



Implementing the New Yellow Book

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- Jerry is an Assistant Director for the State of Tennessee, Comptroller of the Treasury, Division of Local Government Audit. The division has statutory responsibility for audits of approximately 1600 local governments and related organizations in Tennessee. Many of these governments are subject to the Single Audit Act and OMB's Uniform Guidance.
- A 35-year veteran of the division, Jerry has served as an auditor, audit supervisor, training instructor, technical manager, and assistant director. Jerry is a Certified Public Accountant (CPA), Certified Government Financial Manager (CGFM), and a Certified Fraud Examiner (CFE). In his role as assistant director, he is responsible for developing professional compliance procedures and monitoring the division's quality performance under GASB, AICPA, OMB, and GAO accounting and auditing standards. Jerry also has responsibility for supervising the contract review process within the division. Most recently, Jerry assisted the division in implementing GASB Statements 74 and 75. In addition, Jerry teaches the Yellow Book and Audit Findings training classes for the Tennessee Department of Audit. Jerry has been selected as Department of Audit Instructor of the Year four times. Jerry was selected for the AGA National Educator award for 2019.
- Jerry has made training presentations for several other professional organizations including the Tennessee Society of Certified Public Accountants; Mississippi Society of Certified Public Accountants, Missouri Society of Certified Public Accountants, Alabama Society of Certified Public Accountants, Tennessee Government Finance Officers Association; National Association of State Auditors, Comptrollers and Treasurers; Association of Government Accountants; County Technical Assistance Service; Southeastern Intergovernmental Audit Forums; Nashville Chapter of the Association of Certified Fraud Examiners; and various county official's associations. Jerry currently serves on GFOA's CAAFR Committee, NASACT's Financial Management and Intergovernmental Affairs Committee, and NSAA's Audit Standards and Reporting Committee and Single Audit Committee. He has served the National State Auditors Association External Peer Review program as a reviewer, team leader, and concurring reviewer and has served on the Special Review Committee for GFOA's Certificate of Achievement for Excellence in Financial Reporting program. Jerry has also provided training for the New York City Comptroller's Office and state auditors and administrative offices in Arkansas, Idaho, Kentucky, Minnesota, Mississippi, North Dakota, Montana, West Virginia, and North Carolina. In addition to these duties, Jerry currently serves on the state's Interagency Cash Flow Committee which operates under the authority of the Tennessee State Funding Board.
- Jerry was a partner in the accounting firm of Crosthwaite Durham and Associates. He also served as controller for Rural Healthcare of America, Inc., and taught accounting as a member of the adjunct faculty for Columbia State Community College and Austin Peay State University.
- Jerry received his accounting degree from the University of Tennessee at Martin. He is a member of the American Institute of Certified Public Accountants (AICPA); the Association of Government Accountants (AGA) and the Nashville Chapter where he served as chair of the CGFM committee; the Government Finance Officer's Association (GFOA) and the Tennessee Government Finance Officers Association (TGFOA) where he serves as state liaison to the Board of Directors; the Association of Certified Fraud Examiners (ACFE) and the Nashville Chapter of ACFE. Jerry is also a graduate from the Tennessee Government Executive Institute (TGEI) which is a training program for government leaders through the University of Tennessee.
- Jerry is married and has three children and four grandchildren.

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First Disclaimer

The Opinions expressed during this presentation are my own. They do not necessarily represent the views of the Tennessee Comptroller of the Treasury, his representatives, or the Tennessee Department of Audit.

GAO's Government Auditing Standards

- Just a personal thought from me as we begin:
 - There are more and more standards that must be followed by auditors.
 - Sometimes the overload creates ethical dilemmas for auditors.
 - I don't have time. I will be over my time budget.
 - We've always audited this way and its been OK up until now.
 - Who will notice. Our quality control is not that great anyway.
 - It is unlikely peer review will pick this audit.
 - If I write this finding, I will probably lose this client.
 - Independence does not apply to my situation.

Government Auditing Standards -1972

54 Pages



STANDARDS FOR AUDIT OF GOVERNMENTAL ORGANIZATIONS, PROGRAMS, ACTIVITIES & FUNCTIONS

BY THE COMPTROLLER GENERAL
OF THE UNITED STATES
1972

Government Auditing Standards -1972

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GAO Top Twelve



Summary of Key Changes from 2011 Revision

- Internal control: financial audits and examination engagements
- Internal control: performance audits
- New considerations for addressing waste
- Standards for reviews of financial statements
- Management assertions

GAO's Government Auditing Standards

- What I consider as the most important changes:
 1. New format and organization of GAGAS
 2. Independence threats related to preparing records and financial statements
 3. Documenting SKE (application guidance)
 4. Changes to Waste and Abuse (definition of waste, and reporting of waste and abuse)
 5. Quality Control
 6. Internal Control requirements and reporting for Financial Audits.

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- What I consider as the most important changes:
 7. Peer review requirements
 8. Internal control: financial audits, examination engagements, and **performance audits**. Should consider internal control when determining the cause of findings.
 - a. (2011 YB referred to Internal Controls 142 times, the 2018 YB refers to Internal Controls 202 times)

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- **Application Guidance (Cont'd):**
 - **2.09** The application guidance provides further explanation of the requirements and guidance for applying them. In particular, it may explain more precisely what a requirement means or is intended to address or include examples of procedures that may be appropriate in the circumstances. Although such guidance does not in itself impose a requirement, it is relevant to the proper application of the requirements. “May,” “might,” and “could” are used to describe these actions and procedures. The application guidance may also provide background information on matters addressed in GAGAS.

Chapter 6, 7, and 8

Internal Controls

#1 Implementation Issue

Internal Control: Performance Audits (cont.)

Internal control significant to audit objectives = Yes

- Obtain an understanding of internal control that is significant to the audit objectives (para. 8.40).
- Assess and document the assessment of internal control to the extent necessary to address the audit objectives (para. 8.49).
- Evaluate and document the significance of identified internal control deficiencies within the context of the audit objectives (para. 8.54).
- Consider internal control deficiencies when developing the cause element of findings (para. 8.117).
- Identify in the audit report which internal control components and principles are significant (para. 9.30).

Yellow Book vs. AICPA Performance Standards

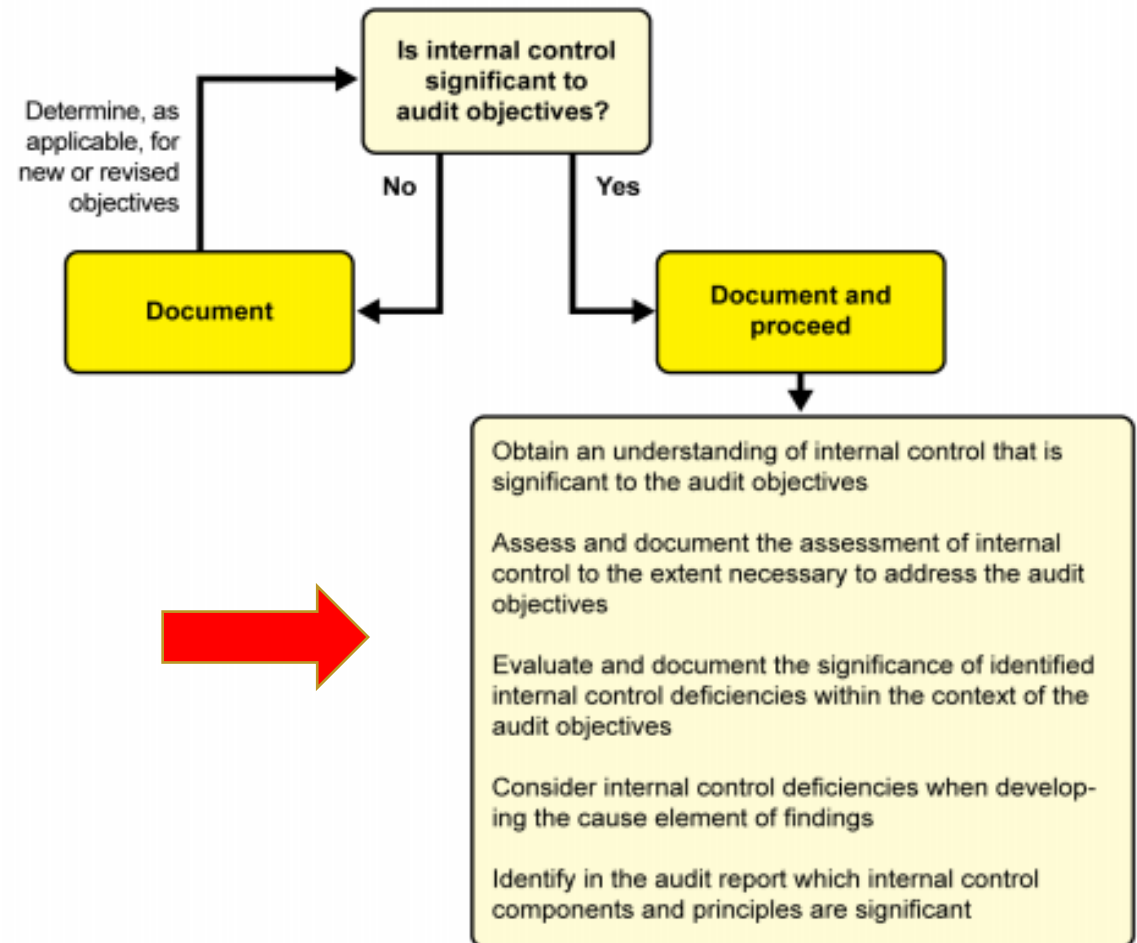
- Keep in mind that the Yellow Book Performance Audit standards are the standards for performance audits.
- Yellow Book Performance Audit Standards do not incorporate by reference AICPA (Auditing Standards Board) standards, because they do not exist.

Chapter 8

Implementation Issues:

- **July 1, 2019 applicability**
- Training, Training, and More Training
See Chart →
- Include Consideration Internal Controls in Audit Report
- Specifically state that the Audit did not include all internal control components

Figure 4: Consideration of Internal Control in a Generally Accepted Government Auditing Standards Performance Audit



Source: GAO. | GAO-18-568G

Chapter 8

- **Fieldwork Standards for Performance Audits**

- Chapter 8: Fieldwork Standards for Performance Audits Guidance is revised to further explain that management assertions are not required when conducting a performance audit in accordance with GAGAS. (para. 8.14)
- If internal control is determined to be significant to the audit objectives, auditors should assess and document their assessment of the design, implementation, and/or operating effectiveness of such internal control to the extent necessary to address the audit objectives. (8.49) **Test Internal Controls??**
- Internal control requirements and guidance are updated to align with the revised **Standards for Internal Control in the Federal Government and Internal Control – Integrated Framework**. (paras. 8.38 through 8.67) (e.g. 8.130)
- Standard is expanded to require that auditors **consider potential internal control deficiencies in their evaluation of identified findings** when developing the cause element of the identified findings. (para. 8.38-8.67)

Chapter 9

- **Reporting Standards for Performance Audits**

- Reporting Standards for Performance Audits Standard is revised to require that audit organizations that meet the independence requirements for internal auditors include in the GAGAS compliance statement, where applicable, **a statement that they are independent per the GAGAS requirements for internal auditors.** (para. 9.03)
- Standard is expanded to require that when internal control is significant within the context of the audit objectives, **auditors include in the audit report discussion of how the auditors considered the concept of accountability for use of public resources and government authority while assessing audit risk associated with internal control.** (para. 9.29-31)
- Standard is expanded to require that auditors **indicate in their report that the audit did not consider all internal control components if internal control that is significant to the audit objectives does not include all internal control components and underlying principles.** (para. 9.30)

Chapter 3

Independence (Nonaudit Services) #2 Implementation Issue

Chapter 3

- Chapter 3 – Ethics, Independence, and Professional Judgment
- 3.30 Auditors should evaluate the following broad categories of threats to independence when applying the GAGAS conceptual framework:
 - **Self-interest threat:** The threat that a financial or other interest will inappropriately influence an auditor's judgment or behavior.
 - **Self-review threat:** The threat that an auditor or audit organization that has provided nonaudit services will not appropriately evaluate the results of previous judgments made or services provided as part of the nonaudit services when forming a judgment significant to a GAGAS engagement.
 - **Bias threat:** The threat that an auditor will, as a result of political, ideological, social, or other convictions, take a position that is not objective.
 - **Familiarity threat:** The threat that aspects of a relationship with management or personnel of an audited entity, such as a close or long relationship, or that of an immediate or close family member, will lead an auditor to take a position that is not objective.

Chapter 3

- Chapter 3 – Ethics, Independence, and Professional Judgment
- 3.30 Auditors should evaluate the following broad categories of threats to independence when applying the GAGAS conceptual framework:
 - **Undue influence threat:** The threat that influences or pressures from sources external to the audit organization will affect an auditor's ability to make objective judgments.
 - **Management participation threat:** The threat that results from an auditor's taking on the role of management or otherwise performing management functions on behalf of the audited entity, which will lead an auditor to take a position that is not objective.
 - **Structural threat:** The threat that an audit organization's placement within a government entity, in combination with the structure of the government entity being audited, will affect the audit organization's ability to perform work and report results objectively.

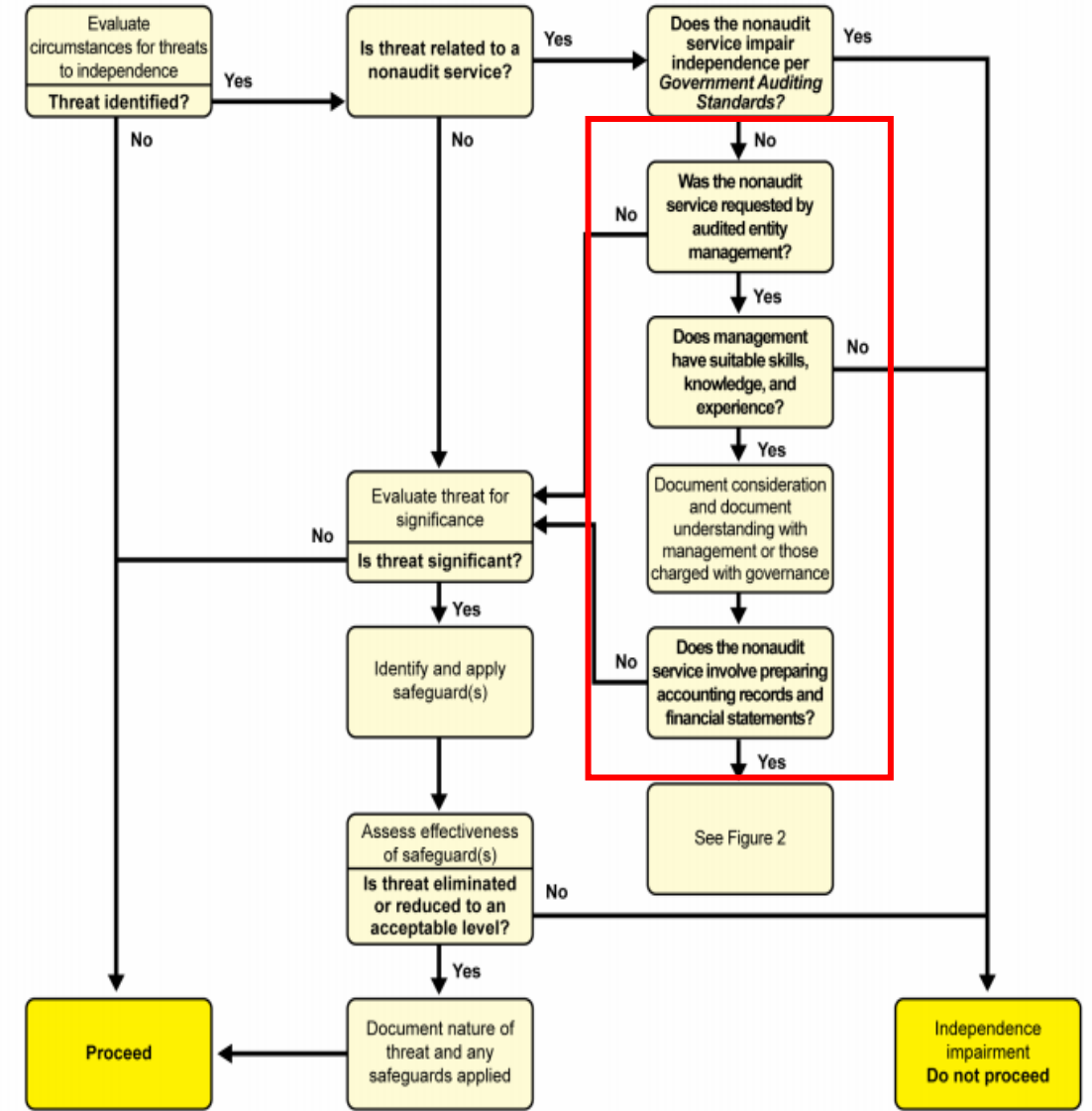
New Conceptual Framework - Independence

Engagement Acceptance and Continuance:

- Engagement Letter
- Determine SKE
- Document All of the above.



Figure 1: Generally Accepted Government Auditing Standards Conceptual Framework for Independence



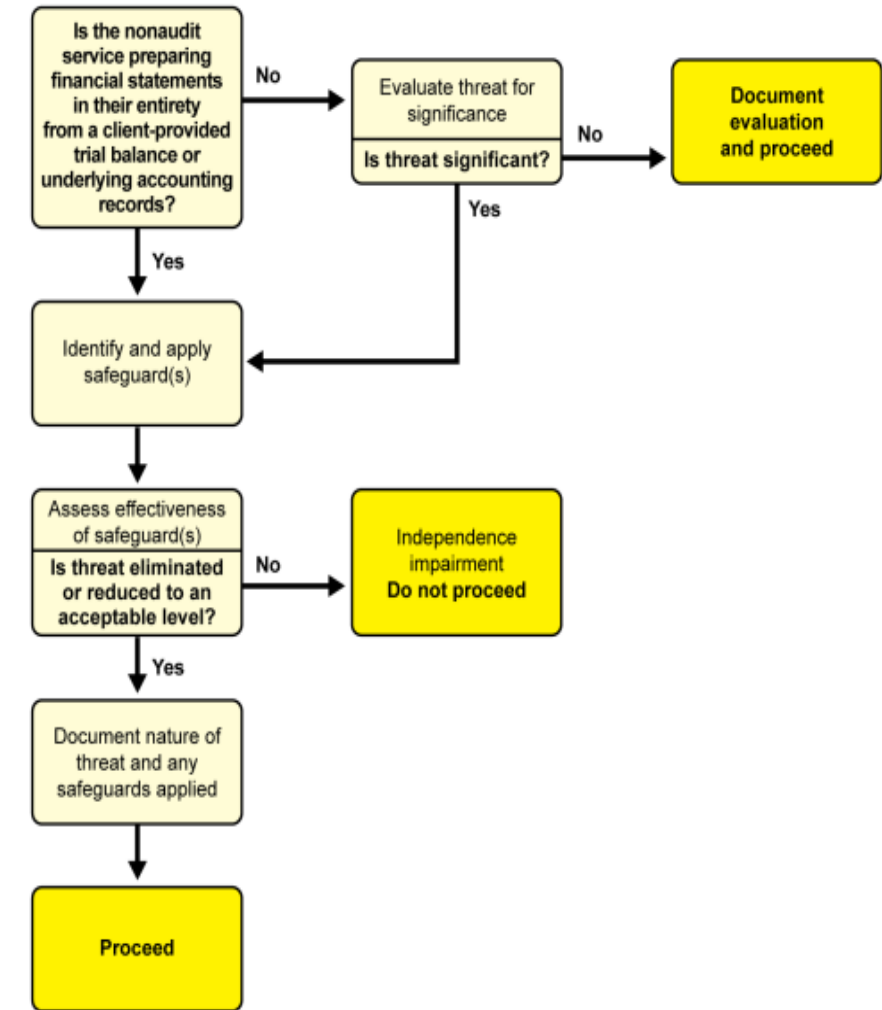
Source: GAO. | GAO-18-568G

New Conceptual Framework – Financial Statement Preparation

We prepare financial statements from a trial balance:

- We use an independence checklist that mirrors the conceptual framework
- We document a significant risk
- We document the safeguards applied – Review by those that did not perform the Audit
- We perform training
- We document in detail how we determined that the client accepted responsibility for our nonaudit services

Figure 2: Independence Considerations for Preparing Accounting Records and Financial Statements



Source: GAO. | GAO-18-568G

Chapter 3

- **Application Guidance: Management Responsibilities**
- **3.79** A critical component of determining whether a threat to independence exists is consideration of management's ability to effectively oversee the nonaudit service to be provided. Although the responsible individual in management is required to have sufficient expertise to oversee the nonaudit services, management **is not required to possess the expertise to perform or re-perform the services. However, indicators of management's ability to effectively oversee the nonaudit service include management's ability to determine the reasonableness of the results of the nonaudit services provided and to recognize a material error, omission, or misstatement in the results of the nonaudit services provided.**

Chapter 5

Quality Control

#3 Implementation Issue

Quality Control

New specific requirements for quality control related to:




- Annual independence affirmation (para. 5.09),
- Undertaking engagements only if the audit organization has the capabilities, including time and resources, to do so (para. 5.12),
- Consultation on difficult or contentious issues (para. 5.24),
- Supervision and review of work (para. 5.36), and
- Assigning an engagement partner or director to each engagement (para. 5.37).

Monitoring of Quality

New specific requirements for monitoring of quality related to:

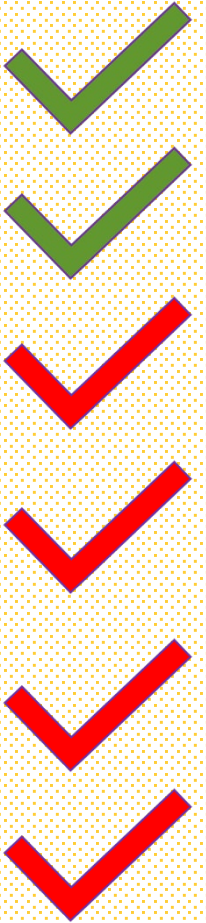
- Communication of monitoring sufficient to enable corrective actions (para. 5.44), and
- Evaluation of deficiencies noted during monitoring (para. 5.45).

Chapter 5

- Chapter 5: Quality Control and Peer Review (from 25 paragraphs to 95 paragraphs)
- Standard is modified to require that audit organizations at least **annually obtain written affirmation** of compliance with policies and procedures on independence from all audit organization personnel required to be independent. (para. 5.09) 
- Standard is expanded to require that audit organizations establish policies and procedures designed to provide reasonable assurance that the audit organization **undertake engagements only** if it has the capabilities to do so. (para. 5.12) 
- Requirements are added and guidance is provided for engagement performance, documentation, and reporting, including requirements for policies and procedures pertaining to the **review and supervision of engagement work** performed by the engagement team. (paras. 5.15 through 5.41) 

Chapter 5

- In particular, the following are discussed:
- The policies and procedures should require that experienced engagement team members review the work of less experienced engagement team members.
- The audit organization should assign responsibility for each engagement to an engagement team partner or director with authority to assume that responsibility. (5.37)
- The audit organization should establish policies and procedures requiring the audit organization to communicate the identity and role of the engagement partner or director to management and those charged with governance of the audited entity. (5.37)
- The audit organization should establish policies and procedures requiring the audit organization to clearly define the responsibilities of the engagement partner or director and communicate them to that individual. (5.37)
- The audit organization should establish policies and procedures designed to provide reasonable assurance that appropriate consultation takes place on contentious issues, sufficient resources are available to enable appropriate consultation, the nature and scope of such consultations are documented and agreed upon, and the conclusions resulting from such consultations are documented and implemented.
- Monitoring, Evaluation, and Corrective Action



Chapter 6, 7, and 8

Waste and Abuse

#4 Implementation Issue

Fraud, Waste, and Abuse



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- **Application Guidance – Definitions for Waste and Abuse**
- 6.21 Waste is the act of using or expending resources carelessly, extravagantly, or to no purpose. Importantly, waste can include activities that do not include abuse and does not necessarily involve a violation of law. Rather, waste relates primarily to mismanagement, inappropriate actions, and inadequate oversight.
- 6.22 The following are examples of waste, depending on the facts and circumstances:
 - a. Making travel choices that are contrary to existing travel policies or are unnecessarily extravagant or expensive. (Intentional?)
 - b. Making procurement or vendor selections that are contrary to existing policies or are unnecessarily extravagant or expensive (Intentional?)
- **Note: These were presented as examples of abuse in the 2011 version**

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- **Application Guidance – Definitions for Waste and Abuse**
- 6.23 Abuse is behavior that is deficient or improper when compared with behavior that a prudent person would consider reasonable and necessary business practice given the facts and circumstances, but excludes fraud and noncompliance with provisions of laws, regulations, contracts, and grant agreements. Abuse also includes misuse of authority or position for personal financial interests or those of an immediate or close family member or business associate.
- 6.24 The following are examples of abuse, depending on the facts and circumstances:

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- **Application Guidance – Definitions for Waste and Abuse**
 - 6.24 The following are examples of **abuse**, depending on the facts and circumstances:
 - Creating unneeded overtime.
 - Requesting staff to perform personal errands or work tasks for a supervisor or manager.
 - Misusing the official's position for personal gain (including actions that could be perceived by an objective third party with knowledge of the relevant information as improperly benefiting an official's personal financial interests or those of an immediate or close family member; a general partner; an organization for which the official serves as an officer, director, trustee, or employee; or an organization with which the official is negotiating concerning future employment).
- **Note: These were presented as examples of abuse in the 2011 version.**

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- **Application Guidance - Reporting Waste and Abuse**
- 6.20 Given the concept of accountability for use of public resources and government authority, evaluating internal control in a government environment may also include considering internal control deficiencies that result in waste or abuse. **Because the determination of waste and abuse is subjective, auditors are not required to perform specific procedures to detect waste or abuse in financial audits. However, auditors may consider whether and how to communicate such matters if they become aware of them.** Auditors may also discover that waste or abuse are indicative of fraud or noncompliance with provisions of laws, regulations, contracts, and grant agreements.

Implementation Dates

- Financial Audits, Attestation Engagements, Reviews for the period ending on or after June 30, 2020. (Planning must take place now!)
- Performance Audits beginning on or after July 1, 2019. Right Now!
- Early implementation is NOT permitted.

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Questions

