

# Memorandum

**Date:** October 10, 2012

**To:** GAO's Financial Management and Assurance Team (FMA)  
CIGIE Financial Audit Community

**From:** James R. Dalkin, Director – FMA  
Kristen Kociolek, Assistant Director – FMA  
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**Subject:** Professional Standards Update No. 58\*  
*January through October 2012*

In order to alert you to changes in professional standards, we issue Professional Standards Updates. The purpose of these updates is to highlight the issuance and some key points of recent standards. Professional Standards Updates do not contain a complete summary of the standards. Those affected by the new standards should refer to the relevant standard for details. Thanks to Barry Grinnell for his contributions to this issue which contains summaries of:

## **Auditing and Attestation Standards and Guidance**

### **GOVERNMENT ACCOUNTABILITY OFFICE (GAO)**

- 2011 Revision of Government Auditing Standards
- Principles of Federal Appropriations Law ~ Annual Update of the Third Edition

### **AMERICAN INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS (AICPA) and the AICPA AUDITING STANDARDS BOARD (ASB)**

- Statement on Auditing Standards No. 126, *The Auditor's Consideration of an Entity's Ability to Continue as a Going Concern* (Redrafted)
- Statements on Auditing Standards No. 125, *Alert That Restricts the Use of the Auditor's Written Communication*
- Audit Risk Alert: *Understanding the Clarified Auditing Standards — 2012 Audit Risk Alert*
- Audit Risk Alert: *Understanding the Responsibilities of Auditors for Audits of Group Financial Statements*
- Audit Risk Alert: *Government Auditing Standards and Circular A-133 Developments*
- Audit Guide: *Government Auditing Standards and Circular A-133 Audits*
- Audit Guide: *Assessing and Responding to Audit Risk in a Financial Statement Audit*
- Practice Aid – *Using an SSAE No. 16 Service Auditor's Report in Audits of Employee Benefit Plans*
- GAQC Practice Aid – *Yellow Book Independence - Nonaudit Services Documentation Practice Aid*

## **Regulatory Requirements**

### **OFFICE OF MANAGEMENT AND BUDGET (OMB)**

- OMB Circular A-133 Compliance Supplement

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\* Previously issued Professional Standards Updates can be found at <http://www.gao.gov/govaud/psu.htm>

- OMB - Circular No. A-136 (Revised)
- OMB Memo M-12-11 — *Reducing Improper Payments through the "Do Not Pay List"*

## **Accounting Standards and Guidance**

### **FEDERAL ACCOUNTING STANDARDS ADVISORY BOARD (FASAB)**

- Statement of Federal Financial Accounting Standards No. 42 - *Deferred Maintenance and Repairs, Amending Statements of Federal Financial Accounting Standards 6, 14, 29 and 32*
- Statement of Federal Financial Accounting Standards No. 43 - *Funds from Dedicated Collections: Amending Statement of Federal Financial Accounting Standards 27, Identifying and Reporting Earmarked Funds*

### **GOVERNMENTAL ACCOUNTING STANDARDS BOARD (GASB)**

- Statement No. 65 — *Items Previously Reported as Assets and Liabilities*
- Statement No. 66 — *Technical Corrections—2012—an amendment of GASB Statements No. 10 and No. 62*
- Statement No. 67 — *Financial Reporting for Pension Plans — an amendment of GASB Statement No. 25*
- Statement No. 68 — *Accounting and Financial Reporting for Pensions — an amendment of GASB Statement No. 27*
- GASB Analyst Guide to Governmental Financial Statements
- Preliminary Views on Major Issues Related to Economic Condition Reporting: *Financial Projections*

## **Auditing and Attestation Standards and Guidance**

### **GOVERNMENT ACCOUNTABILITY OFFICE (GAO)**

[www.gao.gov](http://www.gao.gov)

#### **✚ 2011 Revision of Government Auditing Standards**

GAO has formally issued the 2011 Revision of Government Auditing Standards that will be effective for financial audit and attestation engagements for periods ending on or after December 15, 2012. The 2011 Revision has been effective for performance audits that started on or after December 15, 2011. The December 2011 Revision contains limited changes made since the Internet Version was posted which include: (1) clarification of references to the AICPA Codification of Statements on Auditing Standards; (2) a revision of the list of safeguard examples; and (3) a clarification of and limited change in documentation requirements for procedures related to communication of certain internal control deficiencies, fraud, abuse, and noncompliance. An electronic version of the 2011 Revision of GAGAS and related interpretive publications can be accessed at the GAO's Government Auditing Standards website: <http://www.gao.gov/yellowbook> and a printed version with no change in content from the electronic version is now available for purchase through the Government Printing Office: <http://bookstore.gpo.gov/>

#### **✚ GAO-12-413SP Principles of Federal Appropriations Law ~ Annual Update of the Third Edition (March 2012)**

This is the annual update of the third edition of *Principles of Federal Appropriations Law*, with an objective to present a cumulative supplement to the published third edition text that includes all relevant decisions from January 1 to December 31, 2011. The page numbers identified in the annual update as containing new material are the page numbers in the hard copy of the third edition, and the new, updated information appears as bolded text. The annual updates are not issued in hard copy but are instead posted electronically on GAO's Web site ([www.gao.gov](http://www.gao.gov)).

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### **AMERICAN INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS (AICPA)**

[www.aicpa.org](http://www.aicpa.org)

#### **✚ Statement on Auditing Standards (SAS) No. 126, *The Auditor's Consideration of an Entity's Ability to Continue as a Going Concern (Redrafted)* (July 2012)**

SAS No. 126 addresses the auditor's responsibilities in an audit of financial statements with respect to evaluating whether there is substantial doubt about the entity's ability to continue as a going concern, and applies to all audits of financial statements regardless of whether the financial statements are prepared in accordance with a general purpose or a special purpose framework. Although SAS No. 126 supersedes

SAS No. 59, *The Auditor's Consideration of an Entity's Ability to Continue as a Going Concern*, it does not change or expand SAS No. 59 in any significant respect. This Statement is effective for audits of financial statements for periods ending on or after December 15, 2012.

**✚ Statements on Auditing Standards (SAS) No. 125, *Alert That Restricts the Use of the Auditor's Written Communication* (December 2011)**

SAS No. 125 addresses the auditor's responsibility when the auditor includes language that restricts the use of the auditor's written communication and includes a special *Alert for Engagements Performed in Accordance With Government Auditing Standards* at paragraph 11. This paragraph states that the alert should not be used when the engagement is performed in accordance with GAGAS, and is issued in accordance with AU-C sections 265, 806, or 935. Instead, the alert should describe the purpose of the auditor's written communication and state that the auditor's written communication is not suitable for any other purpose, as follows:

**The purpose of this [report, letter, presentation, or communication] is solely to [describe the purpose of the auditor's written communication, such as to describe the scope of our testing of internal control over financial reporting and compliance, and the result of that testing, and not to provide an opinion on the effectiveness of the entity's internal control over financial reporting or on compliance]. This [report, letter, presentation, or communication] is an integral part of an audit performed in accordance with Government Auditing Standards in considering [describe the results that are being assessed, such as the entity's internal control over financial reporting and compliance]. Accordingly, this [report, letter, presentation, or communication] is not suitable for any other purpose.**


**✚ Audit Risk Alert: *Understanding the Clarified Auditing Standards — 2012 Audit Risk Alert* (March 2012)**

The AICPA has developed this Audit Risk Alert, *Understanding the Clarified Auditing Standards*, to build awareness and to inform auditors of the changes and effects the clarified standards will have on audit practices and methodologies, including the changes that may affect the reports of certain audited financial statements. This alert provides an introduction to the background and implications of the clarity project, presents a schedule mapping the existing standards to the clarified standards, and highlights the changes from the existing standards to provide the auditor with a glimpse of those requirements that may need to be addressed early. It also discusses the issuance of the clarified standards, how to prepare for the transition, and the summarized changes in requirements from SAS Nos. 1-121 to the clarified SASs.

**✚ Audit Risk Alert: *Understanding the Responsibilities of Auditors for Audits of Group Financial Statements* (June 2012)**

This Audit Risk Alert is intended to help auditors understand and implement the requirements of Clarified Statement on Auditing Standards – *Special Considerations* –

*Audits of Group Financial Statements (Including the Work of Component Auditors)* which supersedes AU section 543, *Part of Audit Performed by Other Independent Auditors* and paragraphs 12-13 of SAS No. 58, *Reports on Audited Financial Statements*. The new standard introduces a number of new terms, concepts, and requirements related to group audits that will significantly affect current practice. Because the new standard is much broader than previous guidance and is effective for audits of group financial statements for periods ending on or after December 15, 2012, it is important for auditors to fully understand the requirements of the new standard well in advance of its effective date.

 ***Government Auditing Standards and Circular A-133 Developments – AICPA Audit Risk Alert (June 2012)***

AICPA Audit Risk Alerts are developed to present issues that auditors may face in their current audits, focusing on emerging practice issues and current developments. This alert is intended to achieve a more robust understanding of the economic and business environment in which an entity operates, and is also an important tool in helping identify the significant risks that may result in the material misstatement of an entity's financial statements. Significant updates to this edition also include:

- Reporting on supplementary information under SAS No. 119.
- Information on the OMB Advance Notice, released in February 2012.
- 2011 revision of *Government Auditing Standards*, including an in-depth discussion of the new independence standard.

Ordering information for Audit Risk Alerts can be obtained through the AICPA website: [www.aicpa.org](http://www.aicpa.org). Note: This publication is an “other auditing publication” as defined in AU section 150. It has no authoritative status, but may help auditors understand and apply the SASs.

 ***AICPA Audit Guide: Government Auditing Standards and Circular A-133 Audits (February 2012)***

The *Government Auditing Standards and Circular A-133 Audits* Audit Guide provides information and guidance for auditors performing audits under *Government Auditing Standards* and also provides information related to compliance audits performed in accordance with OMB Circular A-133. This guide provides important information and sample report wording related to the requirements of SAS No. 119. In addition this guide offers clear and practical guidance in areas such as internal control, sampling, and compliance auditing. Significant updates to this edition also include:

- SAS No. 119, *Supplementary Information in Relation to the Financial Statements as a Whole*.
- Updated compliance considerations for auditors performing engagements that include Recovery Act awards.
- *Government Auditing Standards*, December 2011 Revision.

**✚ AICPA Audit Guide: *Assessing and Responding to Audit Risk in a Financial Statement Audit* (March 2012)**

The Audit Guide *Assessing and Responding to Audit Risk in a Financial Statement Audit*, updated as of March 1, 2012, provides practical information, guidance, practice aids, and illustrative examples for the application of the risk assessment standards. The guide has been updated to reflect the issuance of SAS No. 122, *Statements on Auditing Standards: Clarification and Recodification*, and includes guidance such as:

- a plain-English overview of the risk assessment process,
- diagrams and examples to illustrate key points,
- a discussion of internal control and how it impacts your risk assessment,
- step-by-step guidance through the risk assessment procedure,
- a case study illustrating documentation developed in a risk assessment, and
- helpful observations and practice tips.

**✚ Practice Aid -- *Using an SSAE No. 16 Service Auditor's Report (SOC 1 Report) in Audits of Employee Benefit Plans* (March 2012)**

SOC 1 reports provide information to user auditors that assist them in obtaining an understanding of the entity, including its internal control, for the purposes of planning and performing an audit of a user entity's financial statements. This practice aid provides auditors with guidance when auditing the financial statements of an employee benefit plan that uses a service organization. This practice aid provides tools such as the *Audit Program: Auditing the Financial Statements of an Employee Benefit Plan That Uses a Service Organization*, *Planning Checklist for Audits of Employee Benefit Plans That Use a Service Organization*, and *Documentation of Use of a Type 2 Service Auditor's Report in an Audit of an Employee Benefit Plan's Financial Statements*. It also includes new attestation guidance from SSAE No. 16, *Reporting on Controls at a Service Organization*.

**✚ Governmental Audit Quality Center Practice Aid -- *Yellow Book Independence - Nonaudit Services Documentation Practice Aid* (February 2012)**

The Governmental Audit Quality Center (GAQC) has released a new practice aid, *2011 Yellow Book Independence—Nonaudit Services Documentation Practice Aid*, to assist auditors in meeting the requirements for identifying and evaluating threats to independence when considering whether to provide a nonaudit service. It notes that nonaudit services that are not specifically prohibited will have to be evaluated by auditors using the conceptual framework and an assessment will need to be made of management's ability (i.e., skills, knowledge, or experience) to oversee the nonaudit service, and the documentation requirements that include (a) documenting threats to independence that require the application of safeguards, along with the safeguards applied; (b) documenting management's ability to effectively oversee nonaudit services, including whether management possesses suitable skills, knowledge, or experience; and (c) documenting the understanding with the audited entity regarding



the nonaudit services to be performed. AICPA members, including GAQC members, are able to access a PDF file of the practice aid at the GAQC website:  
<http://www.aicpa.org/InterestAreas/GovernmentalAuditQuality/Resources/AuditPracticeToolsAids/Pages/YellowBookAuditToolsandAids.aspx>.

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## Regulatory Requirements

### **OFFICE OF MANAGEMENT AND BUDGET (OMB)**

[www.whitehouse.gov/omb](http://www.whitehouse.gov/omb)

#### **OMB Circular A-133 Compliance Supplement** (*June 2012*)

This Compliance Supplement is based on the requirements of the 1996 Amendments and 1997 revisions to OMB Circular A-133, identifies existing important compliance requirements that the Federal Government expects to be considered as part of a required audit, and also provides guidance to assist auditors in determining compliance requirements relevant to the audit, audit objectives, and suggested audit procedures for programs. Although the focus of this Supplement is on compliance requirements that could have a direct and material effect on a major program, auditors also have responsibility under GAGAS for other requirements when specific information comes to the auditors' attention that provides evidence concerning the existence of possible noncompliance that could have a material indirect effect on a major program. This Supplement is effective for audits of fiscal years beginning after June 30, 2011, and supersedes the OMB Circular A-133 Compliance Supplement dated March 2011.

#### **OMB - Circular No. A-136 (Revised)** (*August 2012*)

OMB, with the Chief Financial Officers Council (CFOC), has updated existing OMB guidance for agency and government-wide financial reporting. OMB Circular No. A-136 *Financial Reporting Requirements* establishes a central reference point and supersedes the OMB memoranda, bulletin and circular listed in Circular Section 1.2.

This update includes:

- Agency due dates and some reporting changes that support the Department of the Treasury in preparing the 2013 Financial Report of the U.S. Government;
- Requirements for agencies to produce elements of a Schedule of Spending as Other Accompanying Information;
- Annual Performance Report performance reporting requirements under the Government Performance and Results Modernization Act (GPRMA); and,
- Continued advance guidance for aligning the Statement of Budgetary Resources with the SF 133, *Report on Budget Execution and Budgetary Resources*, effective in FY 2012.

This revision of Circular No. A-136 is effective upon issuance, unless otherwise specified.

 **OMB Memo M-12-11 — Reducing Improper Payments through the "Do Not Pay List" (April 12, 2012)**


OMB and the Department of the Treasury have established the *Do Not Pay solution*, which is comprised of two components geared toward reducing improper payments: a web-based, single-entry access portal and Data Analytics Services that utilize additional data sources not available through the portal. In addition, the Recovery Accountability and Transparency Board established the Recovery Operations Center to prevent fraud and waste in Recovery Act programs. The Chief Financial Officer of each Federal agency (or the accountable official for improper payments and program integrity) shall submit to OMB the draft of the agency's plan for using these centralized solutions by no later than June 30, 2012. OMB will work closely with agencies in reviewing the draft plans and will provide comments by no later than July 31, 2012. The agency shall then finalize its plan, and submit a copy of it to OMB, by no later August 31, 2012.

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## **Accounting Standards and Guidance**

### **FEDERAL ACCOUNTING STANDARDS ADVISORY BOARD (FASAB)**

[www.fasab.gov](http://www.fasab.gov)

 **Statement of Federal Financial Accounting Standards No. 42 - *Deferred Maintenance and Repairs, Amending Statements of Federal Financial Accounting Standards 6, 14, 29 and 32* (April 2012)**

The objectives of this Statement are to improve the measurement of deferred maintenance and repairs (DM&R) by incorporating changes that are responsive to the concerns raised by the financial and technical communities, and to amend the required supplementary information (RSI) presentation requirements contained in Statement of Federal Financial Accounting Standards (SFFAS) 6, *Accounting for Property, Plant, and Equipment* in addition to conforming amendments. The amendments require entities to: (1) describe their maintenance and repairs (M&R) policies and how they are applied, (2) discuss how they rank and prioritize M&R activities among other activities, (3) identify factors considered in determining acceptable condition standards, (4) state whether DM&R relate solely to capitalized general property, plant and equipment (PP&E) and stewardship PP&E or also to non-capitalized or fully depreciated general PP&E, (5) identify PP&E for which management does not measure and/or report DM&R and the rationale for the exclusion of other than non-capitalized or fully depreciated general PP&E, (6) provide beginning and ending DM&R balances by category of PP&E, and (7) explain significant changes from the prior year. The provisions of this Statement need not be applied to immaterial items, and this Statement is effective for periods beginning after September 30, 2014 with earlier implementation encouraged.



**✚ Statement of Federal Financial Accounting Standards No. 43 - *Funds from Dedicated Collections: Amending Statement of Federal Financial Accounting Standards 27, Identifying and Reporting Earmarked Funds***  
(June 2012)

This Statement amends the requirements of Statement of Federal Financial Accounting Standards (SFFAS) 27, *Identifying and Reporting Earmarked Funds*, to resolve matters that FASAB identified for improvement, and applies to federal entities that present general purpose federal financial reports, including the consolidated financial report of the U.S. Government (CFR). Amendments to SFFAS 27 made by this standard include changing the term “*earmarked funds*” to “*funds from dedicated collections*”, modifying the definition of a fund from dedicated collections, permitting the provision of either consolidated or combined data on funds from dedicated collections, and illustrating optional formats for displaying information on the face of the balance sheet and statement of changes in net position. This Statement is effective for periods beginning after September 30, 2012, and early adoption is not permitted.

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**GOVERNMENTAL ACCOUNTING STANDARDS BOARD (GASB)**  
[www.gasb.org](http://www.gasb.org)

**✚ Statement No. 65 — *Items Previously Reported as Assets and Liabilities***  
(March 2012)

This Statement establishes accounting and financial reporting standards that reclassify, as deferred outflows of resources or deferred inflows of resources, certain items that were previously reported as assets and liabilities and recognizes, as outflows of resources or inflows of resources, certain items that were previously reported as assets and liabilities. It also amends the financial statement element classification of certain items previously reported as assets and liabilities to be consistent with the definitions in Concepts Statement 4, and provides financial reporting guidance related to the impact of the financial statement elements, such as changes in the determination of the major fund calculations and limiting the use of the term *deferred* in financial statement presentations. The provisions of this Statement are effective for financial statements for periods beginning after December 15, 2012, with earlier application encouraged.

**✚ Statement No. 66 — *Technical Corrections—2012—an amendment of GASB Statements No. 10 and No. 62*** (March 2012)

The objective of this Statement is to improve accounting and financial reporting by resolving conflicting guidance that resulted from the issuance of two pronouncements, Statements No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*, and No. 62, *Codification of Accounting and Financial*

*Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements.* This Statement amends Statement No. 10, *Accounting and Financial Reporting for Risk Financing and Related Insurance Issues*, by removing the provision that limits fund-based reporting of an entity's risk financing activities to the general fund and the internal service fund type, and amends Statement No. 62 by modifying the specific guidance on accounting for (1) operating lease payments that vary from a straight-line basis, (2) the difference between the initial investment (purchase price) and the principal amount of a purchased loan or group of loans, and (3) servicing fees related to mortgage loans that are sold when the stated service fee rate differs significantly from a current servicing fee rate. The provisions of this Statement are effective for financial statements for periods beginning after December 15, 2012 with earlier application encouraged.

**✚ Statement No. 67 — Financial Reporting for Pension Plans — an amendment of GASB Statement No. 25 (June 2012)**

The objective of this Statement is to improve financial reporting by state and local governmental pension plans. It replaces the requirements of Statements No. 25, *Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans*, and No. 50, *Pension Disclosures*, as they relate to pension plans that are administered through trusts or equivalent arrangements that meet certain criteria, and requires defined benefit pension plans to present two financial statements—a statement of fiduciary net position and a statement of changes in fiduciary net position. The requirements of Statements 25 and 50 remain applicable to pension plans that are not administered through trusts covered by the scope of this Statement, and to defined contribution plans that provide postemployment benefits other than pensions. This Statement is effective for financial statements for fiscal years beginning after June 15, 2013 with earlier application encouraged.

**✚ Statement No. 68 — Accounting and Financial Reporting for Pensions — an amendment of GASB Statement No. 27 (June 2012)**

The primary objective of this Statement is to improve accounting and financial reporting by state and local governments for pensions. It replaces the requirements of Statement No. 27, *Accounting for Pensions by State and Local Governmental Employers*, as well as the requirements of Statement No. 50, *Pension Disclosures*, as they relate to pensions that are provided through pension plans administered as trusts or equivalent arrangements that meet certain criteria. This Statement requires the liability of employers and nonemployer contributing entities to employees for defined benefit pensions to be measured as the portion of the present value of projected benefit payments to be provided through the pension plan, less the amount of the pension plan's fiduciary net position. This Statement is effective for fiscal years beginning after June 15, 2014 with earlier application encouraged.

## **GASB — An Analyst’s Guide to Governmental Financial Statements** (*July 2012*)

GASB has issued *An Analysts’ Guide to Governmental Financial Statements, 2nd edition*, which is a comprehensive, easy-to-understand primer for investment firms; rating agencies; institutional investors; mutual funds; bond agencies; and legislative, oversight and research organizations that need financial information about state and local government financial reports. The *Guide* has also been updated to cover major new reporting requirements issued by the GASB since the publication of the original guide in 2001, and includes 125 annotated examples of financial statements, note disclosures, and supporting schedules, including full sets of financial statements for a state government, municipality, school district, and public university.

## **Preliminary Views on Major Issues Related to Economic Condition Reporting: Financial Projections** (*November 2011*)

This Preliminary Views document presents GASB’s (the Board) current views on what it believes are the most fundamental issues associated with the reporting of financial projections and related narrative discussions that will assist users in assessing a governmental entity’s economic condition. The Board’s preliminary view is that five components of information are necessary to assist users in assessing a governmental entity’s fiscal sustainability:

- Projections of the total cash inflows and major individual cash inflows, in dollars and as a percentage of total cash inflows, with explanations of the known causes of fluctuations in cash inflows
- Projections of the total cash outflows and major individual cash outflows, in dollars and as a percentage of total cash outflows, with explanations of the known causes of fluctuations in cash outflows
- Projections of the total financial obligations and major individual financial obligations, including bonds, pensions, other postemployment benefits, and long-term contracts, with explanations of the known causes of fluctuations in financial obligations
- Projections of annual debt service payments (principal and interest)
- Narrative discussion of the major intergovernmental service interdependencies that exist and the nature of those service interdependencies.

The assumptions employed in making projections would be based on relevant historical information, as well as events and conditions that have occurred and affect the projection periods. The assumptions would be (1) consistent with each other (where appropriate) and with the information used as the basis for the assumptions and (2) comprehensive by considering significant trends, events, and conditions. Annual financial projections would be made for a minimum of five individual years beyond the reporting period for the purpose of external reporting. All of the components of fiscal sustainability information are believed to be essential for placing the basic financial statements and notes to the basic financial statements in an operational or economic context and therefore would be required and communicated as required supplementary information (RSI).