures designed to ensure compliance with those requirements. Under Statement of Position (SOP) 90-9, "The Auditor's Consideration of the Internal Control Structure Used in Administering Federal Financial Assistance Programs Under the Single Audit Act," the auditor is required to test controls applicable to specific and general requirements for all major programs, or if major programs represent less than 50 percent of total FFA expenditures, for the largest major and/or nonmajor programs until at least 50 percent of total FFA expenditures are subject to tests of controls.

3. The addition of guidance regarding audit responsibilities under OMB Circular A-133 in paragraphs 92-95 - Since guidance for audits of educational institutions and other nonprofit organizations that receive FFA has long been lacking, we believe that paragraphs 92-95 provide an acceptable starting point for such guidance and look forward to the more detailed information to be provided in a forthcoming AICPA SOP.

However, during our review of the document, we also noted areas which we believe could be improved or clarified. Our comments on specific items follow.

Options for Reports Expressing Positive and Negative Assurance

Three of the reports discussed in the exposure draft include statements of positive and negative assurance:

1. The report required under Government Auditing Standards for tests of compliance with laws and regulations performed as part of the financial statement audit (paragraphs 23-27).
2. The report on tests of compliance with general requirements for audits of FFA under OMB Circular A-128 (paragraphs 49-51).
3. The report on tests of compliance with specific requirements applicable to nonmajor FFA programs under OMB Circular A-128 (paragraphs 88-89).

For each report, an example is provided to illustrate the statements of positive and negative assurance. Also, for the first report, paragraph 26 lists the requirements for a report in which the statement of positive assurance is qualified for material instances of noncompliance, and paragraph 27 includes an example of such a report. Footnote 13 to paragraph 26 further notes that the auditor is not precluded from issuing an adverse report on compliance but does not illustrate this type of report.

We believe the exposure draft's guidance for the report on compliance required under Government Auditing Standards should be expanded:

1. To include an example of the adverse report referred to in footnote 13.
2. To recognize that the extent of noncompliance noted in tested items may preclude the auditor from expressing negative assurance on untested items and to illustrate the required reporting language.

We also suggest the exposure draft paragraphs for the two federal compliance reports referred to above be revised to recognize additional reporting options: a qualified or an adverse report or the inability to give negative assurance on untested items.¹ If all these options were adequately discussed and illustrated in the paragraphs for the report on compliance under Government Auditing Standards, the paragraphs for the two federal compliance reports could simply refer to the guidance provided earlier in the document.

¹ The inability to give negative assurance was recognized in examples 17 and 18 of the 1986 revised AICPA audit and accounting guide, Audits of State and Local Governmental Units. Although the situation continues to be encountered, however, the suggested reporting language for this option was not included in either current AU Section 801 or SOP 89-6, "Auditors' Reports in Audits of State and Local Governmental Units."

References to the Report on the Financial Statements

Paragraphs 23, 27, 39, 50, 79, and 88

Under current AU Section 801 requirements, the various compliance and internal control reports begin with a statement that the auditor has audited the financial statements and a reference to the auditor's report on those statements. The exposure draft has modified this requirement to indicate that any departure from the standard report should be described. We have several concerns regarding the AICPA's addition of this requirement:

1. The exposure draft does not provide an example of an appropriate description or clarify how the description relates to the following statement in paragraph 27 regarding the report on compliance with laws and regulations required under Government Auditing Standards:

The auditor may wish to include a statement about whether the misstatements resulting from the material instances of noncompliance have been corrected in the financial statements or a **statement describing the effect of such misstatements on his or her report on the basic financial statements.** [emphasis added]

The example report in paragraph 27 includes these statements in paragraphs after the initial paragraph referring to the financial statement audit. However, if the misstatements resulting from material noncompliance require a departure from the standard report on the financial statements, the auditor would appear to be describing the same situation in both the initial paragraph and subsequent paragraphs of the report on compliance.

2. The requirement is inconsistent with internal control reporting requirements for single audits of FFA in the AICPA's recently issued SOP 90-9. Paragraph 16.a. of the SOP indicates that the report is to begin with a reference to the auditor's report on the financial statements but does not require departures from the standard report to be described.
3. For an audit of a governmental entity, the auditor may issue all required reports together (e.g., in a single bound document). In this situation, describing departures from the auditor's standard report on the financial statements in the reports on compliance and internal control would appear to be unnecessary since the reader has the former report available when he/she reviews the latter reports.

Reporting on Compliance with Specific Requirements - Major Programs

Paragraphs 84-85

These paragraphs lack sufficient guidance to assist the auditor in deciding whether a qualified opinion or an adverse opinion is necessary when instances of noncompliance are noted. We suggest the AICPA include in

3. The revision in the first sentence of Paragraph 45 on Page 18 replaced the word 'supplements' with the word 'implements' in the phrase "The OMB's Compliance Supplement for Single Audits of State and Local Governments, which implements OMB Circular A-128, identifies nine 'general requirements' that..." We assume that the revision was made to reduce redundancy ('Supplement' and 'supplements'); however, we believe the revision is technically incorrect because the Compliance Supplement does not implement OMB Circular A-128. Therefore, we suggest either deleting the phrase "which implements OMB Circular A-128" in its entirety, or replacing the word 'implements' with either 'complements', 'clarifies', 'explains', or 'enhances'.
4. Paragraph 51 on Page 20 illustrates an example of a report on compliance with the general requirements. Although the first paragraph of the example refers to the financial statement audit and materiality is implicitly established at that level, we believe that the subsequent use of the term 'material' in the fourth paragraph, which is not explicitly referenced to the financial statements, may be ambiguous and potentially misleading to the reader. Therefore, we suggest that the second paragraph of the example be revised to read "We have applied procedures to test (name of entity)'s compliance with the following requirements applicable to its federal financial assistance programs, which are identified in the schedule of federal financial assistance, noncompliance with which could have a material effect on the financial statements, for the year ended June 30, 19X1. (List the general requirements tested)."
5. Paragraphs 62-72 on Pages 23 and 24 discuss the concepts of audit risk and Paragraphs 90-91 on Pages 30 and 31 discuss management's written representations. The AICPA has previously issued extensive guidance on these two topics in Statements on Auditing Standards No. 47, entitled Audit Risk and Materiality in Conducting an Audit, and No. 19, entitled Client Representations, respectively. Therefore, to provide further guidance to the auditor, we suggest that Paragraphs 62-72 and 90-91 include appropriate footnote references to those respective Statements on Auditing Standards, similar in content to Footnote No. 21 on Page 19 of the Exposure Draft.
6. Paragraph 79k. on Page 26 states that a basic element of the auditor's report on compliance with specific requirements is "a statement that the report is intended for the information of the audit committee, management, and specific legislative or regulatory bodies, but that this is not intended to limit the distribution of the report, if a matter of public record." We believe that this language is inappropriate, particularly in a report prepared by a governmental auditor, and may in fact confuse the reader. In Michigan, for

example, the Office of the Auditor General has constitutional audit authority and all audit reports are available to the public. Therefore, we suggest that Paragraph 79k. be deleted, or made an optional requirement, in the final Statement.

7. Paragraphs 81-85 on Pages 26 to 28 discuss certain situations, such as a scope limitation, the inability to obtain sufficient competent evidential matter, or an inadequacy in the accounting records, in which the auditor may be required to qualify the opinion or to disclaim an opinion on compliance. However, this guidance does not alert the auditor that these situations may also affect the opinion on the financial statements. We suggest that a sentence be added at the end of Paragraph 81, similar in nature to the second sentence of Paragraph 91 on Page 31, such as "Further, the auditor should consider the effects of these situations on his or her ability to express an unqualified opinion on the financial statements."

Further, we believe that the narrative preceding the examples of auditor's opinions in Paragraphs 81-85 should also clearly indicate that, if the auditor disclaimed an opinion on the financial statements, the first paragraph of the compliance opinion would not be the same ("We were engaged to audit" rather than "We have audited") as illustrated in Paragraph 80.

8. Paragraph 89 on Page 29 states that the report on the results of the tests of compliance with requirements applicable to nonmajor federal financial assistance program transactions may be combined with the report on compliance for major federal financial assistance programs. However, the Exposure Draft does not include an example of the combined report. To avoid confusion, inefficiency, and potential inconsistency within the profession, we suggest that the final Statement include an example of the combined report mentioned in Paragraph 89.
9. Because the word 'major' was deleted, the first sentence of Paragraph 90 on Page 30 currently concludes with the phrase "...that, if not complied with, could have a material effect on a federal financial assistance program." We believe that this revision unintentionally reduces the threshold of materiality to the potentially unacceptable level of the smallest program. Therefore, we suggest that the Board reinstate the word 'major' or revise the phrase to read "...that, if not complied with, could have a material effect on federal financial assistance."
10. Paragraph 90g. on Page 30, as currently written, implies that it is management's responsibility to enforce subrecipient compliance with applicable laws and regulations. We interpret management's responsibility to monitor

and inform subrecipients, but not to enforce compliance. Therefore, we suggest that Paragraph 90g. be revised to read "Management has monitored subrecipients to determine whether the subrecipients expended financial assistance in accordance with applicable laws and regulations and whether the subrecipients have met the requirements of OMB Circular A-128, OMB Circular A-133, or OMB Circular A-110, 'Uniform Requirements for Grants to Universities, Hospitals, and Other Nonprofit Organizations,' whichever is applicable."

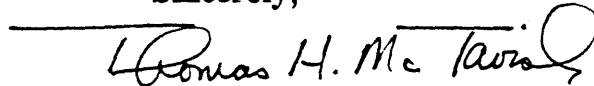
11. The last sentence of Paragraph 96 on Pages 31 and 32 states that "...the auditor should obtain an understanding of the audit requirements for that particular program either from the agreement with the grantor agency, from an audit guide published by the grantor agency, or through contact with the grantor agency." Because the auditor should be encouraged to obtain a complete understanding of the audit requirements from as many sources as may be necessary, we suggest that this sentence be revised to read "...the auditor should obtain an understanding of the audit requirements for that particular program from the agreement with the grantor agency, from an audit guide published by the grantor agency, and/or through contact with the grantor agency."
12. As the proposed Statement is currently formatted, Paragraph 100 on Page 32 appears to relate only to the topics in Paragraphs 98-99. Because the auditor may want to also consider including the audit requirements for a program-specific audit (as discussed in Paragraphs 96-97) in a proposal, contract, or engagement letter, we suggest that the guidance in Paragraph 100 be expanded to also encompass the topics in Paragraphs 96-97.
13. Paragraph 101 on Page 32 establishes audits for fiscal periods ending after December 15, 1991, as the effective date and concludes with the sentence "Early application of this Statement is permissible." Because the Board has indicated that the revisions in this document were principally based on recent developments that have already occurred within the government accounting and auditing community, such as the issuance of OMB Circular A-133, we strongly suggest that the last sentence of Paragraph 101 be revised to read "Early application of this Statement is encouraged."
14. Paragraph 102 on Page 32 states that the provisions of Statement on Auditing Standards No. 63 are applicable "...until this Statement is effective or adopted." We find this phrase to be extremely confusing and, unless the proposed Statement is adopted with immediate effect, contradictory. Therefore, consistent with our Comment #13 to encourage early implementation, we suggest that Paragraph 102 be revised to read "...until

Mr. Douglas P. Sauter
Page 5
June 25, 1991

this Statement is effective or early implemented in accordance with Paragraph 101."

We appreciate this opportunity to comment on the proposed Statement on Auditing Standards. Should you have any questions, or desire further details on our comments, please contact me or Jon A. Wise, C.P.A., Director of Professional Practice.

Sincerely,

A handwritten signature in cursive script that reads "Thomas H. McTavish". The signature is written in dark ink and is positioned below a horizontal line.

Thomas H. McTavish, C.P.A.
Auditor General



STATE OF NEW YORK
OFFICE OF THE STATE COMPTROLLER
ALBANY, NEW YORK
12236

EDWARD V. REGAN
STATE COMPTROLLER

June 28, 1991

Douglas P. Sauter
Technical Manager
Auditing Standards Division, File 2353
AICPA
1211 Avenue of the Americas
New York, N.Y. 10036-8775

Dear Mr. Sauter:

We offer the enclosed comments for your consideration on the Proposed Statement on Auditing Standards dated April 9, 1991 entitled: Compliance Auditing Applicable To Governmental Entities And Other Recipients Of Governmental Financial Assistance.

If we can answer any questions or need to expand upon any of the comments enclosed, please feel free to call me at 518-474-4005.

Sincerely,

A handwritten signature in cursive script, appearing to read 'J. Dwight Hadley'.

J. Dwight Hadley
Assistant Deputy Comptroller
for Municipal Affairs

NEW YORK STATE COMPTROLLER'S OFFICE

Comments On

Proposed Statement On Auditing Standards

Compliance Auditing Applicable To
Governmental Entities And Other Recipients
Of Governmental Financial Assistance

Dated April 9, 1991

1. Paragraph 3 of the PSAS appears to place the entire responsibility on management for obtaining audits that satisfy relevant legal, regulatory or contractual requirements. Given the pervasiveness of such requirements in audit of governments, we believe auditors should assume greater responsibility for the adequacy of audit scope PRIOR to accepting an engagement. Accordingly, we suggest the beginning of this paragraph be altered to read as follows:

Although management is responsible for obtaining audits that satisfy relevant legal, regulatory, or contractual requirements, the auditor should inquire of management as to the nature and extent of these requirements before accepting an engagement to perform a GAAS audit. Once an auditor has contracted to perform a GAAS audit, these standards do not require...

2. The wording in Note 3 to paragraph 3 should be modified so that it applies to governmental entities as well as to nongovernmental recipients of financial assistance.

3. The guidance provided in paragraphs 3 and 4 appears incomplete in that it does not address the situation where two or more auditors are engaged to perform different portions of the financial audit. For example, an auditor is engaged to audit the governmental funds of an entity and a second auditor is engaged to audit an entity's enterprise activity. How is each auditor responsible for ensuring the other auditor has been properly engaged or notified?

4. For paragraph 45 to suggest that the Compliance Supplement IMPLEMENTS Circular A-128 is misleading. We suggest the first sentence of this paragraph be revised to state:

To assist in the implementation of Circular A-128, the OMB has issued the Compliance Supplement for Single Audits of State and Local Governments which identifies nine...

5. Paragraph 46 requires clarification to assist the auditor to distinguish between the work required to issue a report on general requirements versus the work performed on the internal control structure. We recommend the following:

- Add a new second sentence which states: "To issue a report on

compliance with the general requirements the auditor should test some transactions for each of the general requirements which are applicable to that government."

- The auditor needs to understand that their test of transactions performed in connection with their evaluation of the internal control structure may not be significant enough to support issuing a report on the general compliance. The current fourth sentence should be amended to read: "If the government... test of the internal control structure used in administrating federal financial assistance programs included a significant number of transactions to provide sufficient evidence..."

6. Paragraph 79k suggest that language be added to the auditors report on compliance for major federal programs to limit the intended audience for this report. Such language may be appropriate in situations where the auditor has not done enough work to render an opinion (e.g., "positive and negative assurance") because such reports could be open to misinterpretation by uninformed parties; although we note that under freedom of information laws, all reports are publicly available and can not be restricted from the public. In the case of major federal assistance programs the auditor has rendered an opinion, therefore in our view, a limitation on the distribution of the report is NOT appropriate.

This comment also affects paragraphs 80, 82, 83, 84, and 85.

7. In paragraph 86, we agree with the deletion at the end of the paragraph. However, to clarify only the specific requirements need to be tested, we recommend the previous sentence be amended to include that word as follows:

"...they should be tested for compliance with the specific requirements that apply..."

8. The changes to the introduction section of paragraph 90 could create the false impression that materiality is judged in terms of EACH federal program, regardless of whether the program is "major." We suggest the language be amended so it states:

"...a material effect on the entity's financial statements or a major federal financial assistance program."

9. Paragraph 95 is incomplete in that it implies there are only two differences between A-128 and A-133 when in fact there are at least six or seven major differences. All the major differences should be summarized in the sub-paragraphs to paragraph 95.

10. Paragraph 95a is potentially misleading because the description of a major federal awards program under OMB Circular A-133 (i.e., "federal expenditures total the larger of 3 percent of total federal funds or \$100,000') neglects to mention that this dollar threshold applies, not only to individual award programs, but also in certain cases to categories of programs. We recommend that paragraph 95a should be amended to reflect

this fact by substituting the language used in the glossary for "major federal award program" found on page 38 of the PSAS.

11. The description of the common rule furnished in the glossary should be incorporated within the text of the PSAS for the benefit of those unfamiliar with the common rule.

12. The effective date for this PSAS in paragraph 101 should be immediately. Most of the changes incorporated into this PSAS are currently in effect when IG's perform their desk or field reviews of single audits. To prevent more substandard audits being identified, the auditors should comply immediately with the guidance incorporated with in this PSAS. At a minimum, early application of this statement should be ENCOURAGED.

ASSOCIATION OF GOVERNMENT ACCOUNTANTS

June 28, 1991

Douglas P. Sauter
Technical Manager
Auditing Standards Division, File 2353
AICPA
1211 Avenue of the Americas
New York, NY 10036-8775

Dear Mr. Sauter:

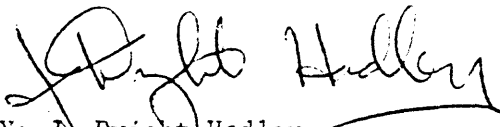
Attached is our response to the April 9, 1991 Proposed Statement on Auditing Standards exposure draft entitled: Compliance Auditing Applicable to Governmental Entities and Other Recipients of Governmental Financial Assistance. This response is submitted on behalf of the Association of Government Accountants (AGA). The AGA represents over 13,000 individuals who have an interest in government accounting and auditing, either as users, preparers or attestors. Our members come from the federal, state and local levels of government and academia.

This response was prepared by the Financial Management Standards Committee which has the primary responsibility for responding to issues that affect government accounting and auditing. Attached is a listing of the members of the Committee.

If you have any questions concerning our response, please address them to me at 208/236-4292 or to J. Dwight Hadley at 518/474-4005.

Respectfully,

Lela (Kitty) D. Pumphrey, Chair
Financial Management Standards Committee


BY: J. Dwight Hadley
Task Force Project Chair

ASSOCIATION of GOVERNMENT ACCOUNTANTS

ASSOCIATION OF GOVERNMENT ACCOUNTANTS
Financial Management Standards Committee
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1990-1991

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Washington, D.C. 20227
202/208-2446

ASSOCIATION OF GOVERNMENT ACCOUNTANTS

Comments On

Proposed Statement On Auditing Standards

Compliance Auditing Applicable To
Governmental Entities And Other Recipients
Of Governmental Financial Assistance

Dated April 9, 1991

1. The wording in Note 3 to paragraph 3 should be modified so that it applies to governmental entities as well as to nongovernmental recipients of Federal financial assistance.

2. The guidance provided in paragraphs 3 and 4 appears incomplete in that it does not address the situation where two or more auditors are engaged to perform an audit of different portions of the financial statements. For example, an auditor is engaged to audit the governmental funds of an entity and a second auditor is engaged to audit an entity's enterprise activity. Or the example where one firm is engaged to audit the financial statements and than one or more different firms are engaged to perform the single audit of the Federal financial assistance programs. How is each auditor responsible for ensuring that all the other auditor(s) have been properly engaged or notified?

3. For paragraph 45 to suggest that the Compliance Supplement IMPLEMENTS Circular A-128 is misleading. We suggest the first sentence of this paragraph be revised to state:

To assist in the implementation of Circular A-128, the OMB has issued the Compliance Supplement for Single Audits of State and Local Governments which identifies nine...

4. Paragraph 48 requires clarification to assist the auditor to distinguish between the work required to issue a report on general requirements versus the work performed on the internal control structure. We recommend the following:

- Add a new second sentence which states: "To issue a report on compliance with the general requirements the auditor should test some transactions for each of the general requirements which are applicable to that government."
- The auditor needs to understand that their test of transactions performed in connection with their evaluation of the internal control structure may not be significant enough to support issuing a report on the general compliance. The current fourth sentence should be amended to read: "If the government... test of the internal control structure used in administering federal financial assistance programs included a significant number of transactions to provide sufficient evidence..."

paragraph 84 guidance modified from AU Section 508.50 which explains considerations affecting the auditor's decision to give a qualified or an adverse opinion on the financial statements due to material departures from generally accepted accounting principles. Presenting such guidance would also be consistent with the procedures followed in paragraph 82 for report modifications due to scope limitations. To assist the auditor in deciding whether to offer a qualified opinion or to disclaim an opinion on compliance due to a scope limitation, paragraph 82 includes guidance modified from AU Section 508.41 for the auditor's report on the financial statements.

Furthermore, in paragraph 85, the example for the adverse opinion on compliance, we suggest the AICPA substitute a pertinent explanatory paragraph for the instruction "[Add a paragraph describing reasons for the adverse opinion]."

References to Specific Compliance Requirements

Paragraphs 79, 80, 82-85, and 88-89

These paragraphs require the auditor to identify in the applicable report on compliance the specific requirements tested for major or nonmajor programs but do not clearly indicate how he/she is to do so. The references to specific requirements such as types of services allowed or not allowed and eligibility that currently appear in the example reports in AU Section 801 have been replaced with the instruction "[list requirements tested]" in the exposure draft examples.

Of particular concern is how this instruction and its predecessor from AU Section 801, "[describe any special tests and provisions]," relate to that category of specific requirements. On single audits of larger governmental entities, the reports will become very lengthy and cumbersome if the auditor is expected to list all special tests and provisions from the OMB Compliance Supplement that were tested for all major or nonmajor programs.

Other Comments

Paragraph 14

Since the requirements for communicating internal control deficiencies differ between SAS No. 60 and Government Auditing Standards, we suggest this paragraph refer to the latter document, as well as SAS No. 60, or to paragraph 32 which summarizes those differences.

Paragraphs 23-29

Paragraph 29 includes a statement that the auditor is to add to the report on compliance required under Government Auditing Standards if nonmaterial instances of noncompliance have been communicated to management in a separate letter. However, the list of report components in paragraph 23 and the report examples in paragraphs 24, 25, and 27 do not refer to this

statement. These paragraphs are inconsistent with paragraphs 39-41 on the report on the internal control structure, which do list or illustrate a similar statement regarding certain control structure matters communicated to management in a separate letter (i.e., paragraph 39.1. and the next to last paragraphs of the reports in paragraphs 40 and 41).

Paragraph 46

We suggest the first parenthetical phrase in item i. be changed to "(in addition to d, f, and g above)" since page 2-9 of the OMB Compliance Supplement refers to cash management (d in paragraph 46) as well as financial reporting and cost principles (f and g, respectively).

Paragraphs 47 and 48

Stating in both paragraphs that the auditor should exercise professional judgment to determine the extent of tests of compliance with the general requirements appears to be unnecessary.

Paragraphs 49 and 50

We suggest paragraphs 49 and 50 be combined since both discuss the report on compliance with the general requirements and paragraph 49 consists only of one sentence. Also, the phrase at the end of paragraph 49, "rather, the auditor issues a report on the results of procedures used to test compliance with the general requirements," is unclear. Regardless of whether the auditor is expressing an opinion on compliance or providing statements of positive and negative assurance, he/she is reporting on the results of the procedures used to test for compliance with applicable requirements (although the nature and extent of those procedures may differ depending on the type of assurance expressed).

Paragraphs 3, 73.a., and 9C.g.

We suggest the references to OMB Circular A-110 be deleted from the body of the paragraphs since the entities to which it applies likely will have been audited under OMB Circular A-133 at least once by the time the final Statement is issued. If necessary, the change in audit requirements from Circular A-110 to Circular A-133 could be addressed in a footnote to the introductory paragraphs of the Statement (e.g., footnote 2 on page 7 of the exposure draft).

Paragraphs 86-88

Unlike the discussions of the other reports on compliance, these paragraphs do not clearly state **before** the list of required report elements the nature of the auditor's assurance to be expressed for compliance with the specific requirements applicable to nonmajor programs (i.e., no opinion on compliance, statements of positive and negative assurance only).

Appendix A

Since the tests of compliance with general requirements applicable to FFA programs and the audit of compliance with specific requirements applicable to major programs represent two distinct sets of procedures as discussed in the exposure draft, we suggest these items be presented as 4. and 5. under "Procedures Performed" instead of being combined under 4. as they currently are. (In the previous version of AU Section 801, combining the procedures under 4. was reasonable since the tests of compliance with the general requirements applied only to major programs.)

In addition to the items discussed above, we have noted several suggested editorial revisions on the enclosed marked draft.

EXPOSURE DRAFT

PROPOSED STATEMENT ON AUDITING STANDARDS

COMPLIANCE AUDITING APPLICABLE TO GOVERNMENTAL ENTITIES AND OTHER RECIPIENTS OF GOVERNMENTAL FINANCIAL ASSISTANCE

APRIL 9, 1991

**Prepared by the AICPA Auditing Standards Board
For comment from persons interested in auditing and reporting**

**Comments should be received by July 1, 1991, and addressed to
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600603

This abbreviation is not used or explained elsewhere in the initial paragraphs.

reasonable assurance that the entity complies with those laws and regulations. As this statement explains, the auditor's responsibility for testing and reporting on compliance with laws and regulations varies according to the terms of the engagement.

X 3. Management is also responsible for obtaining audits that satisfy relevant legal, regulatory, or contractual requirements. Generally accepted auditing standards do not require the auditor to perform procedures beyond those he or she considers necessary to obtain sufficient competent ^{confidential} evidential matter to form a basis for the opinion on the financial statements. Therefore, if during a CAAS audit of the financial statements the auditor becomes aware that the entity is subject to an audit requirement that is not encompassed in the terms of the engagement, the auditor should communicate to management, the audit committee, or others with equivalent authority and responsibility³ that an audit in accordance with generally accepted auditing standards may not satisfy the relevant legal, regulatory, or contractual requirements. For example, the auditor will be required to make this communication if an entity engages an auditor to perform an audit of its financial statements in accordance with generally accepted auditing standards and the auditor becomes aware that by law, regulation, or contractual agreement the entity is also required to have an audit in accordance with one or more of the following:

- Government Auditing Standards, issued by the Comptroller General of the United States
- The Single Audit Act of 1984 and OMB Circular A-128, "Audits of State and Local Governments"
- OMB Circular A-110, "Uniform Requirements for Grants to Higher Education, Hospitals, and Other Nonprofit Organizations"
- OMB Circular A-133, "Audits of Institutions of Higher Education and Other Nonprofit Institutions"
- Other compliance audit requirements, such as state or local laws or program-specific audits under federal audit guides

4. The communication required by paragraph 3 may be oral or written. If the communication is oral, the auditor should document the communication in the working papers. The auditor should consider how the client's actions in response to such communication relate to other aspects of the audit, including the potential effect on the financial statements and on the auditor's report on those financial statements. Specifically, the auditor should consider management's actions (such as not arranging for an audit that meets the applicable requirements) in relation to the guidance in SAS No. 54.

COMPLIANCE AUDITING IN AUDITS CONDUCTED IN ACCORDANCE WITH GENERALLY ACCEPTED AUDITING STANDARDS

5. In an audit performed in accordance with generally accepted auditing standards, the auditor's responsibility for consideration of laws and regulations and how they affect the audit is described in SAS Nos. 54 and 53. SAS No. 54, paragraph 5, equates the auditor's responsibility for detecting misstatements caused by certain illegal acts with the responsibility for other errors and irregularities:

The auditor considers laws and regulations that are generally recognized by auditors to have a direct and material effect on the determination of financial statement amounts However, the auditor considers such laws or regulations from the perspective of their known relation to audit objectives derived from financial statement assertions rather than from the perspective of legality *per se*. The auditor's responsibility to detect and report misstatements resulting from illegal acts having a direct and material effect on the determination of financial statement amounts is the same as that for errors and irregularities as described in SAS No. 53, *The Auditor's Responsibility to Detect and Report Errors and Irregularities*.

6. SAS No. 53, paragraph 5, describes the auditor's responsibility for detecting errors and irregularities as follows:

The auditor should assess the risk that errors and irregularities may cause the financial statements to contain a material misstatement. Based on that assessment, the auditor should design the audit to provide reasonable assurance of detecting errors and irregularities that are material to the financial statements.

7. Thus, the auditor should design the audit to provide reasonable assurance that the financial statements are free of material misstatements resulting from violations of laws and regulations that have a

³For entities that do not have audit committees, the phrase "others with equivalent authority and responsibility" may include the board of directors, the board of trustees, or the owner in owner-managed entities.

regulations that may have a direct and material effect on the determination of amounts in their financial statements. ^{such} laws and regulations may deal with the following matters:

- that items a.-d. are only examples of laws and regulations that may have a material effect on the financial statements.*
- a. *Types of services* ^{These} allowed or not allowed—specifies the types of goods or services entities may purchase with financial assistance ^{such as}
 - b. *Eligibility*—specifies the characteristics of individuals or groups to whom entities may give financial assistance
 - c. *Matching, level of effort, or earmarking*—specifies amounts entities should contribute from their own resources towards projects for which financial assistance is provided
 - d. *Allowable cost/cost principles*—*specifies principles and standards for determining costs* applicable ~~chargeable~~ *to federal financial assistance programs*

16. The auditor's responsibility to detect material misstatements of financial statements resulting from violations of laws and regulations that have a direct and material effect on the determination of financial statement amounts is addressed in paragraphs 5 through 7 of this Statement. In carrying out this responsibility in an audit of the financial statements of a not-for-profit organization or business enterprise that receives financial assistance from a governmental entity, the auditor should apply the guidance in paragraphs 10 through 14 that is relevant to that audit.

Working-Paper Documentation

17. The auditor should document procedures performed to evaluate compliance with laws and regulations that have a direct and material effect on the determination of financial statement amounts in accordance with SAS No. 41, *Working Papers*. The auditor's understanding of the internal control structure as it pertains to compliance with such laws and regulations, as well as the related assessment of control risk, should be documented in accordance with SAS No. 55. (Page 4-6 of *Government Auditing Standards* includes additional working-paper requirements that the auditor should follow when engaged to perform an audit in accordance with those standards.)

Written Representations From Management

18. SAS No. 19, *Client Representations*, requires the auditor to obtain written representations from management as part of an audit conducted in accordance with generally accepted auditing standards. Among the matters ordinarily included in those representations are "violations or possible violations of laws or regulations whose effects should be considered for disclosure in the financial statements or as a basis for recording a loss contingency." In audits to which this Statement applies, auditors should consider obtaining additional representations from management acknowledging that—

- a. Management is responsible for the entity's compliance with laws and regulations applicable to it.
- b. Management has identified and disclosed to the auditor all laws and regulations that have a direct and material effect on the determination of financial statement amounts.

REPORTING UNDER GOVERNMENT AUDITING STANDARDS

19. A governmental entity, not-for-profit organization, or business enterprise may engage an auditor to audit its financial statements in accordance with *Government Auditing Standards*. In performing an audit in accordance with *Government Auditing Standards*, the auditor assumes responsibilities beyond those in an audit in accordance with generally accepted auditing standards to report on compliance with applicable laws and regulations and on the internal control structure.¹⁰

Reporting on Compliance With Applicable Laws and Regulations

20. Paragraph 5 on page 5-2 of *Government Auditing Standards* includes the following requirement to report on compliance with applicable laws and regulations:

The auditors should prepare a written report on their tests of compliance with applicable laws and regulations. This report, which may be included in either the report on the financial audit or a separate

¹⁰Concerning audit follow-up, paragraph 41 on page 3-16 of *Government Auditing Standards* states: "Due professional care also includes follow-up on known findings and recommendations from previous audits that could have an effect on the current audit objectives to determine whether prompt and appropriate corrective actions have been taken by entity officials or other appropriate organizations. . . . The auditor's report should disclose the status of known but uncorrected significant or material findings and recommendations from prior audits that [a]ffect the current audit objective."

We have audited the financial statements of [name of entity] as of and for the year ended June 30, 19X1, and have issued our report thereon dated August 15, 19X1.

We conducted our audit in accordance with generally accepted auditing standards and *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

Compliance with laws, regulations, contracts, and grants applicable to [name of entity] is the responsibility of [name of entity]'s management. As part of obtaining reasonable assurance about whether the financial statements are free of material misstatement, we performed tests of [name of entity]'s compliance with certain provisions of laws, regulations, contracts, and grants. However, ~~our~~ the objective of our audit of the financial statements was not to provide an opinion on overall compliance with such provisions. Accordingly, we do not express such an opinion.

The results of our tests indicate that, with respect to the items tested, [name of entity] complied, in all material respects, with the provisions referred to in the preceding paragraph. With respect to items not tested, nothing came to our attention that caused us to believe that [name of entity] had not complied, in all material respects, with those provisions.

This report is intended for the information of the audit committee, management, and [specify legislative or regulatory body]. This restriction is not intended to limit the distribution of this report, which is a matter of public record.¹²

[Signature]
[Date]

25. In rare circumstances, based on assessments of materiality and audit risk, auditors may decide not to perform any tests of compliance with certain provisions of laws, regulations, contracts, and grants. For example, an auditor may conclude that transactions and balances directly affected by laws and regulations are not material to the financial statements taken as a whole. In such circumstances, *Government Auditing Standards*, in paragraph 6 on page 5-2, states that "the report should contain a statement that the auditor did not test for compliance with laws and regulations." The auditor's report should not include a statement of positive assurance; however, the assessments of materiality and audit risk provide a basis for the auditor to conclude that the likelihood of material instances of noncompliance is low. These assessments are based, in part, on the procedures and considerations presented in paragraphs 10 through 14 of this Statement. Thus, the auditor has a basis for expressing negative assurance about compliance under *Government Auditing Standards*. The following is an illustration of the auditor's report on compliance when, based on assessments of materiality and audit risk, the auditor concluded that it was not necessary to perform tests of compliance with laws and regulations:

[First two paragraphs are the same as in the report illustrated in paragraph 24.]

Compliance with laws, regulations, contracts, and grants applicable to [name of entity] is the responsibility of [name of entity]'s management. As part of our audit, we assessed the risk that noncompliance with certain provisions of laws, regulations, contracts, and grants could cause the financial statements to be materially misstated. We concluded that the risk of such material misstatement was sufficiently low that it was not necessary to perform tests of [name of entity]'s compliance with such provisions of laws, regulations, contracts, and grants.

However, in connection with our audit, nothing came to our attention that caused us to believe that [name of entity] had not complied, in all material respects, with the laws, regulations, contracts, and grants referred to in the preceding paragraph.

[Fifth paragraph, signature, and date are the same as in the report illustrated in paragraph 24.]

X Reporting Noncompliance

X 26. For purposes of this Statement, material instances of noncompliance are failures to follow requirements, or violations of prohibitions, contained in statutes, regulations, contracts, or grants that cause the auditor to conclude that the aggregation of the misstatements (that is, the auditor's best estimate of the total misstatement) resulting from those failures or violations is material to the financial statements. When the auditor's procedures disclose material instances of noncompliance, the auditor should modify the statements of positive and negative assurance included in the report. A qualified report¹³ should include—

a. The definition of material instances of noncompliance.

¹²If the report is not part of the public record, this sentence should not be included in the report.

¹³The auditor is not precluded from issuing an adverse report on compliance.

- b. An identification of material instances of noncompliance noted.¹⁴
- c. A statement that the noncompliance noted was considered in forming an opinion on whether the entity's financial statements are presented fairly, in all material respects, in conformity with generally accepted accounting principles.

27. The auditor should report material instances of noncompliance regardless of whether the resulting misstatements have been corrected in the entity's financial statements. The auditor may wish to include a statement about whether the misstatements resulting from the material instances of noncompliance have been corrected in the financial statements or a statement describing the effect of such misstatements on his or her report on the basic financial statements. The following is an illustration of the auditor's report on compliance when material instances of noncompliance are identified.

Word used in example report, paragraph 24.

[First three paragraphs are the same as in the report illustrated in paragraph 24.]
 Material instances of noncompliance are failures to follow requirements, or violations of prohibitions, contained in ^{aws} statutes, regulations, contracts, or grants that cause us to conclude that the aggregation of the misstatements resulting from those failures or violations is material to the financial statements. The results of our tests of compliance disclosed the following material instances of noncompliance, the effects of which have been corrected in [name of entity]'s 19X1 financial statements.
 [Include paragraphs describing the material instances of noncompliance noted.]

X

Divide into two sentences as in paragraph 24.

We considered these material instances of noncompliance in forming our opinion on whether [name of entity]'s 19X1 financial statements are presented fairly, in all material respects, in conformity with generally accepted accounting principles, and this report does not affect our report dated [date of report] on those financial statements.
 Except as described above, the results of our tests of compliance indicate that, with respect to the items tested, [name of entity] complied, in all material respects, with the provisions referred to in the third paragraph of this report, and with respect to items not tested, nothing came to our attention that caused us to believe that [name of entity] had not complied, in all material respects, with those provisions.
 [Last paragraph, signature, and date are the same as in the report those illustrated in paragraph 24.]

X

28. Page 5-3 of *Government Auditing Standards* includes the following provisions for reporting immaterial instances of noncompliance:

Other nonmaterial instances of noncompliance need not be disclosed in the compliance report but should be reported in a separate communication to the audited entity, preferably in writing. Such instances of noncompliance when communicated in a management letter to top management should be referred to in the report on compliance. All communications should be documented in the working papers.

29. If the auditor has issued a separate letter describing immaterial instances of noncompliance, the report prepared in accordance with paragraphs 23, 25, or 26 of this statement should be modified to include a statement such as the following: "We noted certain immaterial instances of noncompliance that we have reported to the management of [name of entity] in a separate letter dated August 15, 19X1."

Illegal Acts

30. As noted in paragraph 20, *Government Auditing Standards* requires the auditor to report instances or indications of illegal acts that could result in criminal prosecution.* However, the auditor ordinarily does not possess the expertise to form a conclusion about whether an illegal act or possible illegal act could result in criminal prosecution. Thus, in complying with this requirement to report instances or indications of illegal acts that could result in criminal prosecution, the auditor may choose to report all illegal acts or possible illegal acts noted. (See paragraph 15, pages 4-4 and 4-5, of *Government Auditing Standards*, regarding consultation with legal counsel.)

¹⁴Pages 5-3 and 5-4 of *Government Auditing Standards* provide the following guidance on reporting material instances of noncompliance: "[T]he auditors should place their findings in proper perspective. The extent of noncompliance should be related to the number of cases examined to give the reader a basis for judging the prevalence of noncompliance. . . . In presenting the findings, the auditor should follow the report contents standards, as appropriate, for objectives, scope and methodology, audit results, and views of responsible officials, and the report presentation standards, discussed in chapter 7 [of *Government Auditing Standards*]."

*The auditor will have complied with the requirements of *Government Auditing Standards* by designing the audit to consider the possibility of and to detect illegal acts by clients as required by SAS No. 54, *Illegal Acts by Clients*.

31. Paragraphs 13 and 16 in chapter 5 of *Government Auditing Standards* provide guidance on reporting illegal acts:

Public accountants conducting audits of government entities will discharge their responsibilities for reporting illegal acts or indications of such acts found during or in connection with an audit by promptly reporting to the top official of the entity arranging for the audit (including audit committees or others with equivalent authority). The auditor should also consider reporting to the appropriate oversight body. If the audited entity and the top official [are] believed to be [parties] to such acts or otherwise implicated, the auditor should in all cases report to the appropriate oversight body. Also, when the illegal acts involve funds received from other government entities, the audited entity should report to the proper officials, including those at the audit organization of those entities. If the audited entity does not do so within a reasonable time or was unable to because the top official was involved, the auditor should report to the officials of those other government entities.

Illegal acts or indications of such acts that auditors become aware of need not be included in the required audit reports, but may be covered in a separate written report and submitted in accordance with the preceding paragraphs, thus permitting the required report or reports to be released. However, auditors generally should not release information or reports containing information on such acts or reports with references that such acts were omitted from reports, without consulting with appropriate legal counsel, since this release could interfere with legal processes, subject the implicated individuals to undue publicity, or subject the auditor to potential legal action.

Reporting on the Internal Control Structure

32. Consistent with SAS No. 60 the auditor should communicate any reportable conditions noted during the audit; however, reporting on the internal control structure under *Government Auditing Standards* differs from reporting under SAS No. 60.¹⁶ *Government Auditing Standards* requires a written report on the internal control structure in all audits; SAS No. 60 requires communication — oral or written — only when the auditor has noted reportable conditions. *Government Auditing Standards* requires a description of any reportable conditions noted, including the identification of those that are considered to be material weaknesses. SAS No. 60 permits, but does not require, the auditor to separately identify and communicate as material weaknesses those reportable conditions that, in the auditor's judgment, are considered to be material weaknesses. Finally, *Government Auditing Standards* requires communication of the following matters, which are not addressed by SAS No. 60:

- a. Identification of the categories of the internal control structure
- b. Description of the scope of the auditor's work in obtaining an understanding of the internal control structure and in assessing control risk
- c. Description of deficiencies in the internal control structure not considered significant enough to be reportable conditions

33. Paragraphs 34 and 35 of this Statement provide guidance on identifying elements of the internal control structure in the auditor's report, and paragraph 36 addresses reporting the scope of the auditor's work. Paragraphs 37 and 38 address the communication of "nonreportable conditions." Paragraphs 39 through 41 illustrate reports on the internal control structure.

Identifying Controls

34. Paragraph 17 on page 5-6 of *Government Auditing Standards* requires that the auditor's report on internal control structure related matters describe "the entity's significant internal controls or control structure including the controls established to ensure compliance with laws and regulations that have a material impact on the financial statements." *Government Auditing Standards* presents examples of different ways in which the internal control structure might be classified, noting that auditors may modify these examples or use other classifications as appropriate for the particular circumstances on which they are reporting.

35. Several variations are possible in the classifications presented in *Government Auditing Standards*. An entity might classify its transactions into a fewer or greater number of classifications than mentioned in *Government Auditing Standards*. For example, the treasury or financing cycle might be classified as separate investments and debt cycles. For federal agencies, departments, and programs, the purchases/disbursements

¹⁶*Government Auditing Standards* states on page 5-6 that the requirement for a report "does not require any additional audit work other than that required as part of a financial audit . . ."

reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control structure and its operations that we consider to be material weaknesses as defined above.

However, we noted certain matters involving the internal control structure and its operation that we have reported to the management of [name of entity] in a separate letter dated August 15, 19X1.

[Last paragraph of the report is paragraph 40.] ~~signature, and date~~ are the same as that ~~those~~ illustrated in paragraph 40.

Paragraph 40 does not include a signature and date.

RESPONSIBILITIES UNDER THE SINGLE AUDIT ACT

42. The Single Audit Act and OMB Circular A-128, "Audits of State and Local Governments," which the Office of Management and Budget (OMB) issued to prescribe policies, procedures, and guidelines to implement the Act, require state and local governments that receive total federal financial assistance equal to or in excess of \$100,000 in a fiscal year to have an audit performed in accordance with the Single Audit Act. The Single Audit Act states that a state or local government receiving at least \$25,000, but less than \$100,000, of total federal financial assistance in a year has the option of having an audit performed in accordance with either the Act or with federal laws and regulations governing the programs in which the government participates. The Single Audit Act does not require state or local governments receiving less than \$25,000 in total federal financial assistance to have an audit.¹⁷ ~~State and local governments that are primary recipients of federal financial assistance may require not-for-profit organizations that are subrecipients to have audits performed in accordance with the Single Audit Act.~~

Changed paragraph references to be consistent with format in a. and d.

43. The Single Audit Act and OMB Circular A-128 require the auditor to *should test and* report on the following matters pertaining to compliance with laws and regulations:

- a. Compliance with laws and regulations that may have a material effect on the financial statements (see paragraphs 20 through 31 of this Statement*)
- b. Compliance with ~~laws and regulations~~ *general requirements over that may have a material effect on each major federal financial assistance program, as defined by the Single Audit Act (see paragraphs XX through XX; paragraphs XX through XX address the specific requirements and (paragraphs 45 through 51) address the general requirements)* *See*
- c. ~~Compliance with the specific requirements that may have a material effect on each major program, as defined by the Single Audit Act (paragraphs 52 through 85) address the specific requirements;~~ *See*
- d. Compliance with certain laws and regulations applicable to nonmajor federal financial assistance programs (see paragraphs 86 through 89)

"Supplements" is the word used in paragraph 60, as well as the OMB Compliance Supplement.

44. Among the other audit reports required by the Single Audit Act and OMB Circular A-128 are reports on the financial statements,¹⁸ on the supplementary schedule of federal financial assistance, and on internal control structure policies and procedures relevant to federal financial assistance programs.¹⁹ This Statement discusses the relationship between the work auditors do to form a basis for issuing those reports and the work auditors do to support their reports on compliance.

Compliance Auditing—General Requirements

45. The OMB's *Compliance Supplement for Single Audits of State and Local Governments*, which ~~supplements~~ *implements* OMB Circular A-128, identifies ~~six~~ *nine* "general requirements" that "involve *supplements*"

¹⁷Auditors of colleges and other not-for-profit organizations that are not required to follow OMB Circular A-128 should follow applicable OMB guidance. On November 10, 1988, the OMB proposed Circular A-133, "Audits of Institutions of Higher Education and Other Nonprofit Organizations *Institutions*," which is patterned after Circular A-128. *See paragraphs 92 through 95.*

¹⁸The basic elements of the auditor's report described in paragraph 21 should be modified to include a reference that the audit was conducted in accordance with OMB Circular A-128, "Audits of State and Local Governments."

¹⁹If, after the date of the report on the audited financial statements, (a) the auditor performs other procedures as part of a single audit and (b) the results of those procedures indicate that facts may have existed at the date of the report on the audited financial statements that might have affected that report had the auditor then been aware of such facts, the auditor should follow AU section 561, "Subsequent Discovery of Facts Existing at the Date of the Auditor's Report."

²⁰Appendix A to this Statement summarizes the procedures performed and reports issued in a single audit. The appendix includes paragraph references for those matters discussed in this Statement. References to the relevant portions of the AICPA Audit and Accounting Guide *Audits of State and Local Governmental Units* (1986 revised edition) are presented for matters for which guidance is not provided in this Statement *an audit in accordance with the Single Audit Act of 1954 and OMB Circular A-128 or OMB Circular A-133.*

Add brackets to show that words were capitalized in original document.

significant national policy and for which failure to comply could have a material impact on an organization's financial statements ~~and that should including those prepared for federal programs.~~ Accordingly, these compliance requirements shall be included as part of every audit of state, local, and Tribal government that involves [f]ederal financial assistance ~~whether or not the government has a major program.~~ The general requirements may or may not be laws and regulations that have a direct and material effect on the determination of financial statement amounts. Thus, the auditor should evaluate each general requirement based on the circumstances of the engagement to determine whether a particular requirement relates more to laws and regulations, described in SAS No. 54, ~~Illegal Acts by Clients~~, that have an indirect effect on the financial statements than those that have a direct and material effect on the determination of financial statement amounts.

46. These general requirements deal with the following matters:²⁰

- a. *Political activity*—prohibits the use of federal funds for partisan political activity.
- b. *Davis-Bacon Act*—requires that laborers working on federally financed construction projects be paid a wage not less than the prevailing regional wage established by the Secretary of Labor.
- c. *Civil rights*—prohibits violation of anyone's civil rights in a program funded by the federal government.
- d. *Cash management*—requires recipients of federal financial assistance to minimize the time lapsed between receipt and disbursement of that assistance.
- e. *Relocation assistance and real property acquisition*—prescribes how real property should be acquired with federal financial assistance and how recipients must help relocate people displaced when that property is acquired.
- f. *Federal financial reports*—prescribes federal financial reports that must be filed.
- g. *Allowable costs/cost principles*—prescribes the direct and indirect costs allowable for federal reimbursement. *Act* ← *As shown in Compliance Supplement*
- h. *Drug-free Workplace*—prescribes that grantees must certify that they provide a drug-free workplace.
- i. *Administrative requirements*—prescribes administrative requirements (in addition to f and g above) that should be followed (Common Rule).

47. The *Compliance Supplement* suggests procedures for testing compliance with the general requirements. As the *Single Audit Act* and *OMB Circular A-128* has have been implemented, it has become generally accepted that the nature of these procedures is sufficient to satisfy the requirements of the Act with respect to the general requirements. However, the *Compliance Supplement* does not specify the extent of such procedures. The auditor should exercise professional judgment in determining the extent of procedures for testing compliance with the general requirements. and may wish to obtain an understanding with the client about the extent of such procedures. The auditor should consider the guidance on the identification of major federal financial assistance programs and materiality presented in paragraphs XX through XX in testing and reporting on compliance with the general requirements.

48. The auditor should issue a report on compliance with the general requirements regardless of whether the government being audited has major programs. Determining the extent of any tests of compliance with the general requirements is a matter of professional judgment. Among the matters the auditor considers are the extent of any tests of compliance with general requirements performed for major programs. If the government being audited has no major programs, the auditor should consider whether his or her tests of controls over compliance with general requirements provide evidence that would also support a report on compliance. If the tests of controls do not provide sufficient evidence to support a report on compliance, additional testing on the general requirements would need to be performed.²¹

49. This Statement does not require the auditor to issue an opinion on compliance with the general requirements; rather, the auditor issues a report on the results of procedures used to test compliance with the general requirements. However, auditors may choose to express an opinion on compliance with one or more of the general requirements if management's implied assertion about compliance with a

Suggest deleting this phrase; referring to compliance with respect to both internal controls and laws or regulations becomes confusing.

Idea repeated

²⁰The section of the *Compliance Supplement* that discusses the general requirements is reproduced in Appendix D to this statement. Besides describing the general requirements, the *Compliance Supplement* includes references to the *Code of Federal Regulations* or other statutes where additional information about the requirements can be obtained. The auditor should consider referring to this information when planning to test compliance with the general requirements.

²¹Further guidance is provided in *Statement of Position 90-9, The Auditor's Consideration of the Internal Control Structure Used in Administering Federal Financial Assistance Programs Under the Single Audit Act.*

by Circular A-128, we have performed auditing procedures to test compliance with the requirements governing ~~types of service allowed or unallowed, eligibility, and [describe any special tests and provisions]~~ [list requirements tested] that are applicable to those transactions. Our procedures were substantially less in scope than an audit, the objective of which is the expression of an opinion on the City's [name of entity]'s compliance with these requirements. Accordingly, we do not express such an opinion.

With respect to the items tested, the results of those procedures disclosed no material instances of non-compliance with the requirements listed in the preceding paragraph. With respect to items not tested, nothing came to our attention that caused us to believe that the City of Example [name of entity] had not complied, in all material respects, with those requirements. However, the results of our procedures disclosed immaterial instances of noncompliance with those requirements, which are described in the accompanying schedule of findings and questioned costs.⁸⁴

This report is intended for the information of the audit committee, management, and [specify legislative or regulatory body]. This restriction is not intended to limit the distribution of this report, which is a matter of public record.⁸⁵

[Signature]
[Date]

Written Representations From Management

90. The auditor should obtain written representations from management as a part of an audit conducted in accordance with the Single Audit Act of 1984 and OMB Circular A-128 to ~~express an opinion report~~ on compliance with requirements that, if not complied with, could have a material effect on a major federal financial assistance program. The specific written representations obtained by the auditor ordinarily include the following matters:

- a. Management has identified in the schedule of federal financial assistance all assistance provided by federal agencies in the form of grants, contracts, loans, loan guarantees, property, cooperative agreements, interest subsidies, insurance, or direct appropriations.
- b. Management has identified the requirements governing political activity, the ^{acquisition} Davis-Bacon Act, civil rights, cash management, relocation assistance and real property management, federal financial reports, allowable costs/cost principles, drug-free workplace, and administrative requirements over federal financial assistance.
- c. Management has identified the requirements governing types of services allowed or ^{not} unallowed; eligibility; matching, level of effort, or earmarking; reporting; [include any special provisions]; claims for advances and reimbursements; and amounts claimed or used for matching that are applicable to its major federal financial assistance programs, which are identified in the schedule of federal financial assistance. ^{Act}
- d. Management has complied with reporting requirements in connection with federal financial assistance.
- e. Information presented in federal financial reports and claims for advances and reimbursements is supported by the books and records from which the basic financial statements have been prepared.
- f. Amounts claimed or used for matching were determined in accordance with OMB Circular A-87, "Cost Principles for State and Local Governments," and the OMB's *Uniform Administrative Requirements for Grants and Cooperative Agreements to State and Local Governments*.
- g. Management has monitored subrecipients to determine that the subrecipients expend financial assistance in accordance with applicable laws and regulations and have met the requirements of OMB Circular A-128, OMB Circular A-133, or OMB Circular A-110, "Uniform Requirements for Grants to Universities, Hospitals, and Other Nonprofit Organizations," whichever is applicable. ^{audit}
- h. Management has taken appropriate corrective action on a timely basis after receipt of a subrecipient's auditor's report that identifies noncompliance with federal laws and regulations.
- i. Management has considered the results of subrecipients' audits and made any necessary adjustments to the entity's own books and records.
- j. Management has identified and disclosed to the auditor all amounts questioned and known noncompliance with requirements that could have a material effect on a major federal financial assistance program.

⁸⁴If there are no instances of noncompliance, this sentence should be omitted.

⁸⁵See footnote 12.

Changes to make requirements listed agree with those in paragraphs 46 and 57 or the OMB Compliance Supplement

tests and

word used in paragraph 73.a.

91. Management's refusal to furnish written representations constitutes a limitation on the scope of the audit sufficient to require a qualified opinion or disclaimer of opinion on compliance with the specific requirements.⁹⁶ Further, the auditor should consider the effects of management's refusal on his or her ability to rely on other management representations.

RESPONSIBILITIES UNDER OMB CIRCULAR A-133

92. OMB Circular A-133, "Audits of Institutions of Higher Education and Other Nonprofit Institutions," prescribes audit requirements for institutions of higher education and other nonprofit institutions receiving federal awards (either directly or indirectly). Circular A-133 states that nonprofit institutions receiving \$100,000 or more a year in federal awards are to have an audit in accordance with Circular A-133. Nonprofit institutions receiving \$100,000 or more but receiving awards under only one program have the option of having an audit in accordance with the provisions of Circular A-133 or having an audit made of the one program. Nonprofit institutions that receive at least \$25,000 but less than \$100,000 a year in federal awards have the option of having an audit in accordance with Circular A-133 or having an audit made of each federal award. Nonprofit institutions receiving less than \$25,000 a year in federal awards are exempt from federal audit requirements, but records are to be available for review by appropriate officials of the federal grantor agency or subgranting entity.

93. The auditor is to test and report on the following matters pertaining to compliance with laws and regulations:

- a. Compliance with laws and regulations that may have a direct and material effect on the entity's financial statement amounts
- b. Compliance with the general requirements applicable to the federal award programs
- c. Compliance with specific requirements that may have a direct and material effect on each major program, as defined in OMB Circular A-133

94. These reports are similar to those required by the Single Audit Act and OMB Circular A-128; therefore, the guidance in paragraphs 42 through 91 of this Statement is also generally applicable to audits in accordance with OMB Circular A-133. Among the other audit reports required by OMB Circular A-133 are reports on the financial statements, on the supplementary schedule of federal awards, and on the internal control structure policies and procedures relevant to federal awards.

95. However, the Single Audit Act and OMB Circular A-128 differ from OMB Circular A-133 in certain respects, and the auditor should be aware of these differences, which are summarized below.

- a. Major program — OMB Circular A-133 defines a major program as one in which federal expenditures total the larger of 3 percent of total federal funds expended or \$100,000. (Under the Single Audit Act and OMB Circular A-128, a major program is defined as the larger of 3 percent of total federal expenditures or \$300,000.)
- b. Disclosure of immaterial findings — OMB Circular A-133, unlike OMB Circular A-128, does not require the auditor to include a description of immaterial noncompliance in the audit reports. However, immaterial noncompliance is required to be reported in a separate written communication to the institution, which management is required to submit to the appropriate federal agency.

OTHER COMPLIANCE AUDITING RESPONSIBILITIES

Program-Specific Audits

96. Under certain circumstances, the Single Audit Act and OMB Circulars A-128 and A-133 permit certain recipients of federal financial assistance to have a "program specific" audit. Entities not covered by the Single Audit Act or OMB Circular A-133 may also engage an auditor to conduct a program-specific audit in accordance with a federal audit guide or in accordance with an agreement from the grantor agency (such as the U.S. Department of Education's Student Financial Aid Audit Guide and the U.S. Department of Housing and Urban Development's Audit Guide for Mortgages Having HUD Insured or Secretary Held Multifamily Mortgages). When engaged to conduct a program-specific audit, the auditor should

⁹⁶See paragraph 83 of this Statement for an illustration of the auditor's report on compliance with specific requirements when the auditor concludes that management's refusal to provide written representations is cause for a disclaimer of opinion.

APPENDIX A

AUDIT AND REPORTING REQUIREMENTS UNDER THE SINGLE AUDIT ACT AND OMB CIRCULAR A-128 OR UNDER OMB CIRCULAR A-133

The following table shows procedures performed and reports issued in a single audit an audit in accordance with the Single Audit Act of 1984 and OMB Circular A-128 or with OMB Circular A-133. The table refers to guidance on procedures or reports that differ from those ordinarily performed or issued in an audit conducted in accordance with generally accepted auditing standards. *Additional guidance may be found in the AICPA Audit and Accounting Guide, Audits of State and Local Governmental Units and related AICPA statements of position. The AICPA plans to issue a statement of position that would provide guidance about OMB Circular A-133 requirements.*

<u>Procedures Performed</u>	<u>Report Issued</u>
1. Audit of the financial statements in accordance with generally accepted auditing standards	<ul style="list-style-type: none"> • Opinion on the financial statements • Report on supplementary schedule of federal financial assistance (see paragraph 23.16 of the AICPA Audit and Accounting Guide Audits of State and Local Governmental Units)
2. Audit of the financial statements in accordance with <i>Government Auditing Standards</i>	<ul style="list-style-type: none"> • Report on compliance with laws and regulations that may have a material effect on the financial statements (see paragraphs 18-29) • Report on internal control structure-related matters based solely on an assessment of control risk made as part of the audit of the financial statements (see paragraphs 37-39 of this Statement) • Report on internal controls over federal financial assistance (see paragraph 23.24 of the AICPA Audit and Accounting Guide Audits of State and Local Governmental Units)
3. Study and evaluate controls over federal financial assistance (see paragraphs 21.6-21.16 of the AICPA Audit and Accounting Guide Audits of State and Local Governmental Units) Obtain <u>an understanding and assess control risk</u> of the internal control structure over federal financial assistance and assessment of control risk	
4. Audit of compliance with specific requirements and testing of compliance with general requirements applicable to major federal financial assistance programs, as defined by the Single Audit Act (see paragraphs 43-72 and 80-82) <u>Testing of compliance with general requirements applicable to federal financial assistance programs, and audit of compliance with specific requirements applicable to major federal financial assistance programs as defined by the Single Audit Act or OMB Circular A-133</u>	<ul style="list-style-type: none"> • Report on compliance with general requirements applicable to major federal financial assistance programs (see paragraphs 83 and 84) • Opinion on compliance with specific requirements applicable to <i>each</i> major federal financial assistance program (see paragraphs 73-79) • Schedule of all findings and questioned costs (see paragraph 23.16 of the AICPA Audit and Accounting Guide Audits of State and Local Governmental Units)
5. Testing of compliance with laws and regulations applicable to nonmajor federal financial assistance program transactions selected for testing in connection with 1 or 2, 3, above (see paragraphs 85 and 86)	<ul style="list-style-type: none"> • Report on compliance with laws and regulations applicable to nonmajor federal financial assistance program transactions tested (see paragraphs 87 and 88) • Schedule of all findings and questioned costs (see paragraph 23.16 of the AICPA Audit and Accounting Guide Audits of State and Local Governmental Units)

parallel structure

5. Paragraph 79k suggest that language be added to the auditors report on compliance for major federal programs to limit the intended audience for this report. Such language may be appropriate in situations where the auditor has not done enough work to render an opinion (e.g., "positive and negative assurance") because such reports could be open to misinterpretation by uninformed parties; although we note that under freedom of information laws, all reports are publicly available and can not be restricted from the public. In the case of major federal assistance programs the auditor has rendered an opinion, therefore in our view, a limitation on the distribution of the report is NOT appropriate.

This comment also affects paragraphs 80, 82, 83, 84, and 85.

6. In paragraph 86, we agree with the deletion at the end of the paragraph. However, to clarify only the specific requirements need to be tested, we recommend the previous sentence be amended to include that word as follows:

"...they should be tested for compliance with the specific requirements that apply..."

7. The changes to the introduction section of paragraph 90 could create the false impression that materiality is judged in terms of EACH federal program, regardless of whether the program is "major." We suggest the language be amended so it states:

"...a material effect on the entity's financial statements or a major federal financial assistance program."

8. Paragraph 95 is incomplete in that it implies there are only two differences between A-128 and A-133 when in fact there are at least six or seven major differences. All the major differences should be summarized in the sub-paragraphs to paragraph 95.

9. Paragraph 95a is potentially misleading because the description of a major federal awards program under OMB Circular A-133 (i.e., "federal expenditures total the larger of 3 percent of total federal funds or \$100,000") neglects to mention that this dollar threshold applies, not only to individual award programs, but also in certain cases to categories of programs. We recommend that paragraph 95a should be amended to reflect this fact by substituting the language used in the glossary for "major federal award program" found on page 38 of the PSAS.

10. The description of the common rule furnished in the glossary should be incorporated within the text of the PSAS for the benefit of those unfamiliar with the common rule.

11. The effective date for this PSAS in paragraph 101 should be immediately. Most of the changes incorporated into this PSAS are considered in effect currently when IG's perform their desk or field reviews of single audit reports. To prevent more audits from being identified as substandard, auditors should comply immediately with the guidance incorporated in this PSAS. At a minimum, early application of this statement should be ENCOURAGED.

For Reference
Do Not Take
From the Library
(212) 575-6200 Telex: 70-3396
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August 7, 1991

File Ref. No. 1120
2353

To the Auditing Standards Board:

Re: Exposure Draft of proposed SAS, Compliance Auditing Applicable to Governmental Entities and Other Recipients of Governmental Financial Assistance

Here are additional comment letters received to date on the proposed SAS, Compliance Auditing Applicable to Governmental Entities and Other Recipients of Governmental Financial Assistance.

<u>Name/Affiliation</u>	<u>Location</u>
41. Robert Rocha Arizona Dept. of Administration	Phoenix, Arizona
42. Paul H. Ettinger Dept. of Education	Lansing, Michigan
43. Walter M. Primoff, CPA New York State Society of CPAs	New York, New York
44. Tom Breed Government Accounting & Auditing Committee	Denver, Colorado

Sincerely,


Douglas P. Sauter
Technical Manager
Auditing Standards Division

DPS/lf
Enclosures

cc: SAS No. 63 Implementation Task Force

FIFE SYMINGTON
Governor



4
GERARD W. TOBIN
Deputy Director

ARIZONA DEPARTMENT OF ADMINISTRATION
STATE CAPITOL • 1700 WEST WASHINGTON, ROOM 290
PHOENIX, ARIZONA 85007

July 9, 1991

Mr. Douglas P. Souter, Technical Manager
AICPA Auditing Standards Division
AICPA File 2353
1211 Avenue of Americas
New York, NY 10036-8775

Dear Mr. Souter:

The Arizona Technical accounting Committee submits the following response to your request for written comments regarding the "Exposure Draft - Proposed Statement on Auditing Standards - Compliance Auditing Applicable to Governmental Entities and Other Recipients of Governmental Financial Assistance".

Our Committee has reviewed the Exposure Draft and is in general agreement with its content. However, the Committee does have some concerns which it feels should be addressed prior to the finalization of the Exposure Draft.

1. For three of the required reports, there are no examples of the appropriate language to use when material weaknesses or material instances of noncompliance are identified.
 - For the report on internal control structure-related matters based solely on an assessment of control risk made as part of the audit of the financial statements in accordance with Government Auditing Standards, paragraph 39.k requires "a statement about whether the auditor believes any of the reportable conditions described in the report are material weaknesses and, if they are, identifies the material weaknesses noted." The example report in paragraph 40 illustrates the language when none of the reportable conditions are considered material, but there is no example of the language to be used when material weaknesses exist
 - For the report on compliance with specific requirements applicable to nonmajor program transactions, paragraph 88.f requires "a statement of positive assurance that, with respect to the items tested, the results of those procedures disclosed no material instances of noncompliance with the specific requirements identified." However, neither the report requirements in paragraph 88 nor the illustrative report in paragraph 89 discusses how to report material instances of noncompliance.

Mr. Douglas P. Souter, Technical Manager

Page 2

July 9, 1991

- For the report on compliance with the general requirements, paragraph 50.e requires a similar "statement of positive assurance that, with respect to the items tested, the results of those procedures disclosed no material instances of noncompliance with the general requirements." Again, there is no guidance as to how to report material instances of noncompliance.
- 2. There is no clear definition of material instances of noncompliance as the term relates to general requirements. The Glossary defines general requirements as "those requirements that involve significant national policy and of which failure to comply could have a material impact on an organization's financial statements." This implies that noncompliance with any of the general requirements could be considered material. However, Appendix B, example 1.g refers only to noncompliance that would have a direct effect on the determination of cost-related amounts in the entity's financial statements. The Statement should clarify in what instances noncompliance with any of the general requirements would be considered material.
- 3. Is it really necessary to describe any departure from the auditor's standard report in the required reports referred to in ¶23, ¶39, ¶50, ¶79, and ¶88? Since the auditor's report is issued in conjunction with the required reports and is referred to in them, the reader has the information readily available. Because the required reports are numerous and individually lengthy, we think there should be an effort made to lessen their content rather than unnecessarily expand it.

If you have any questions regarding our response, please feel free to contact me at (602) 542-5405.

Sincerely,



Robert Rocha
State Accounting Administrator
General Accounting Office

cc: ReImond P. Van Doniker
Executive Director for NASACT

RR/KO/lp



DONALD L. BEMIS
 Superintendent
 of Public Instruction

STATE OF MICHIGAN

DEPARTMENT OF EDUCATION

P.O. Box 30008
 Lansing, Michigan 48909

July 15, 1991

42

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AICPA

Douglas P. Sauter, Tech.Mgr.
 Auditing Standards Division
 1211 Avenue of the Americas
 New York, NY 10036-8775

RE: Comments on Proposed Statement on Auditing Standards
 Compliance Auditing Applicable to Governmental Entities and
 Other Recipients of Governmental Financial Assistance

I. I believe the illustrative report in Paragraph 89 is appropriate for recipients when the total amount of major Federal assistance program expenditures is more than 50% of the recipient's total Federal financial assistance expenditures for the year under audit.

I also believe that an optional report should be issued which modifies the illustrative report in Paragraph 89, when the recipient organization has no major programs or if total assistance expended under major programs is less than 50% of total Federal assistance expended by the recipient during the year under audit.

Therefore, I suggest the following changes:

1. Change the sentence, "We selected certain transactions applicable to certain nonmajor Federal financial assistance programs..." to read for example, "We selected certain transactions applicable to the largest nonmajor programs [list the programs] and the other (smaller) nonmajor programs."
2. Change the sentence, "Our procedures were substantially less in scope than an audit..." to read, "Our procedures were less in scope than audit for the largest nonmajor programs and substantially less in scope for other nonmajor programs, the objective of which..."

These suggested changes in reporting would;

- allow the reader (user of the report) to focus on the largest nonmajor programs tested and to differentiate between the level and extent of testing for the largest nonmajor and the other (smaller) nonmajor programs that may have taken place.
- correlate with the AICPA 50% rule when considering the internal control structure applicable to managing the largest nonmajor programs in compliance with laws, regulations and policies.
- apply the OMB Circular A-128 regulations in paragraph 8(3), "The transactions related to (under the 50% rule of the AICPA for considering the internal control structure, which applies to the largest non-major and other nonmajor programs)...shall be tested for compliance with Federal laws and regulations that apply to such transactions."

- provide for a correlation with and integration of the report on the internal control structure over Federal financial assistance programs with the compliance report on Federal programs by the statement, "the auditor's procedures were less in scope than an audit," which is similar to the statement in the single audit report on the internal control structure and by naming the largest nonmajor programs.

Determining whether additional testing for compliance with the specific requirements is necessary is a matter of professional judgment. Among the matters the auditor considers are the nature of the control elements and whether his or her tests of controls over compliance with specific requirements provides evidence that would support this report on compliance.

in regard to this sentence in Paragraph 89, "However, the results of our procedures disclosed immaterial instances of noncompliance with those requirements, which are described in the accompanying schedule of findings and questioned costs." I make the following comment;

If there are no instances of noncompliance, this should be stated. This statement should be made, "Further, the results of our procedures disclosed no instances of noncompliance with those requirements..."

II. under the topic, "Compliance Auditing - General Requirements", paragraph 51 which gives an example of a report on compliance with general requirements, I suggest the following:

The report should identify the types or nature of the programs tested, which should give the reader some confidence in the range and size of the programs tested for compliance. For example, the statement might read, "We have applied procedures to test the General Government, compliance with the following requirements applicable to (each of its major) the largest nonmajor, and the smaller nonmajor Federal financial assistance programs..."

Because of the broad range in programs and the nature of the requirements tested, it may be appropriate to say, "Our procedures were substantially less in scope..." However, for certain general requirements of the largest nonmajor and major programs the auditor should consider whether he could issue a report saying, "Our procedures were less in scope..." The auditor should issue the highest level of report consistent with the scope and extent of tests performed for the programs tested. With some additional testing for major and largest nonmajor, the auditor may issue a report and differentiate between the level and extent by saying, "Our procedures were less in scope for major/largest nonmajor programs and substantially less in scope for the smaller nonmajor programs."

Again, I suggest that if there are no instances of noncompliance this should be stated. This statement applies to all compliance reports.

III. Appendix C -Single Audit Reporting on Compliance (p.36)

The diagram does not match the requirements in the text in a clear and concise manner as it applies to the general requirements. The diagram presently used in SAS 63 on page 70 could be used as a model if modified. There should be an arrow from the box, "Test specific requirements applicable to nonmajor transactions" to a box titled, "Test general requirements (Paragraphs 45-47)."

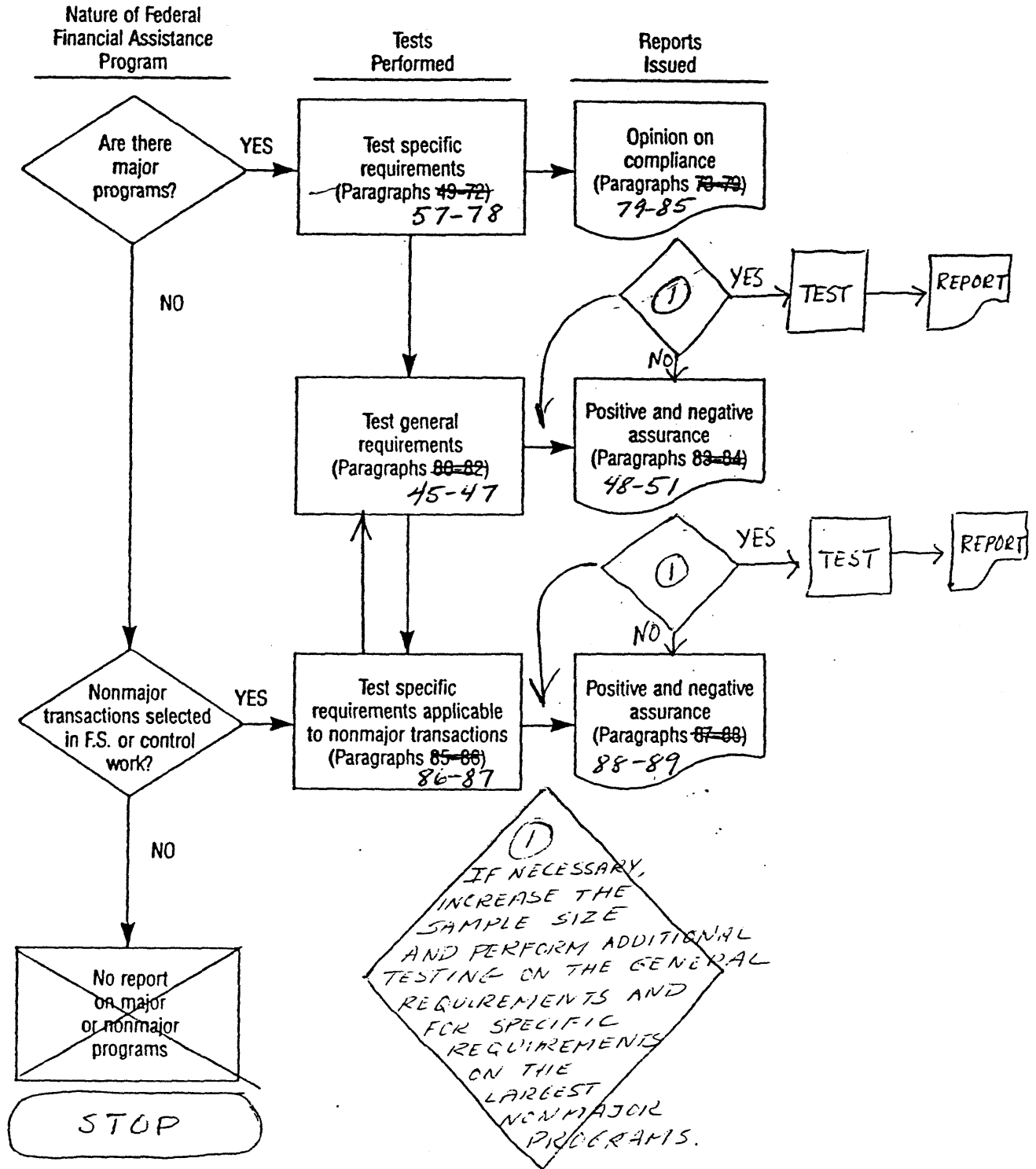
For nonmajor programs, paragraph 48 in the Proposed Statement says, "the auditor should consider whether his or her tests of controls over compliance with general requirements provides evidence that would support a report on compliance." Therefore, the control work and transactions selected in financial statements and any additional procedures used provide a basis for test of compliance with general requirements and specific requirements of the nonmajor programs. As a result of audit procedures used, a report on the general requirements and a report on the specific requirements are issued. The reports give positive and negative assurance for the item tested. The report on compliance for general requirements would incorporate and identify the types of Federal financial assistance programs as major and nonmajor Federal programs.

Sincerely Yours,

Paul H. Ettinger

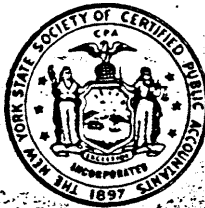
Paul H. Ettinger
Single Audit Coordinator
Department of Education

Single Audit Reporting on Compliance



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NEW YORK, NY 10166-0010
212 973-8300
TELECOPIER 212 972-5710

nysscpa

July 23, 1991

Douglas P. Sauter, Technical Manager
AICPA Auditing Standards Division, File 2353
American Institute of CPAs
1211 Avenue of the Americas
New York, New York 10036-8775

RE: PROPOSED STATEMENT ON AUDITING STANDARDS
COMPLIANCE AUDITING APPLICABLE TO GOVERNMENTAL
ENTITIES AND OTHER RECIPIENTS OF GOVERNMENTAL
FINANCIAL ASSISTANCE

Dear Mr. Sauter:

We are enclosing the comments of the New York State Society of Certified Public Accountants in response to the above AICPA exposure draft. These comments were prepared by the Society's Government Accounting Committee and Auditing Standards & Procedures Committee.

Thank you for your consideration.

Very truly yours,

Walter M. Primoff, CPA
Director of Professional
Programs

WMP/er
enc.

cc: Accounting & Auditing Chairmen

ANDREW J. CAPELLI, CPA PRESIDENT
STEVEN C. BAUM, CPA PRESIDENT-ELECT
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NEW YORK, NY 10166-0010
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nysscpa

July 2, 1991

American Institute of Certified
Public Accountants
1211 Avenue of the Americas
New York, New York 10036-8775

Attention: Auditing Standards Division, File 2353

Dear Sirs:

The following are the New York State Society of Certified Public Accountant's Government Accounting and Auditing Standards and Procedures Committee's joint comments on the Exposure Draft entitled "Proposed Statements on Auditing Standards - Compliance Auditing Applicable to Governmental Entities and Other Recipients of Governmental Financial Assistance":

The following points were developed by the Government Accounting Committee:

- The contents of reports on compliance and internal control structure would require a statement that the auditor has audited the financial statements and a reference to the auditor's report on the financial statements, including a description of any departure from the standard report is a positive change that will aid the reader of the reports, especially as these reports are often issued separately from the general purpose financial statements. It is imperative that the reader of these reports understand any departure from the standard report so that the findings of the report can be evaluated in that context.
- The exposure draft requires the auditor issue a report on compliance with the general requirements regardless of whether the government being audited has major programs. It would appear that this is not a question of whether the change is a positive or negative one, but rather one of service to our clients. If those who administer federal assistance, our clients, indicate their desire for us as auditors to expand the scope of our procedures, as a service organization, we must comply.

American Institute of
Certified Public Accountants

July 2, 1991

Page Two

- The exposure draft provides guidance on the auditor's compliance auditing responsibilities under OMB Circular A-133. This is a positive change in that the exposure draft provides comprehensive guidance in an area where previously none had existed.
- The provisions of the statement are effective for audits of financial statements and of compliance with laws and regulations for fiscal periods ending after December 31, 1991. We would recommend that the effective dates for the various proposed Statement of Position and Statements on Auditing Standards effecting compliance and internal control reports be coordinated so that the effective dates are simultaneous. In this way, confusion among practitioners, regulators, and other users of the reports would be minimized.

In addition to the above suggestions, the following points were developed by the members of the Auditing Standards and Procedures Committee:

- Paragraph 25, reporting example - consider changing wording to read "...laws, regulations, contracts, or grants." The implication of present wording is that all listed items apply and this may not be the case.
- Paragraph 45 requires reporting on general compliance requirements for all programs. We believe that the intent is that, as stated in paragraph 42, this would apply to programs which receive in excess of \$25,000. However, this point is open to interpretation and we believe that the wording should be changed (in paragraph 42, 45 or in a footnote) to clarify the reporting requirements required by paragraph 46.
- Page 38 of the exposure draft gives the definition of a "major federal financial assistance program." We believe that the term "all programs" should be expanded to describe the meaning of this term (do we mean: of the funding agency? the federal government as a whole? the receiving entity? the agency administering the funds within the recipient government?).

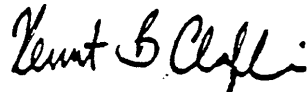
American Institute of
Certified Public Accountants

July 2, 1991

Page Three

- General observation - this proposed SAS is exposed in order to include new requirements under OMB Circular A-133. The SAS is attempting to give detailed information as to the auditor's responsibility under governmental standards. This type of information would be more appropriate in an audit guide. Also, presentation of detailed requirements would require update for each change in law or regulation. We would suggest that consideration be given to advising auditors of the necessity to comply with the regulations governing entities or programs being examined and that the ASB designate these publications as designating GAAP and GAAS for federally financed programs (see paragraphs 96 to 100).

Very truly yours,



Kenneth B. Clafin, CPA
Government Accounting Committee
Urbach Kahn & Werlin PC
66 State Street
Albany, New York 12207

Very truly yours,



Paul J. Weireter, CPA, Chairman
Auditing Standards and Procedures
Committee
Eisner & Lubin
250 Park Avenue
New York, New York 10177

**Colorado Society of
Certified Public Accountants**

June 24, 1991

44

American Institute of Certified Public Accountants
Mr. Douglas P. Sauter, Technical Manager
Auditing Standards Division
1211 Avenue of the Americas
New York, New York 10036-8775

Re: File 2353, Exposure Draft, Proposed statement on auditing standards.

Compliance auditing applicable to governmental entities and other recipients of governmental financial assistance.

Dear Mr. Sauter:

The following represents the views of the Colorado Society of Certified Public Accountants' Governmental Accounting and Auditing Committee with regard to this exposure draft.

Paragraph 3

This is a good discussion emphasizing the client's responsibility and providing the auditor with guidance that is applicable to the normal course of auditing smaller governmental entities, in that single audit applicability is not determined until field work has commenced.

Paragraph 48

This requirement would produce a significant burden on practitioners who audit smaller governmental entities because sufficient evidence to issue a report on compliance with general provisions is generally not obtained as part of the study and evaluation of control structure as it relates to federal financial assistance.

Paragraph 96

Additional discussion is required to address the following questions and issues related to the examples provided in paragraph 96.

1. To what extent do the provisions of paragraph 96 override paragraph 42 when more than \$100,000 of federal financial assistance is involved? Additionally, the examples in paragraph 96 should discuss that program specific audits are generally not elective, but are required by the agency.
2. Would following one of the example audit guides and issuing the reports as described in these audit guides be an acceptable alternative to issuing the additional reports required by the Single Audit Act as defined in OMB Circular A-128 and or OMB Circular A-133?

3. The committee sees a need for additional guidance on the reporting for Single Audit purposes relating to housing authorities and other not-for-profit corporations that elect to follow specific program audits, yet are a component unit of a reporting entity that has Single Audit reporting requirements. Additionally, guidance is requested in the case of housing authorities and other not-for-profit corporations which receive federal financial assistance in addition to HUD, and are required by HUD to do specific program audits in accordance with the audit guides in the example.

Generally, the exposure draft will make SAS63 a more understandable and logical document.

Very truly yours,

Tom Breed

Tom Breed
Chairman
Governmental Accounting and Auditing Committee

September 3, 1991

File Ref. No. 1120
2354


To the Auditing Standards Board:

Re: Exposure Draft of proposed SAS, Compliance Auditing
Applicable to Governmental Entities and Other Recipients of
Governmental Financial Assistance

Here are additional comment letters received to date on the
proposed SAS, Compliance Auditing Applicable to Governmental
Entities and Other Recipients of Governmental Financial Assistance.

<u>Name/Affiliation</u>	<u>Location</u>
45. Philip Calder Gov't Accounting and Auditing Committee	New York, New York
46. Lawrence F. Alwin National State Auditors Association	Austin, Texas
47. James B. Thomas, Jr. President's Council on Integrity & Efficiency Standards Subcommittee	Washington, DC

Sincerely,



Douglas P. Sauter
Technical Manger
Auditing Standards Division

DPS/lf

cc: SAS No. 63 Implementation Task Force

August 12, 1991

Mr. Douglas P. Sauter
Technical Manager
Auditing Standards Division, File 2353
American Institute of Certified Public Accountants
1211 Avenue of the Americas
New York, New York 10036

Proposed Statement on Auditing Standards, Compliance Auditing
Applicable to Governmental Entities and Other Recipients
of Governmental Financial Assistance

Dear Doug:

The AICPA Government Accounting and Auditing Committee (the committee) generally supports the issuance of the above-captioned proposed statement. The committee believes it updates existing guidance to properly reflect changes resulting from the recent issuance of the revised Compliance Supplement for Single Audits of State and Local Governments and OMB Circular A-133, Audits of Institutions of Higher Education and Other Nonprofit Organizations. However, as discussed below, the committee believes the proposed statement would be improved by providing additional guidance when reporting on compliance under Government Auditing Standards, providing guidance on materiality when testing the "general requirements," removing certain guidance on testing nonmajor program transactions, and by expanding the information provided on Circular A-133. Other comments, principally of an editorial nature, are listed in the attachment to this letter.

Reporting on Compliance under Government Auditing Standards
(Paragraph 25)

Paragraph 25 provides guidance in situations where the auditor, decides, based on an assessment of materiality, not to perform any tests of compliance with provisions of laws, regulations, contracts, and grants. When conducting a Single Audit engagement, the auditor is required to perform such tests and, therefore, a sentence or footnote should be added to paragraph 25 to indicate this difference in requirements as to an audit conducted in accordance with Government Auditing Standards and an audit which is conducted in accordance with the Single Audit Act.

Materiality when Testing the "General Requirements" (Paragraphs 47-48)

Paragraphs 47-48 provide guidance on the procedures to be performed and other matters the auditor should consider when reporting on the general requirements. A final statement should also provide that materiality with respect to these requirements is based on the entity's total expenditures under federal financial assistance programs. Such guidance would assist the auditor in determining the extent of testing of the general requirements.

Restrictive Use Paragraph in Report on "Specific Requirements" (Paragraphs 79 and 80)

Paragraph 79 k states that the auditor's report on the specific compliance requirements should contain a statement that the report is intended for the information of the audit committee, et al. This restriction is unnecessary and that it is inconsistent with professional standards when expressing an opinion. Therefore, the committee recommends that the requirement not be included in a final statement.

Specific Compliance Requirements - Nonmajor Programs (Paragraph 86)

Paragraph 86 proposes to delete the last phrase of the last sentence in paragraph 86. The phrase, as included in the original statement, should not be deleted because it provides useful, explanatory guidance to auditors.

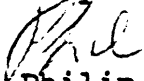
Information on Circular A-133 (Paragraphs 92-95)

The committee recognizes that a statement of position will be issued by the AICPA to provide detailed guidance to auditors conducting audits in accordance with OMB Circular A-133; nevertheless, it believes that this section of a final statement should include all differences between the requirements of OMB Circular A-133 and the Single Audit Act of 1984 and OMB Circular A-128. Paragraph 92 should include a statement that if a state or local government has a nonprofit organization, which is a part of the state or local government's reporting entity, the state or local government has an option of having that nonprofit organization audited in accordance with OMB Circular A-133 or of having the Single Audit of the state or local government encompass the nonprofit organization.

* * * * *

The committee would be pleased to discuss these comments with the Auditing Standards Board or to answer any questions that may arise.

Very truly yours,



Philip T. Calder, Chair
Government Accounting and Auditing Committee

Attachment

AICPA Government Accounting and Auditing Committee

Other Comments on the Proposed Statement

Paragraph 46

Paragraph 46 i refers to "f and g above." The reference should be "d,f and g above" to conform to OMB Compliance Supplement for Single Audits of State and Local Governments

Glossary, page 39

In the definition of "specific requirements," a statement is made that the Compliance Supplement includes the requirements specific to sixty-two federal programs that provide approximately 90 percent of the federal aid to state and local governments. While this was true of the earlier edition of the Compliance Supplement, it is not true of the 1990 edition. The committee recommends that references to the number of programs and percent of dollars be deleted from the definition of "specific requirements."

National State Auditors Association

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August 12, 1991

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Douglas P. Sauter, Technical Manager
AICPA Auditing Standards Division
File 2353
1211 Avenue of Americas
New York, NY 10036-8775

Dear Mr. Sauter:

The National State Auditors Association (NSAA) is pleased to submit the following comments on the American Institute of Certified Public Accountants' (AICPA's) proposed Statement on Auditing Standards (SAS) entitled, "Compliance Auditing Applicable to Governmental Entities and Other Recipients of Governmental Financial Assistance." We appreciate the opportunity to respond to the proposed SAS. It should be noted that the following comments are not intended to represent a single response for all NSAA members individually. The views of some members may not be fully in concert with all of the comments presented here. Individual state auditors may wish to respond to this proposed SAS separately.

Overall, we believe the document is a step forward and provides improved guidance to auditors. However, we did identify several areas which seem to be either unclear as drafted or technically incorrect and therefore, should be modified. Although some issues are more significant than others, we have presented our comments in paragraph number sequence to simplify your review process.

Introduction and Applicability

We believe that paragraph three should be revised as indicated below (new language is shown in italics):

....Therefore, if during a GAAS audit of the financial statements the auditor becomes aware that the entity is subject to an audit requirement that is not encompassed in the terms of the engagement, the auditor should communicate to management *and* the audit committee, or others with authority and responsibility *equivalent to that of an audit committee*, that an audit in accordance with generally accepted auditing standards may not satisfy the relevant legal, regulatory, or....

As written in the proposed revision, paragraph three indicates that an auditor may satisfy the standard by notifying management, but not other appropriate parties, about deficiencies in an audit engagement. However, reporting such matters solely to management

does not ensure that all appropriate parties are informed. Furthermore, if an audit committee or other equivalent authority was involved in preparing the request for proposal, selecting the auditor, and/or signing the engagement agreement, etc., all matters affecting the propriety of the engagement agreement should be communicated to that party.

Reporting Under Government Auditing Standards

Paragraph 23.a (as well as paragraphs 39.a, 50.a, 79.a, and 88.a) states that the auditor's report on compliance shall include a reference to the auditor's report on the financial statements "...including a description of any departure from the standard report." Under current AU Section 801 requirements, the various compliance and internal control reports begin with a statement that the auditor has audited the financial statements and a reference to the auditor's report on those statements. The Exposure Draft (ED) has modified this requirement to indicate that any departure from the standard report should be described. We have several concerns regarding the AICPA's addition of this requirement:

1. The term "description" is ambiguous and may be interpreted by the reader in many different ways. Therefore, we suggest that the final Statement clearly indicate that the description to be included in the auditor's report on compliance is intended to be a summary or paraphrased version of the departure, not the departure repeated verbatim from the auditor's report on the financial statements. Because the required reports are numerous and individually lengthy, we believe there should be an effort made to lessen their content rather than expand it.
2. The ED does not provide an example of an appropriate description or clarify how the description in paragraph 23 relates to the following statement in paragraph 27 regarding the reporting of material instances of noncompliance with laws and regulations required under Government Auditing Standards:

The auditor may wish to include a statement about whether the misstatements resulting from the material instances of noncompliance have been corrected in the financial statements or a statement describing the effect of such misstatements on his or her report on the basic financial statements. [emphasis added]

The example report in paragraph 27 includes these statements in the paragraphs after the initial paragraph referring to the financial statement audit. It is possible that the auditor could be describing the same situation in both the initial paragraph and subsequent paragraphs of the report on compliance if the misstatements resulting from material noncompliance require a departure from the standard report on the financial statements. We believe this warrants clarification.

3. The requirement is inconsistent with internal control reporting requirements for single audits of federal financial assistance in the AICPA's recently issued SOP 90-9. Paragraph 16.a of the SOP indicates that the report is to begin with a reference to the auditor's report on the financial statements but does not require departures from the standard report to be described.

4. For an audit of a governmental entity, the auditor may issue all required reports together (e.g., in a single bound document). In this situation, describing departures from the auditor's standard report on the financial statements in the reports on compliance and internal control would appear to be unnecessary since the reader has the former report available when he/she reviews the latter reports.

Paragraph 26 lists the requirements for a report in which the statement of positive assurance is qualified for material instances of noncompliance, and paragraph 27 includes an example of such a report. Footnote 13 to paragraph 26 further notes that the auditor is not precluded from issuing an adverse report on compliance but does not illustrate this type of report. We believe the ED's guidance for the report on compliance required under Government Auditing Standards should be expanded to:

1. Include an example of the adverse report referred to in footnote 13.
2. Recognize that the extent of noncompliance noted in tested items may preclude the auditor from expressing negative assurance on untested items and to illustrate the required reporting language.

We also suggest the paragraphs for the two federal compliance reports discussed in paragraphs 49-51 and 88-89 be revised to recognize additional reporting options: a qualified or an adverse report or the inability to give negative assurance on untested items. The inability to give negative assurance was recognized in examples 17 and 18 of the 1986 revised AICPA audit and accounting guide, Audits of State and Local Governments. Although the situation continues to be encountered, the suggested reporting language for this option was not included in either current AU 801 or SOP 89-6, "Auditors' Reports in Audits of State and Local Governmental Units."

Paragraph 29 includes a statement that the auditor is to modify the report on compliance required under Government Auditing Standards if nonmaterial instances of noncompliance have been communicated to management in a separate letter. However, the list of report components in paragraph 23 and the report examples in paragraphs 24, 25, and 27 do not refer to this statement. These paragraphs are inconsistent with paragraphs 39-41 on the report on the internal control structure, which do list or illustrate a similar statement regarding certain control structure matters communicated to management in a separate letter (i.e., paragraph 39.1 and the next to last paragraphs of the reports in paragraphs 40 and 41).

For the report on internal control structure based solely on an assessment of control risk made as part of the audit of the financial statements in accordance with Government Auditing Standards, paragraph 39.k requires "a statement about whether the auditor believes any of the reportable conditions described in the report are material weaknesses and, if they are, identifies the material weaknesses noted." The example report in paragraph 40 illustrates the language when none of the reportable conditions are considered material, but there is no example of the language to be used when material weaknesses exist.

Responsibilities Under the Single Audit Act

As a general comment, we believe paragraph 45 needs clarification in regards to the materiality level for general requirements. As written, we believe the paragraph is very confusing, if not misleading. The first sentence in paragraph 45 describes the general requirements as those that involve significant national policy and for which failure to comply could have a material impact on an organization's financial statements including those prepared for federal programs. The phrase "including those prepared for federal programs" has been added in this ED. The discussion of materiality for the general requirements that was contained in the original SAS 63 has been deleted. We are confused as to what the materiality level is for the general requirements. Is it the financial statement level or the federal financial assistance program level? This confusion is further compounded by the report language contained in paragraph 51. The first paragraph of the report refers to the financial statements. Yet, the reference in the fourth paragraph to "material instances" is not well defined.

Paragraph 45 also discusses general requirements that have a direct and material effect on the determination of financial statement amounts as opposed to those that have an indirect effect on the financial statements. Is the auditor required to test those general requirements that don't have a direct and material effect on the overall financial statements or on federal financial assistance if that is the level they are supposed to be evaluating against?

Finally in paragraph 45, we believe the language in the first sentence is incorrect. The OMB Compliance Supplement for Single Audits of State and Local Governments (Compliance Supplement), does not implement OMB Circular A-128. The Compliance Supplement is a federal document which sets forth the major compliance requirements that should be considered in an organization-wide audit of state and local governments that receive federal assistance. It supplements OMB Circular A-128, it does not implement it (emphasis added). Also, the first sentence of this paragraph should indicate that the Compliance Supplement includes "numerous" general requirements rather than specifically indicating that there are "nine" general requirements. With the enactment and/or changes in laws and the periodic revision of the Supplement, there are also changes in the number of general requirements to be considered by the auditor. Hence, there is no need to be specific about the number of "general requirements" included in the Compliance Supplement. This could help prevent unnecessary revisions to the Statement.

In paragraph 46, we suggest the first parenthetical phrase in item i be changed to "(in addition to d, f, and g above)" since page 2-9 of the Compliance Supplement refers to cash management (d in paragraph 46) as well as financial reporting and cost principles (f and g, respectively). Also, footnote 20 to paragraph 46 should indicate that the auditor should be aware that the Compliance Supplement is revised periodically and that with each revision the number of general requirements may also change.

For the report on compliance with general requirements, paragraph 50.e requires a "statement of positive assurance that, with respect to items tested, the results of those procedures disclosed no material instances of noncompliance with the general requirements." Again, there is no guidance as to how to report material instances of noncompliance.

Mr. Douglas P. Sauter
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Paragraphs 62-72 discuss the concepts of audit risk and paragraphs 90-91 discuss management's written representations. The AICPA has previously issued extensive guidance on these two topics in Statements on Auditing Standards No. 47 entitled, Audit Risk and Materiality in Conducting an Audit, and No. 19 entitled, Client Representations, respectively. Therefore, to provide further guidance to the auditor, we suggest that paragraphs 62-72 and 90-91 include appropriate footnote references to those respective Statements on Auditing Standards, similar in content to footnote No. 21 and page 19 of the ED.

Paragraph 79.k states that a basic element of the auditor's report on compliance with specific requirements is "a statement that the report is intended for the information of the audit committee, management, and specific legislative or regulatory bodies, but that this is not intended to limit the distribution of the report, if a matter of public record." We believe that this language is inappropriate, particularly in a report prepared by a governmental auditor, and may, in fact, confuse the reader. In several states, the State Auditor or the Auditor General has constitutional audit authority and all audit reports are available to the public. Therefore, we suggest that paragraph 79.k be deleted, or made an optional requirement, in the final Statement.

Paragraph 80 gives an example of an unqualified opinion on an entity's compliance with requirements which govern each major federal financial assistance program. The first sentence in the second paragraph has been modified to the point where it is presently unclear to us. The language addressing specific requirements (types of services allowed or unallowed; eligibility; matching, level of effort, or earmarking; reporting; claims for advances and reimbursements; and amounts claimed or used for matching) has been lined out and replaced with the following [list requirements tested]. We do not know if this implies listing only those specific requirements tested once for all major programs covered or whether one has to list each major program along with the specific compliance requirements which apply for each major program. On single audits of larger governmental entities, the reports will become very lengthy and cumbersome if the auditor is expected to list all special tests and provisions from the Compliance Supplement that were tested for all major or nonmajor programs. The reason for making a change and the expectation of what is required is simply unclear to us.

Paragraphs 81-85 on pages 26 to 28 discuss certain situations, such as a scope limitation, the inability to obtain sufficient competent evidential matter, or an inadequacy in the accounting records, in which the auditor may be required to qualify the opinion or to disclaim an opinion on compliance. However, this guidance does not alert the auditor that these situations may also affect the opinion on the financial statements. We suggest that a sentence be added at the end of paragraph 81, similar in nature to the second sentence of paragraph 91 on page 31, such as "Further, the auditor should consider the effects of these situations on his or her ability to express an unqualified opinion on the financial statements." Further, we believe that the narrative preceding the examples of auditor's opinions in paragraphs 81-85 should also clearly indicate that, if the auditor disclaimed an opinion on the financial statements, the first paragraph of the compliance opinion would not be the same ("We were engaged to audit" rather than "We have audited") as illustrated in paragraph 80.

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Page 6

Paragraphs 84-85 lack sufficient guidance to assist the auditor in deciding whether a qualified opinion or an adverse opinion is necessary when instances of noncompliance are noted. We suggest the AICPA include in paragraph 84 guidance modified from AU Section 508.50 which explains considerations affecting the auditor's decision to give a qualified or an adverse opinion on the financial statements due to material departures from generally accepted accounting principles. Presenting such guidance would also be consistent with the procedures followed in paragraph 82 for report modifications due to scope limitations. To assist the auditor in deciding whether to offer a qualified opinion or to disclaim an opinion on compliance due to a scope limitation, paragraph 82 includes guidance modified from AU Section 508.41 for the auditor's report on the financial statements.

Paragraphs 86-88 differ in the discussion of the other reports on compliance in that these paragraphs do not clearly state before the list of required report elements the nature of the auditor's assurance to be expressed for compliance with the specific requirements applicable to nonmajor programs (i.e., no opinion on compliance, statements of positive and negative assurance only). Also, for the report on compliance with specific requirements applicable to nonmajor program transactions, paragraph 88.f requires "a statement of positive assurance that, with respect to the items tested, the results of those procedures disclosed no material instances of noncompliance with the specific requirements identified." However, neither the report requirements in paragraph 88 nor the illustrative report in paragraph 89 discuss how to report material instances of noncompliance. As stated earlier in this response, additional guidance should be offered on how to report material instances of noncompliance.

Also, paragraph 89 states that the report on the results of the tests of compliance with requirements applicable to nonmajor federal financial assistance program transactions may be combined with the report on compliance for major federal financial assistance programs. However, the ED does not include an example of the combined report. To avoid confusion, inefficiency, and potential inconsistency within the profession, we suggest that the final Statement include an example of the combined report mentioned in paragraph 89.

Because the word "major" was deleted, the first sentence of paragraph 90 on page 30 currently concludes with the phrase "...that, if not complied with, could have a material effect on a federal financial assistance program." We believe that this revision unintentionally reduces the threshold of materiality to the potentially unacceptable level of the smallest program. Therefore, we suggest that the word "major" be reinstated or the phrase be revised to read "...that, if not complied with, could have a material effect on federal financial assistance."

Also, paragraph 90.g as currently written, implies that it is management's responsibility to enforce subrecipient compliance with applicable laws and regulations. We interpret management's responsibility to monitor and inform subrecipients, but not to enforce compliance. Therefore, we suggest that paragraph 90.g be revised to read "Management has monitored subrecipients to determine whether the subrecipients expended financial assistance in accordance with applicable laws and regulations and whether the subrecipients have met the requirements of OMB Circular A-128, OMB Circular A-133, or OMB Circular A-110, whichever is applicable."

Paragraph 95.a should be expanded to indicate that in determining a major Federal assistance program, OMB Circular A-128 treats each Federal assistance program individually. OMB Circular A-133, in contrast, treats all federal assistance provided to the recipient for research and development as one Federal assistance program and similarly combines all Federal assistance furnished to the recipient for Student Financial Aid purposes and considers it as one Federal assistance program.

Other Compliance Auditing Responsibilities

The first sentence of paragraph 96 may need to be expanded to further show that infrequently a Single Audit may not satisfy audit provisions for a Federal program because a Federal statute may require that a program-specific audit be performed of a Federal assistance program. Also, the last sentence of paragraph 96 states that "...the auditor should obtain an understanding of the audit requirements for that particular program either from the agreement with the grantor agency, from an audit guide published by the grantor agency, or through contact with the grantor agency." Because the auditor should be encouraged to obtain a complete understanding of the audit requirements from as many sources as may be necessary, we suggest that this sentence be revised to read "...the auditor should obtain an understanding of the audit requirements for that particular program from the agreement with the grantor agency, from an audit guide published by the grantor agency, and/or through contact with the grantor agency."

As the proposed Statement is currently formatted, paragraph 100 appears to relate only to the topics in paragraphs 98-99. Because the auditor may want to also consider including the audit requirements for a program-specific audit (as discussed in paragraphs 96-97) in a proposal, contract, or engagement letter, we suggest that the guidance in paragraph 100 be expanded to also encompass the topics in paragraphs 96-97.

Effective Date

Paragraph 101 establishes audits for fiscal periods ending after December 15, 1991, as the effective date and concludes with the sentence "Early application of this Statement is permissible." Because the Auditing Standards Board (Board) has indicated that the revisions in this document were principally based on recent developments that have already occurred within the government accounting and auditing community, such as the issuance of OMB Circular A-133, we strongly suggest that the last sentence of paragraph 101 be revised to read "Early application of this Statement is encouraged."

On the other hand, if the Board is unable to issue the revised Statement soon after the close of the comment period, consideration should be given to extending the effective date of implementation. It is important to understand that some entities will engage their audit for the year ending December 31, 1991, as much as six months before the year-end. The auditor, as well as the entity, should know which auditing standards are applicable to an audit at the time the audit engagement is signed.

Transitional Guidance

Paragraph 102 states that the provisions of SAS No. 63 are applicable "...until this Statement is effective or adopted." We find this phrase to be confusing and, unless the proposed Statement is adopted with immediate effect, contradictory. Therefore, we suggest that paragraph 102 be revised to read "...until this Statement is effective or early implemented in accordance with Paragraph 101."

Appendix A

Item number 4, under the "Procedures Performed" heading needs adjustment. Since the tests of compliance with general requirements applicable to federal financial assistance programs and the audit of compliance with specific requirements applicable to major programs represent two distinct sets of procedures as discussed in the ED, we suggest these items be presented as 4 and 5 rather than being combined in 4 as they currently are. In the previous version of AU Section 801, combining the procedures under 4 was reasonable since the tests of compliance with the general requirements applied only to major programs.

Item number 5, first bullet under "Report Issued" heading needs adjustment. To be consistent with descriptions in the text, Appendix C, and with other report titles in this appendix, the description should read "Report on compliance with specific requirements applicable to nonmajor federal financial assistance program transactions tested."

Appendix B

In several paragraphs of Appendix B and in the Glossary definition of the Single Audit Act of 1984, "general-purpose" is hyphenated, but in previous pronouncements it hasn't been. Also, the statement in the Glossary definition of the Single Audit Act of 1984, which states that the Act requires an audit of the general purpose financial statements, is incorrect. According to OMB's Questions and Answers document on OMB Circular A-128, "The Circular does not require the preparation of general purpose financial statements in accordance with GAAP. However, financial statements are required. The Circular requires an audit of financial statements that are prepared by the recipient to meet its needs and the needs of other statement user. However, if these statements are not prepared in accordance with generally accepted accounting principles, the audit report should state the nature of the variances therefrom and follow professional guidance for reporting on financial statements which have not been prepared in accordance with GAAP." Nowhere in the Single Audit Act of 1984 or OMB Circular A-128 is the modifier "general purpose" used in conjunction with "financial statements."

As always, NSAA is pleased to present these comments and we look forward to providing a response on similar issues in the future. As stated earlier, the state auditors generally agree with the content of this proposed SAS. The comments presented in this response are intended to assist the AICPA's Auditing Standards Board in making this SAS a more clear, comprehensive and efficient

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document. If you require further information or have any questions in this matter, please contact ReImond P. Van Daniker, Executive Director of NASACT, at (606) 276-1147 or myself at (512) 479-4900.

Sincerely,

Lawrence F. Alwin

Lawrence F. Alwin
President



PRESIDENT'S COUNCIL on INTEGRITY & EFFICIENCY
STANDARDS SUBCOMMITTEE

August 29, 1991

Douglas P. Sauter, Technical Manager
AICPA Auditing Standards Division
File 2353
American Institute of Certified Public Accountants
1211 Avenue of the Americas,
New York, N.Y. 10036-8775

Dear Mr. Sauter:

The Standards Subcommittee of the President's Council on Integrity and Efficiency (PCIE) appreciates the opportunity to comment on the AICPA Exposure Draft: Proposed Statement On Auditing Standards - Compliance Auditing Applicable To Governmental Entities And Other Recipients Of Governmental Financial Assistance. The proposal generally provides reasonable guidance. However, we do have the following comments and recommendation for your consideration:

Paragraph

No.

Comment

3

There should be an expansion of either this paragraph or the accompanying footnote in regards to auditor communication, when there are audit requirements not encompassed in the terms of the engagement. The expansion should require communication to elected officials or governing bodies. An example is that often in local government the auditor selection and audit contract approval is performed by the local governing body and not management. Also, elected officials hold the public trust for government accountability. Therefore these elected officials need to be told when the planned audit will not meet laws, regulations, and contractual agreements.

The expansion should also require communication to a governmental auditor within the level of government being audited who has oversight responsibility for auditing within that government. For example, a state auditor may have responsibility for overseeing auditing of all state departments. Therefore, the state auditor needs to be told when a planned department's audit will not meet laws, regulations, or contractual agreements.

Further, the reference to OMB Circular A-110 should be eliminated from this paragraph.

- 4 Paragraph states that the communication required when an auditor discovers that the entity is subject to an audit requirement not covered in the engagement can be either verbal or written. We believe the communication should be written.
- 23f The addition of a "disclaimer of opinion on compliance with laws, regulations, contracts, and grants" detracts from the usefulness of the compliance report. Most readers of a report with both a disclaimer of opinion and positive/negative assurance statements would find the report confusing in that they appear to be conflicting. We strongly recommend that the disclaimer requirement be deleted.
- 34 This paragraph should be expanded to include the discussion contained on page 11 under Reporting on Internal Controls in the American Institute of Certified Public Accountants publication State and Local Governmental Developments - 1990. Based on our experience, auditors require better guidance than is currently available on identifying internal control categories. Many auditors do not understand that the individual accounting and administrative controls designed to ensure compliance with laws and regulations must be listed in this report. Auditors are currently using terms "general controls" and "specific controls" rather than identifying individual controls such as eligibility or cash management. This is required by Government Auditing Standards.
- 43 We believe that the paragraph should be returned to the way it was previously written. The paragraph properly stated the requirements of the Single Audit Act and OMB Circular A-128. As such, the paragraph was technically correct and should not be altered. However we believe that the new paragraph is also needed as an indication of how to meet the requirements of the Single Audit Act and OMB Circular A-128. Therefore we believe that paragraph 43 should be unchanged with a new paragraph that follows that would indicate how to meet the regulations, which would be the changed version of paragraph 43.
- 45 In the first sentence of this paragraph "supplements" was replaced by "implements". The word "supplements" was correct. Therefore the sentence should be returned to its original form.

- 46 In item "i" the reference in parenthesis should be altered to include item "d". The reference should be as follows:

(In addition to d, f and g above)

- 50 The report expressing positive and negative assurance on compliance should contain a requirement that the auditors identify the general requirements not tested and the reasons for excluding them from testing. Also, the sample report in paragraph 51 should show the general requirements not tested and the reasons for not testing. This clarification is needed because we have been receiving reports without all the general requirements being identified that would generally be applicable to various Federal programs. We concede that not all general requirements apply to all programs, but to determine applicability currently the auditors must be contacted.
- 79 This paragraph should require the basic elements of a finding (condition, cause, criteria, effect, and recommendation) to be included in the report. We receive many single audit reports whose findings do not contain these elements. We have rejected audit reports that had insufficient information in the findings.
- 92 The sentence concerning the audit requirement for nonprofit institutions that receive at least \$25,000 but less than \$100,000 a year in federal awards is inconsistent with Circular A-133. Circular A-133 states that the Federal award audit will be made in accordance with Federal laws and regulations governing the programs in which they participate. It is possible that the laws or regulations governing the programs will not require a program audit and accordingly no audit will be needed. The sentence in this paragraph mandates that an audit be performed, which goes beyond what is required by Circular A-133.
- 93 The paragraph is silent as to the requirement for non-major programs. Paragraph 13(c)(1) of OMB Circular A-133 states "... transactions selected for non-major programs shall be tested for compliance with Federal laws and regulations that apply to such transactions." This requirement should be added to this paragraph.
- 93 The exposure draft is not consistent with Circular A-133. The exposure draft states that compliance with the general requirements (applicable to Federal award programs with specific requirements) that may have a

direct effect on each major program must be tested. Paragraph 13(c)(1) of the attachment to Circular A-133 states that the auditor will determine whether the recipient has complied with the laws and regulations which may have a direct and material effect on any of its major programs. Paragraph 13(c)(6) of the attachment states that the principle compliance requirements may be ascertained by referring to the compliance supplements. The Circular and attachment do not discuss general and specific requirements. We believe the SAS should have a paragraph that reflects the exact wordings of the Circular followed by a paragraph that would indicate how to meet OMB Circular A-133 requirements, which is paragraph 93 of the proposed SAS.

94-95 There are numerous other differences between OMB Circular A-133 and OMB Circular A-128. The differences should be indicated.

96 The second sentence of the first paragraph needs to be changed to indicate that program-specific audits are to be performed in accordance with laws and regulations or in accordance with an agreement from the grantor agency. The audit guide is a supplement to these laws and regulations. There may not be an audit guide for each program-specific audit that is required by the laws and regulations. Further, some audit guides may not be comprehensive of all laws and regulations. This change also should be reflected in the third sentence. Therefore we recommend that this paragraph should be changed as follows:

"Under certain circumstances, the Single Audit Act and OMB Circulars A-128 and A-133 permit certain recipients of federal financial assistance to have a "program specific" audit. Entities not covered by the Single Audit Act or OMB Circular A-133 also may be required to have a program-specific audit. The auditor engaged to conduct a program-specific audit must perform the audit in accordance with the applicable laws and regulations or in accordance with an agreement from the grantor agency. When engaged to conduct a program-specific audit, the auditor should obtain an understanding of the audit requirements for that particular program from the agreement with the grantor agency, from the laws and regulations, or through contact with the grantor agency. Some grantor agencies have prepared program-specific audit guides to provide guidance

in the performance of these audits (such as the U.S. Department of Education's Student Financial Aid Audit Guide, U.S. Department of Agriculture's Multistate Food Processors Audit Guide, and U.S. Department of Housing and Urban Development's Audit Guide for Mortgagors Having HUD Insured or Secretary Held Multifamily Mortgages). The program-specific audit guides are not to be considered laws or regulations. Therefore, there may be additional audit requirements that the auditor may have to perform beyond those required by the audit guides to meet the applicable laws and regulations."

97 This paragraph notes that there may be different responsibilities in a program audit, but does not identify them. Typically in a program specific audit there is more in depth compliance testing and more focussed reporting. Adding this would make the guidance more informative.

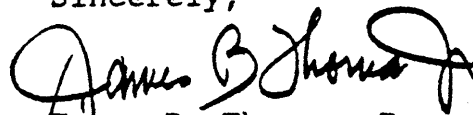
Footnote 9 (page 10) This footnote attempts to clarify the definition of a Federal award by giving a couple of illustrations. However, we believe one of the examples could be misleading as a contract to design and manufacture aircraft normally is a cost type contract and, if awarded to nonprofit, would be a Federal award per OMB Circular A-133.

Append C The no answer to the question "Nonmajor transactions selected in F.S. or control work?" is correct only when there are major programs.

General OMB is soon to release a bulletin titled "Guidance on Audit Requirements for Federal Financial Statements". The bulletin will establish auditing requirements for the auditing of Federal financial statements. We believe that the AICPA should consider this bulletin in the finalization of this SAS.

We appreciate the opportunity to comment. If you have any questions, please contact Russell Young at (202) 732-4070.

Sincerely,


James B. Thomas, Jr.
Chair