

441 G St. N.W.
Washington, DC 20548

June 17, 2021

Ms. Sherry Hazel
American Institute of Certified Public Accountants
1211 Avenue of the Americas
New York, NY 10036-8775

GAO's Response to the AICPA's Exposure Draft, *Proposed Statement on Auditing Standards – Inquiries of the Predecessor Auditor Regarding Fraud and Noncompliance With Laws and Regulations*, February 2021

Dear Ms. Hazel:

This letter provides GAO's response to the American Institute of Certified Public Accountants' (AICPA) Auditing Standards Board's (ASB) exposure draft, *Proposed Statement on Auditing Standards – Inquiries of the Predecessor Auditor Regarding Fraud and Noncompliance With Laws and Regulations*. GAO provides standards for performing high-quality audits of governmental organizations, programs, activities, and functions and of government assistance received by contractors, nonprofit organizations, and other nongovernmental organizations with competence, integrity, objectivity, and independence.¹ These standards, often referred to as generally accepted government auditing standards (GAGAS), are to be followed when required by law, regulation, agreement, contract, or policy. For financial audits, GAGAS incorporates by reference the AICPA's Statements on Auditing Standards (SAS).

The ASB proposes to amend SAS No. 122, *Statements on Auditing Standards: Clarification and Recodification*, as amended, section 210, *Terms of Engagement* (AU-C section 210). The proposal requires

- an auditor, before accepting an engagement, to inquire of the predecessor auditor (with management approval) about identified or suspected fraud and matters involving noncompliance with laws and regulations (NOCLAR) in engagement acceptance and
- the predecessor auditor to respond fully and timely and to state clearly whether the response is limited.

We support the ASB's proposal and believe that it is in the public interest to require certain actions that facilitate transfer of knowledge of suspected fraud and NOCLAR from a predecessor auditor to an auditor and will assist in the engagement acceptance process.

To improve the clarity of the standard with respect to governmental audit organizations, we suggest that the ASB consider clarifying that in the governmental environment auditors may find it is necessary to obtain authorization from parties in addition to management for inquiries to predecessor auditors about suspected fraud and NOCLAR. Such parties may include those charged with governance or those contracting for or requesting the audit. We believe that our

¹GAO, *Government Auditing Standards: 2018 Revision Technical Update April 2021*, [GAO-21-368G](#) (Washington, D.C.: April 2021).

suggestion will provide a more thorough understanding of required communications for governmental audit organizations.

Thank you for the opportunity to comment on these important issues. If you have questions about this letter or would like to discuss any of the matters it addresses, please contact me at (202) 512-3133 or dalkinj@gao.gov.

Sincerely yours,

A handwritten signature in black ink, appearing to read "James R. Dalkin". The signature is stylized with a large initial "J" and a long horizontal stroke at the end.

James R. Dalkin
Director
Financial Management and Assurance

Enclosure

Enclosure: Responses to Questions Included in the Proposed Statement on Auditing Standards

- 1. Does the respondent agree with the ASB's determination that it is appropriate to retain the requirement for the auditor, prior to accepting an initial audit, including a reaudit engagement, to request management to authorize the predecessor auditor to respond fully to the auditor's inquiries?**

If not, why not, and how would the respondent revise the requirement (for example, by making the procurement of management's agreement a precondition for the auditor to accept the engagement or requiring the auditor to communicate with the predecessor auditor without management's authorization)?

We agree with the Auditing Standards Board's (ASB) proposal to retain the requirement for the auditor, prior to accepting an initial audit or reaudit engagement, to request that management authorize the predecessor auditor to respond fully to the auditor's inquiries. We believe that management not authorizing the predecessor auditor to fully respond to the auditor's inquiries is important information for the auditor to consider during the engagement acceptance process.

To improve the clarity with respect to governmental audit organizations, we suggest that the ASB consider clarifying that in the governmental environment, auditors may find it is necessary to obtain authorization from parties in addition to management for inquiries to predecessor auditors about suspected fraud and noncompliance with laws and regulations (NOCLAR).² Such parties may include, for example, those charged with governance or those contracting for or requesting the audit.³ We suggest that the ASB add to the application guidance a paragraph explaining this distinction, followed by some examples.

- 2. Are the proposed requirements appropriate and complete, including whether it is appropriate to continue to provide an exception that permits the predecessor auditor to decline to respond to the auditor's inquiries due to impending, threatened, or potential litigation; disciplinary proceedings; or other unusual circumstances? If not, please suggest specific revisions to the proposals.**

We believe that the proposed requirements are appropriate and complete. These include whether it is appropriate to continue to provide an exception that permits the predecessor auditor to decline to respond to the auditor's inquiries because of impending, threatened, or potential litigation; disciplinary proceedings; or other unusual circumstances.

In our view, it is in the public interest for the auditor to seek information on identified or suspected fraud and matters involving NOCLAR to help make informed decisions about whether to accept an audit engagement. It is also our view that the predecessor auditor should clearly state when a response is limited when circumstances warrant.

²Management refers to the persons with executive responsibility for the conduct of the entity's operations. For some entities, management includes some or all of those charged with governance, for example, senior executives.

³Those charged with governance refers to those who have the responsibility for overseeing the strategic direction of the entity and obligations related to the accountability of the entity, including overseeing the entity's financial reporting process. Accordingly, for these purposes, those charged with governance are considered part of the entity's internal control. For a governmental entity, those charged with governance may include, for example, members of a board or commission, an audit committee, or senior executives and financial managers responsible for the entity.

3. Is the proposed requirement appropriate and complete? If not, please suggest specific revisions.

We believe that the proposed requirement in paragraph 15 is appropriate and complete. Paragraph 15 states that the auditor should document its inquiries and the results of those inquiries with the predecessor auditor. In our view, such audit documentation constitutes the principal record of the work performed in accordance with standards and the conclusions reached.

4. Are respondents supportive of the proposed effective date? If you are not supportive, please provide reasons for your response.

We believe that the proposed effective date for audits of financial statements for periods ending on or after December 15, 2022, would provide sufficient time for preparers, auditors, and others to adopt the new standard and related conforming amendments.