

2018 Peer Review Conference

Engagements Under *Government Auditing Standards* Must-Select Update FAQs

Most of the questions I get are around tax classes and whether they qualify for Yellow Book CPE. What exactly is required related to the Yellow Book CPE requirement?

Each auditor performing work under *Government Auditing Standards* (GAS) (2011 revision) “Yellow Book” should complete, every two years, at least 80 hours of CPE that “directly enhance the auditor’s professional proficiency to perform audits and/or attestation engagements.” Tax services, in general, are not related to the subject matter of audits performed under Yellow Book, and, accordingly CPE related to tax would not normally qualify as CPE for purposes of satisfying Yellow Book requirements. However, if taxation relates to an objective or the subject matter of an engagement, the training could qualify as CPE under Yellow Book. The audit organization is ultimately responsible for determining whether a subject or topic qualifies as acceptable CPE for its auditors.

Please refer to GAO’s [Guidance on GAGAS Requirements for Continuing Professional Education](#) to learn more about the CPE requirements prescribed by the Yellow Book. (Note: the 2018 revision of the Yellow Book supersedes this 2005 guidance and is effective for financial audits, attestation engagements and reviews of financial statements for periods ending on or after June 30, 2020, and for performance audits beginning on or after July 1, 2019.)

What safeguards are required when significant threats to independence are identified?

The independence section in chapter 3 of the Yellow Book provides examples of safeguards that may be effective, either individually or in combination, under certain circumstances. While the list doesn’t provide safeguards for all circumstances, it provides a starting point for auditors who have identified significant threats to independence and are considering what safeguards could eliminate those threats or reduce them to an acceptable level. Please see paragraphs 3.17-3.19 of the 2011 Yellow Book for examples of safeguards.

Additionally, reviewers are encouraged to consult the AICPA [2011 Yellow Book Independence—Nonaudit Services Documentation Practice Aid](#), Appendix E: “Application of Safeguards,” for a listing of several safeguards that can be implemented. Reviewers are reminded that it is not possible to rely solely on the safeguards that the audited entity has implemented to eliminate significant threats or reduce them to an acceptable level (GAS paragraph 3.18).

To clarify, under the current Yellow Book standards and the 2011 Yellow Book Independence – Nonaudit Services Documentation Practice Aid, the auditor can conclude that there is no financial statement significant threat issue if the client is suitably able to prepare the statements themselves. Will this no longer be the case after the implementation of the new Yellow Book (in other words, a significant threat will be required to be assessed in the above instance)?

Yes. The 2011 Yellow Book did not specifically indicate that financial statement preparation by the auditor in its entirety should be considered a significant threat (though it was presumed); whereas the 2018 Yellow Book will be more specific about the presumptive nature of the threat.

From the *2011 Yellow Book Independence – Nonaudit Services Documentation Practice Aid*: “The Government Accountability Office (GAO) has indicated that financial statement preparation,

except in rare circumstances, should generally be considered a significant threat to independence for which safeguards should be applied and documented.” Peer reviewers should carefully evaluate whether self-review threats have been properly considered if the reviewed firm prepares the audited entity’s financial statements. A situation where it might be reasonable to conclude financial statement preparation is not a significant threat to independence is when the auditor only provides pro-forma financial statements to be completed by the auditee with sufficient SKE to correctly prepare the statements. Please note the revised standards state that auditors should conclude that preparing financial statements in their entirety from a client-provided trial balance or underlying accounting records creates significant threats to auditor’s independence.

Refer to the [June 2018 Reviewer Alert](#) for Yellow Book: Consideration of Financial Statement Preparation as a Significant Threat to Independence.

The 2018 revision clarifies the following requirements for auditors who perform nonaudit services for an audited entity:

- Auditors should conclude that preparing financial statements in their entirety from a client-provided trial balance or underlying accounting records creates significant threats to auditors' independence and should document the threats and safeguards applied to eliminate and reduce threats to an acceptable level or decline to provide the services (GAS par. 3.88).
- Certain other bookkeeping and financial statement preparation activities (for example, preparing certain line items or sections of the financial statements based on information in the trial balance, posting entries that the audited entity’s management has approved to the entity’s trial balance) create threats to independence that an auditor should evaluate to determine whether they are significant, and document the evaluation of the significance of such threats (GAS par. 3.89).

The end of Chapter 3 of the 2018 Yellow Book contains two flowcharts to further illustrate independence requirements and enhance auditor understanding. Please refer to [GAO's Yellow Book Web page](#) for an electronic version of the 2018 Yellow Book and to learn more about the new standard.

Prior to the implementation of the 2018 Yellow Book, justification within the peer review working papers is still expected to address why financial statement preparation was not deemed a significant threat by the auditor. Firms should document on the engagement profile and reviewers should document within the engagement checklist and SRM to reduce uncertainty of this assessment during technical review.

How can a firm have complied with the requirements related to assessing skills, knowledge or experience as required by AICPA if it isn’t documented?

While both the AICPA and Yellow Book require an auditor to assess whether the designated individual who is overseeing the nonattest or nonaudit services possesses suitable skill, knowledge and/or experience (SKE), Yellow Book explicitly requires this assessment to be documented. There is no explicit requirement in the AICPA Code of Professional Conduct that an auditor document the SKE of the individual from the client overseeing the non-attest service. ET sec. 1.295.050 requires that, before performing nonattest services, the member should establish and document in writing his or her understanding with the attest client regarding the following:



- Objectives of the engagement
- Services to be performed
- Client's acceptance of its responsibilities
- Member's responsibilities
- Any limitations of the engagement

While not explicitly required, auditors should consider whether documentation should provide details about the member of management who will oversee non-attest services, that person's SKE and the auditor's assessment of the SKE. Auditors should also consider whether documentation complies with AU-C 230, including documentation of significant findings or issues arising during the audit, the conclusions reached thereon and significant professional judgements.

Reviewers may refer to the [Frequently Asked Questions](#) issued by the AICPA Professional Ethics Division as of July 31, 2017, for more information on nonattest services, as well as the [Nonattest Service Toolkit](#) which provides the auditor an opportunity to document SKE of the individual identified.

Can you comment on not having to perform a risk assessment on Type B programs that do not exceed the \$187,500 threshold?

Risk assessments of Type B programs are not required if there are no low-risk Type A programs. When risk assessments of Type B programs are required, the auditor is only required to perform risk assessments on Type B programs that exceed 25% of the determined Type A threshold. For example, at the minimum Type A threshold of \$750,000, the auditor would not be required to assess risk on small awards where \$187,500 or less (25% of \$750,000) was expended. See the Uniform Guidance §200.518 and the GAS-SA Guide Chapter 8 for the detailed requirements.

Will the outside practitioner or internal pre-issuance reviewer of the financial statements have to meet the Yellow Book CPE requirements?

Auditors assigned to planning, directing, performing field work or reporting under Yellow Book audits or attestation engagements should meet both the 80-hour and the 24-hour CPE requirements. The term "reporting" includes the EQCR process and is defined by GAO as "Determining the report contents and substance of reviewing reports to determine whether the audit objectives have been accomplished and the evidence supports the report's technical content and substance prior to issuance. ***This includes those who review engagement quality prior to issuing the report*** and those signing the report."

Please refer to GAO's [Guidance on GAGAS Requirements for Continuing Professional Education](#) for more information on Yellow Book requirements for CPE.

Are single audits permitted when they are not required under the Uniform Guidance?

Non-federal auditees that expend less than \$750,000 in federal awards are generally exempted from the single audit requirement. While the Uniform Guidance does not explicitly prohibit the use of its audit requirements for entities expending less than \$750,000, reviewers should question why a single audit was performed. If a single audit was performed when it was not required under the Uniform Guidance, the reviewer should consider:

- Auditor's documentation of impact on reporting, procedures, unallowable audit costs to federal funds and future audits
- Applicability of PRP Section 22,100 Part A and B or if modified appropriately



- Implications to the firm's system of quality control
- Engagement meets GAS, but not single audit must-select peer reviewer requirements

Refer to the [June 2018 Reviewer Alert](#) for Compliance Audits Below the Single Audit Threshold.

What if the funder requires a single audit, even if funding is less than \$750,000?

If a funder requires a single audit when funding is less than \$750,00 the auditor should consider the implications as previously noted (appropriately modifying the report and procedures). Alternatively, the auditor could consider discussing whether a different type of engagement could be performed in accordance with Yellow Book, such as an agreed upon procedure or other attestation engagement related to compliance requirements. Uniform Guidance §200.425(c) discusses similar situations that would allow a pass-through entity to charge the cost of agreed-upon-procedures to monitor subrecipients who are exempted from the requirements of the Single Audit Act and Subpart F.

Can a federal awarding agency designate an auditee as "high risk"?

The Uniform Guidance indicates the criteria for a low-risk auditee in §200.520, noting that an auditee that meets all of the stipulated conditions for each of the preceding two audit period must qualify as a low-risk auditee and be eligible for reduced audit coverage in accordance with §200.518 Major program determination. While the Uniform Guidance does not appear to indicate criteria that would allow an agency to designate a non-federal entity as not a low-risk auditee, it does provide that federal agencies, with concurrence of OMB, may identify federal programs that are higher risk. OMB will provide this identification in the compliance supplement (Uniform Guidance §200.519 (c)(2)).

When a practitioner is selected for enhanced oversight, the practitioner is required to submit a complete set of work papers. The cost of having these copied, indexed, and then shipped are currently the practitioner's responsibility. Shouldn't the practitioner be reimbursed for these costs?

We offer to work with firms to find the easiest and most cost-effective way for the firm to provide the working papers. All firms can submit their working papers electronically. For firms who only use paper files, the most cost-effective method would be scanning their files and sending them electronically. We have not offered to reimburse firms for their costs to provide their working papers. We will discuss this issue with our task forces to determine if any further action is necessary.

The definition of a nonconforming engagement continues to expand under peer review standards, isn't this lessening the significance of these engagements on the results of the peer review? How do we distinguish between a truly bad engagement and one that just missed on standard but is still nonconforming?

There is only one definition of nonconforming engagement. A nonconforming engagement is defined as an engagement that is not performed or reported on in conformity with applicable professional standards in all material respects. The severity of issues identified should be reflected in the evaluation of matters. For example, an isolated matter that happens to render the engagement nonconforming would be appropriate to remain on an MFC. While more significant matters may rise to the level of a deficiency or significant deficiency depending on nature, systemic causes, pattern or pervasiveness, including the relative importance of the matters to the quality control system taken as a whole.



Are we required to select both a Yellow Book and an UG engagement?

According to Interpretation No. 63-2, if a firm performs an engagement of an entity subject to GAS and the peer review is intended to meet the requirements of those standards, at least one engagement conducted pursuant to those standards should be selected for review. Additionally, if the engagement selected is of an entity subject to GAS but not subject to the Single Audit Act and the firm performs engagements of entities subject to the Single Audit Act, at least one such engagement should also be selected for review. The review of this additional engagement must evaluate the compliance audit requirements and may exclude those audit procedures strictly related to the audit of the financial statements.