






Avoiding Common Deficiencies in Yellow Book and Single Audits

A Governmental Audit Quality Center Web Event
March 22, 2016

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Presenters

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What We Will Cover

- Common Deficiencies in Single Audits and Audits Performed under *Government Auditing Standards* (Yellow Book)
- Top Areas that Auditors Need to Get Right to Avoid Quality Issues
- Preparing for the Next Single Audit Quality Study
- AICPA Enhancing Audit Quality Initiatives
- Resources

But First.....Why Should These Audits be a Focus Area for Auditors?

- Single audits are a “risky” business
- Regulator and other scrutiny
 - Quality Control Reviews (QCRs) and Desk Reviews of auditors
 - Single audits are a “must select” area in peer review
 - Ongoing federal oversight of non-federal auditees
- Implementation of the [Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards](#) at 2 CFR 200 (UG or Uniform Guidance)
- Historical evidence shows audit quality issues
- Future periodic study of audit quality required by UG

Common Single Audit and Yellow Book Deficiencies



- [AICPA Professional Ethics, Most Frequent Violations of Professional Standards: Government and Not-for-Profit Investigations](#)
- [AICPA Peer Review Program, Annual Report on Oversight](#) (see page 52 of report)

Failed to Accurately Identify and/or Test all Major Programs

| | | |
|---|---|----------------------------|
| Failure to combine same CFDA#s as one program for major program determination and testing | Clusters not treated as one program for major program determination and testing | Type A threshold incorrect |
| Failure to consider effect of large loans on Type A Threshold | Failed to meet % of coverage requirement | |

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Incorrectly Identified Auditee as a Low-Risk Auditee When One of More of Following Occurred

| | |
|--|---|
| Data Collected Form (DCF) not filed or filed late | Opinion on financial statements or Schedule of Expenditures of Federal Awards (SEFA) was modified |
| Material weaknesses in internal control (IC) over financial reporting or compliance were noted | Material noncompliance on major federal program(s) was reported |

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Internal Control over Compliance and Compliance Testing Problematic

| | | |
|--|---|--|
| Compliance requirements documented as applicable, but no testing performed | Use of out-of-date work programs | Improper application of dual purpose testing |
| Lack of understanding of difference between IC and compliance testing | Inappropriate and/or unsupported sample sizes | Lack of testing of IC over direct and material compliance requirements |

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Documentation Issues

| | |
|---|---|
| Type A or B risk assessment documentation missing or inadequate | No documentation of fraud risk regarding noncompliance for major programs |
| Failure to perform or document analytical procedures in the planning and/or final stages of audit | Failure to utilize or customize an audit program |

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Reporting Issues

| | |
|---|--|
| Auditor's reports did not include all required elements | Auditor did not properly date the report(s) |
| Inconsistency in reporting of findings between the Schedule of Findings and Questioned Costs (SFQC) and the reports | Other reporting issues such as outdated wording and failure to correctly opine on prior year information |

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Yellow Book Issues

| | |
|---|-----------------------------------|
| Engagement team did not meet CPE requirements | Independence documentation issues |
| Failed to meet YB peer review requirements | |

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Top Areas that Auditors Need to Get Right to Avoid Audit Quality Issues

What Auditors Must Get Right

-  Yellow Book Independence Evaluation and Documentation
Engagement Team Selection
Acceptance and Continuance of Single Audit Engagements
-  Major Program Determination, Percentage of Coverage, SEFA
IC Over Compliance and Compliance Testing (Including Sampling)
Documentation, Documentation, Documentation
-  Correct Reporting
Correct Reporting of Audit Findings in Both Single Audit Reporting and the DCF

Planning - Yellow Book Independence Evaluation and Documentation

- **Identify** nonaudit services
- ✓ **Meet preconditions**
- ✓ **Evaluate and document** Skills Knowledge and Experience (SKE) of management
- **Assess threats**
 - Consider individually and in the aggregate
- **Document consideration of significant threats**
- **Document your understanding of non-audit services with the auditee**
- ✓ **Apply safeguards when significant threats exist**

No SKE = No Independence

You can't
safeguard
your way out
of no SKE

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Planning – Engagement Team Selection

Ensure all members of the team meet YB CPE requirements

Experience and competency of engagement team members

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Planning – Acceptance and Continuance

- Firm's quality control (QC) policies and procedures should provide reasonable assurance that it will undertake or continue relationships and engagements only where it is competent to perform the engagement and has the capabilities, including the time and resources, to do so
- Key policies include:
 - Evaluating whether the engagement can be completed with professional competence;
 - Undertaking only those engagements for which the firm has the capabilities, resources, and professional competence to complete; and
 - Evaluating, at the end of specific periods or upon occurrence of certain events, whether the relationship should be continued.

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Planning - Acceptance and Continuance

Objective: Only undertake engagements when appropriate



QC Procedures

- Document communications with prior auditors
- Document relevant information before accepting or continuing client relationship
- Document services to be performed
- Procedures for withdrawal from an engagement
- Document the fact that the firm possesses the expertise and knowledge to perform the engagement

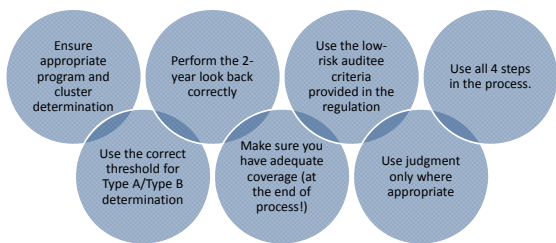
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Performing - SEFA Requirements

- Remember....first and foremost the SEFA is a client responsibility!
- From auditor perspective:
 - Ensure familiar with changes to the SEFA as a result of the Uniform Guidance
 - Are clusters and programs identified correctly? This is key!
 - Determine whether information required on the face of SEFA is there and that all required disclosures included
 - Reconciliation of SEFA amounts to financial records

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Performing – Major Program Determination



- Ensure appropriate program and cluster determination
- Perform the 2-year look back correctly
- Use the low-risk auditee criteria provided in the regulation
- Use all 4 steps in the process.
- Use the correct threshold for Type A/Type B determination
- Make sure you have adequate coverage (at the end of process!)
- Use judgment only where appropriate

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Performing - Understanding and Testing Internal Control

- Use COSO/GAO's Green Book
- Test of design and implementation AND test of effectiveness
- Need evidence of who, when, what
- Evaluate results of test of controls on tests of compliance
- Control must be effective or you should have a finding!

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Performing - Compliance Testing

- Use all parts of *Compliance Supplement* for a correct Single Audit
 - 2: Matrix of Compliance Requirements
 - 3.1 and 3.2: Compliance Requirements for audits performed under A-133 and under Uniform Guidance – **USE CORRECT PART 3**
 - 4: Agency Program Requirements
 - 5: Clusters of Programs
 - 6: Internal Control – **NOT INCLUDED IN 2015 SUPPLEMENT AND UNSURE WHETHER WILL APPEAR IN 2016**
 - 7: Guidance for Auditing Programs not Included in the Supplement
- Don't forget Appendices
- Use the correct year's Supplement

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Performing – I/C and Compliance

- Complete full circle on risk of material noncompliance
 - Identify, Assess, Respond, Evaluate
- The risk assessment process is not complete until the audit report is issued!
- Internal controls should be continually reevaluated throughout the audit process
- Understand the difference between control vs. compliance
 - Controls: What did entity do to ensure compliance?
 - Compliance: Did entity comply?
- Testing compliance gives indirect evidence on controls, but cannot serve as the basis for assessing controls as operating effectively

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Performing - Ensure Understanding of Sampling

- Access more detailed [GAQC Sampling Web event](#)
- Ensure sample sizes appropriate
- Appropriate documentation
- Watch out for dual purpose sampling

■ Tests of Controls

- Provide evidence about the effectiveness of the design, implementation, or operation of controls and policies in preventing or detecting material noncompliance.
- **Concern: Rates** of deviations from a prescribed control.

■ Tests of Compliance

- Provide evidence about an auditee's ability to adhere to the direct and material compliance requirements of its major programs.
- **Concern: Rates** and potential **magnitude** of noncompliance.

Performing - Documentation

If it was not documented it was not done!
Key areas of documentation include:

| | | | | |
|---|---|--|--|---------------------|
| Materiality levels and basis for how determined | Major program determination – including individual program risk assessments | Understanding and testing of I/C over compliance | Compliance testing and support for sampling used | Overall Conclusions |
|---|---|--|--|---------------------|

Performing – Documentation

■ I/C and Compliance Documentation Best Practices

- Documenting an understanding of I/C over compliance that addresses the five elements of COSO
- Documentation supporting the operating effectiveness of controls **and** that controls have been implemented
- Documenting evidence of who, when, what
- Documentation that indicates the use of a combination of procedures (versus inquiry alone)
- When using dual-purpose sampling, a clear distinction between the compliance test versus the controls test
- Documentation of the evidence that supports results of test of controls including:
 - Understanding of deviation and consequences
 - Assessment of the deviation and proper reporting
 - Assessment of the impact on tests of compliance

Reporting – Audit Reports

- Reports must use up-to-date language and include all appropriate references to *Government Auditing Standards, Uniform Guidance, Compliance Supplement, etc.*
 - Use illustrative audit reports provided in the AICPA Audit Guide, *Government Auditing Standards and Single Audits*
- Report on compliance and I/C over compliance refers to major programs in the Summary of Auditor Results in SFQC
 - Ensure major programs in Summary of Auditor Results correct and matches what is in audit documentation!
 - Ensure DCF identifies same major programs!

Reporting – Correctly Reporting Findings

Key Point
Audit reports = SFQC = DCF = Documentation

- Ensure single audit report on compliance and I/C over compliance appropriately identifies I/C findings
 - Do not report significant deficiencies or material weaknesses in the management letter in lieu of putting them in your audit report
- Include all required finding elements in your findings write-ups (see next slide)
- Do not ignore reporting findings that were “corrected” later in the year of audit

Reporting - Uniform Guidance Finding Elements



Reporting - Tips to Avoid DCF Errors

- Errors in the DCF can lead to federal quality reviews
- Review DCF thoroughly before it is submitted
- Avoid these common specific issues (some broadly discussed previously)
 - DCF doesn't indicate some or all of the programs in a cluster were audited as major
 - All lines on DCF with same CFDA # not marked as audited as major
 - Type A/B threshold on DCF doesn't match threshold in SFQC
 - Amounts on DCF do not agree with SEFA
 - Inconsistency between federal awards and audit findings tabs
 - Identifies that a program-specific audit was performed when a single audit was performed

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Preparing for the Upcoming Single Audit Quality Study

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Single Audit Quality Study

UG §200.513(a)(3)(ii)

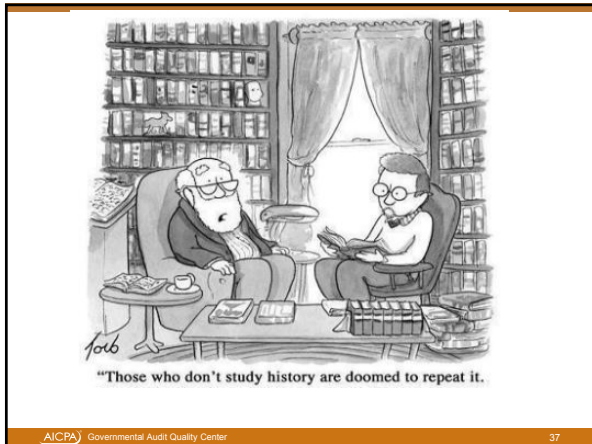
UG requirement for a federal study of quality once every 6 years beginning in 2018

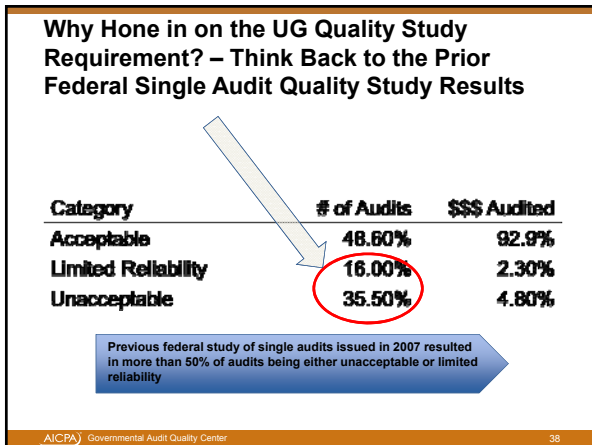
Statistically reliable estimate of the extent that single audits conform to applicable requirements, standards, and procedures

Results of reviews must be made public

Start out on the right foot with UG and all of its requirements

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- ### What Should Auditors be Doing?
- Ensure understanding of UG effective dates and requirements
 - Focus QC systems on areas that the prior quality study showed to be problematic (see last section of this presentation):
 - Major program determination
 - Understanding and testing internal control
 - Use of *Compliance Supplement* and compliance testing
 - SEFA requirements
 - Ensuring adequate audit documentation
 - Single audit reporting
 - Writing findings
 - DCF requirements
 - Pay attention to deficiency listings from AICPA Peer Review and Ethics teams (see earlier slide)
 - Use your GAQC membership and refer to its resources!

What Should Auditors be Doing?

- Obtain appropriate CPE each year and ensure competency
 - New [competency framework](#) and assessment tool relevant to single audits offered at [AICPA Competency and Learning Web site](#)
 - Exam-based single audit certificate program coming soon! Learn more!
- Utilize various checklists to assist in reviewing single audit engagements (e.g., [peer review checklists](#) or federal quality checklists)
- Proactively review your firm's DCF submissions in the FAC

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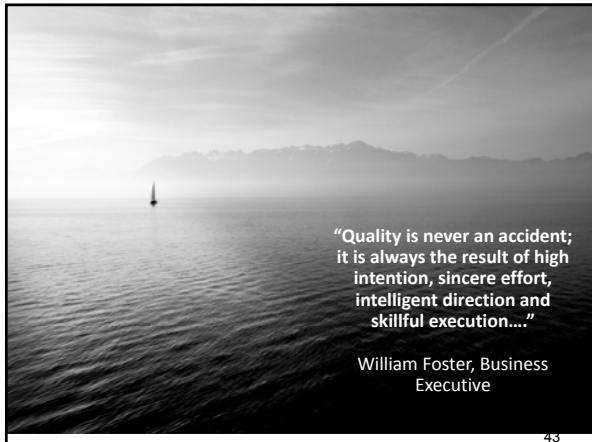
What Should Auditors be Doing?

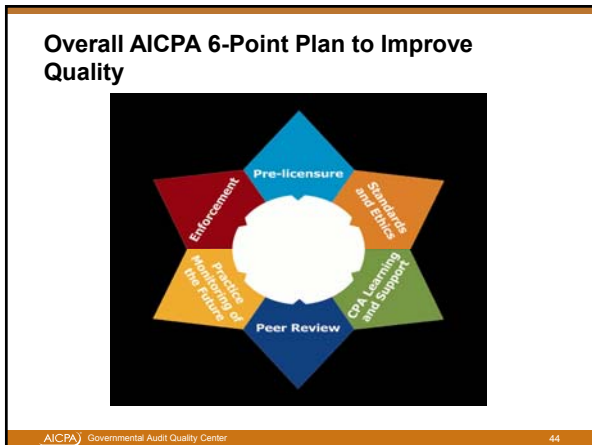
- Select an adequate cross-section of governmental audits for Engagement Quality Control Review
- Select a peer reviewer that has adequate experience and knowledge in the type of governmental engagements your firm performs

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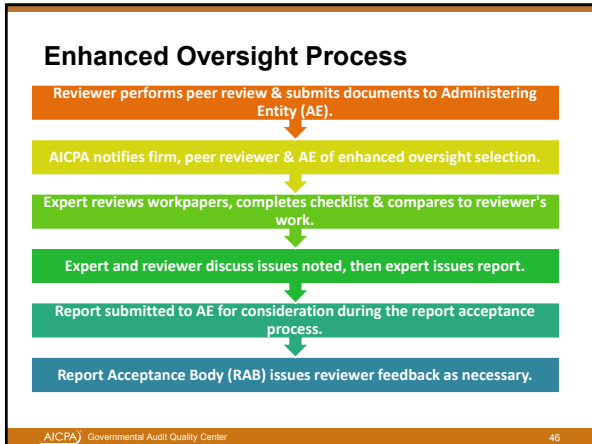
Enhancing Audit Quality Initiatives at AICPA

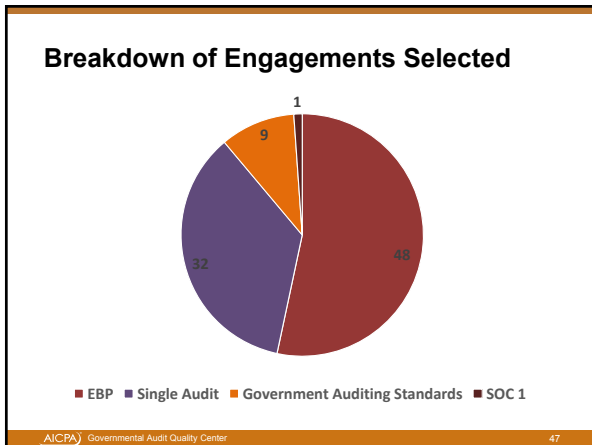
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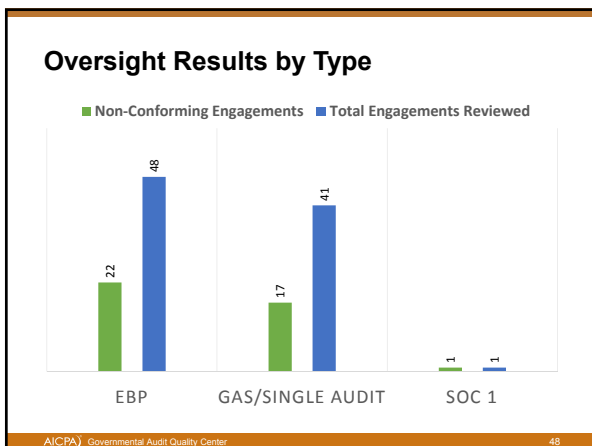


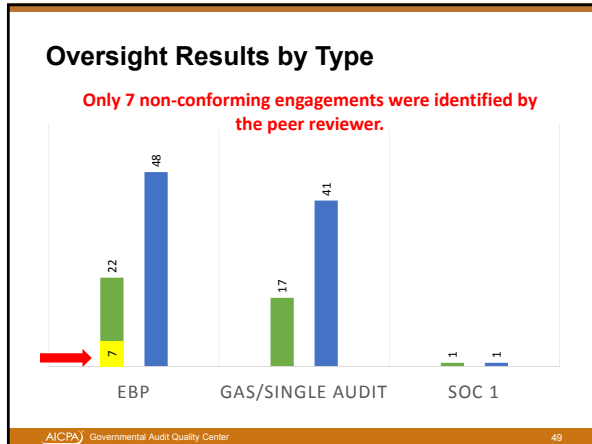


- ### Enhancing Peer Reviewer Quality
- **Expand oversights with experts to review engagements and firms**
 - Review audit engagements and firms prior to report acceptance
 - Better measure how system is working
 - Facilitate prevention of undetected deficiencies
 - **Increase initial and ongoing training**
 - Team captains
 - Reviewers of high-risk and regulated industries
 - Includes competency assessment
 - **Streamline removal of ineffective reviewers**
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- ### Strengthening Firm Quality – Areas of Focus
- Current peer review areas of focus include:
 - Independence (non-attest services and appropriate evaluation of client SKE)
 - Single audits
 - Audits of governmental entities that issue municipal securities
 - Sufficiency of audit evidence - sampling, risk assessment, and internal controls
 - Employee Benefit Plans, including Employee Stock Ownership Plans and government plans
 - Crowdfunding
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- ### Strengthening Firm Quality
- Evaluate “new” engagements promptly
 - Audits in high-risk industries
 - Performed outside of peer review year
 - Require pre-issuance or post-issuance review in instances of non-conformity
 - Identify deficient audits through the FAC
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Population Completeness

- Updated peer review scheduling and enrollment forms
- Continue to explore publicly available databases
- Confirmed ability to obtain Employee Identification Numbers (EINs) for:
 - Single audits
 - Employee benefit plan audits
 - U.S. Department of Housing and Urban Development (HUD) engagements

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Complete Engagement Listing

- Enhanced warning to firms
- Revised representation letter
- Material misrepresentation consequences
 - Report recalled (with state board notification)
 - Hearing panels determine outcome
 - Re-enrollment subject to second hearing panel
 - Individual referral to Ethics
- Use publicly available databases

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Accelerated Remediation Process

- Effective January 1, 2015
- **Mandatory assessment** to hearing panel for two consecutive non-pass reports
- **Presumptively mandatory referral** for two consecutive fail reports OR pass with deficiency to fail reports
- **Mandatory referral** to hearing panel for three consecutive non-pass reports

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Why Should We Care About Quality Control?

- **AICPA is seeing significant quality issues**
- **The effectiveness of the quality control system directly impacts the quality of the work product**
 - Similar to internal controls over financial reporting
 - Better quality controls help mitigate risks
- **It's required!**
 - Statements on Quality Control Standards (SQCS) No. 8—The firm *must* establish a system of quality control
 - Applies to accounting and auditing practices of all CPA firms
- **Starting in 2016—enhanced Quality Control focus in peer review**

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Establishing and Maintaining a System of Quality Control for a CPA Firm's Accounting and Auditing Practice

- **Two versions of practice aid prepared by the Quality Control Standards Task Force**
 - Small and Medium-Sized Firms
 - Sole Practitioner
- **Practice aids have been revised to :**
 - make the illustrative policies and procedures more applicable to a wider range of firms
 - make the illustrative policies and procedures more easily customizable for practitioners
 - include tips, warnings and notes to help practitioners better implement the policies and procedures

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Establishing and Maintaining a System of Quality Control for a CPA Firm's Accounting and Auditing Practice

- **Tips, warnings and reminders**
 - Developed by the task force based on years of experience as peer reviewers and partners responsible for their firms' system of quality control.
 - Take the time to read them – they provide insightful and practical advice.
- **Practice aids include references to resources offered by the AICPA at no charge to assist practitioners in enhancing engagement quality and improving efficiency.**
- **Expected to be available July 2016**

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Questions/Discussion

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Resources

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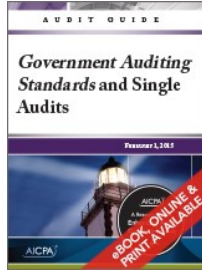
Access Auditing Standards of AICPA and GAO

- **AICPA Auditing Standards**
 - A&A hotline - <http://apps.aicpa.org/technicalhotline/form.asp> or 877.242.7212
- **Government Auditing Standards**

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AICPA Audit Guide: Government Auditing Standards and Single Audits

- Updated for Uniform Guidance
- Covers internal control over financial reporting in *Government Auditing Standards* section
- Includes chapters on internal control over compliance and sampling
- Purchase from www.cpa2biz.com
- 2016 Update expected this summer



Other Relevant AICPA Guides for Financial Statement Audits

- AICPA Audit and Accounting Guide, *State and Local Governments*
 - AICPA Audit and Accounting Guide, *Not-for-Profit Entities*
 - AICPA Audit and Accounting Guide, *Health Care Entities*
- All three of above Guides can be ordered at www.cpa2biz.com

AICPA 2011 Yellow Book Independence - Nonaudit Services Documentation Practice Aid



- **Flat PDF Version.** Free to AICPA members, including GAQC members;
- **For Sale Version.** Designed for Auditor Documentation Input and available for a small fee.
- Can be saved and included as part of auditor's documentation

AICPA - Ethics

- Updated AICPA — Yellow Book (GAGAS) [Independence Rules Comparison](#)
- [AICPA Professional Ethics, Most Frequent Violations of Professional Standards: Government and Not-for-Profit Investigations](#) (Issued April 2015)
- Ethics - ethics@aicpa.org
 - 888.777.7077

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AICPA – Peer Review and QC

- Peer Review - prsupport@aicpa.org or 919-402-4500
 - [AICPA Peer Review Program, Annual Report on Oversight](#)
 - [Archived Peer Review Update Webinar](#)
 - [Archived Sufficiency of Audit Evidence Webinar](#)
- Quality Control
 - [Workshops](#)
 - [Toolkit](#)
 - New virtual group study course

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Key Single Audit-Related Information

- Uniform Guidance codified in [Title 2 of CFR, Subtitle A, Chapter II, Part 200](#)
- How to Access the Uniform Guidance
 - [Electronic Code of Federal Regulations \(e-CFR\)](#) version
- OMB Federal Financial Management Web site
 - OMB [Compliance Supplement](#)
 - Other Uniform Guidance related documents at: http://www.whitehouse.gov/omb/grants_docs
 - [Office of Federal Financial Management Web page](#)
- COFAR guidance including FAQs, archived webcasts, and other information
 - Visit <https://cfo.gov/COFAR/> for all resources
- The DCF and related instructions can be accessed from the [Federal Audit Clearinghouse](#)

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GAQC Archived Uniform Guidance Events

- GAQC archived Web events that may help with the Uniform Guidance
 - [Single Audit Fundamentals Series](#)
 - [Preparing for a Single Audit: An Auditee Perspective](#)
 - [Now is the Time for Auditors to Get Ready for the Uniform Guidance Audit Requirements](#)
 - [Internal Control: COSO, the Green Book, and More](#)
 - [Sampling in a Single Audit Environment](#)

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GAQC Archived Uniform Guidance Events

- GAQC archived Web events that may help with the Uniform Guidance
 - [Uniform Guidance for Federal Awards: The New Cost Principles, Time and Effort Reporting, Procurement and Other Administrative Requirements](#)
 - [Uniform Guidance for Federal Awards: How Clients will Need to Monitor Subrecipients Going Forward](#)
 - [Uniform Guidance for Federal Awards: Auditor Planning Considerations for the New Single Audit Rules](#)
 - [2015 OMB Compliance Supplement and Single Audit Update](#)

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