

## GAQC Practice Aid: *A Primer on Government Auditing Standards*

This nonauthoritative AICPA Governmental Audit Quality Center (GAQC) practice aid provides an overview of the requirements in *Government Auditing Standards, 2018 Revision* with a focus on the use of these standards in a financial audit.

## Introduction

### **A Primer on *Government Auditing Standards***

To serve AICPA members and promote audit quality, the AICPA Governmental Audit Quality Center (GAQC) has developed this practice aid to provide an overview of the requirements of [\*Government Auditing Standards, 2018 Revision\*](#) (also referred to as the Yellow Book or GAGAS). It addresses common questions the GAQC frequently receives from practitioners when they are newer to performing financial audits under the Yellow Book. Specifically, it includes a series of questions and answers intended to explain what *Government Auditing Standards* are, when they are required, how to access the standards, and some of the key areas that differ from or add to AICPA standards in a financial audit.

Auditors are strongly encouraged to review the sections of the Yellow Book relevant to a financial audit in their entirety. Chapters 1 – 4 of the AICPA Audit Guide, [\*Government Auditing Standards and Single Audits\*](#) (AICPA GAS-SA Guide) are also a key resource to assist with understanding what an audit under GAGAS involves.

This practice aid provides nonauthoritative guidance on *Government Auditing Standards* as developed by AICPA staff. Official AICPA positions are determined through certain specific committee procedures, due process, and extensive deliberation. The AICPA staff views expressed in this report are intended to provide member services, but not for the purposes of providing accounting services or practicing public accounting. This document has not been approved, disapproved, or otherwise acted on by any senior technical committee of the AICPA. The AICPA makes no warranties or representations concerning the accuracy of information issued.

## **What are Government Auditing Standards?**

*Government Auditing Standards* are issued by the Comptroller General of the United States of the U.S. Government Accountability Office (GAO). *Government Auditing Standards* contains requirements and guidance for financial audits, attestation engagements, reviews of financial statements, and performance audits. The information in this practice aid focuses on the requirements of GAGAS in a financial audit.

## **How does an auditor access Government Auditing Standards?**

The Yellow Book may be accessed at <https://www.gao.gov/assets/700/693136.pdf>. The [GAO Yellow Book Web page](#) also contains other relevant information about the standards.

## **When is the use of GAGAS required?**

Typically, the use of GAGAS is required by laws, regulations, agreements, contracts, or other authoritative sources. For example, single audits conducted in accordance with the Single Audit Act and Title 2 U.S. Code of Federal Regulations (CFR) Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) are required to be performed in accordance with GAGAS.

## **When performing financial audits under Government Auditing Standards does the auditor also refer to other professional auditing standards?**

GAGAS incorporates by reference AICPA Statements on Auditing Standards. Therefore, auditors performing financial audits in accordance with *Government Auditing Standards* should comply with GAAS, the requirements found in chapters 1–5 of *Government Auditing Standards*, and the additional requirements for financial audits found in chapter 6, "Standards for Financial Audits," of *Government Auditing Standards*.

*Government Auditing Standards* states that auditors may use GAGAS in conjunction with professional standards issued by the Public Company Accounting Oversight Board (PCAOB) and the International Auditing and Assurance Standards Board. For example, in situations where certain for-profit entities whose financial statement audits are performed under PCAOB audit standards are also subject to *Government Auditing Standards* due to their participation in federal programs.

## **In what areas does an auditor have additional responsibilities when conducting an audit in accordance with GAGAS?**

In conducting Yellow Book audits, the auditor assumes certain responsibilities beyond those of audits performed in accordance with GAAS. The standards and guidance applicable to financial audits are contained in chapters 1-6 of the Yellow Book and include ethical principles, general standards, and additional standards for performing and reporting on financial audits.

*Ethics.* The ethical principles presented in Chapter 3 of the Yellow Book provide the foundation, discipline, structure and environment that influence the application of GAGAS. The five ethical principles that guide the work of auditors conducting audits in accordance with GAGAS are: the public interest; integrity; objectivity; proper use of government information, resources, and position; and professional behavior.

*Independence.* Per the Yellow Book, an auditor should be independent from an audited entity during any period of time that falls within the period covered by the financial statement audit or subject matter of the engagement and the period of professional engagement. Therefore, AICPA members are subject to the AICPA Code of Professional Conduct as well as the additional independence requirements found in chapter 3 of *Government Auditing Standards*. GAGAS establishes a conceptual framework that auditors use to identify, evaluate, and apply safeguards to address threats to independence.

**Note:** The GAGAS independence requirements, while similar to the AICPA independence rules, contain key differences, particularly relating to the performance of nonaudit services such as preparing accounting records and financial statements. GAGAS states 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 auditors' independence and should document the threats and safeguards applied to eliminate and reduce threats to an acceptable level in accordance with Chapter 3 of *Government Auditing Standards* or decline to provide the services. Auditors should also identify as threats to independence certain other services related to preparing accounting records and financial statements and GAGAS contains a documentation requirement for the evaluation of the significance of the threats.

This practice aid does not provide auditors with all the GAGAS independence requirements and nuances, as they are many, but serves as an alert to the additional requirements. Auditors should familiarize themselves with the independence requirements found in Chapter 3 of the Yellow Book in their entirety. In addition, there are many existing AICPA and other resources available including the following:

- Chapter 2 of the [AICPA GAS-SA Audit Guide](#) provides guidance on Yellow Book independence requirements.
- [The Independence Rules Comparison: AICPA and Government Auditing Standards](#), issued by the AICPA Professional Ethics team, provides:
  - a high-level overview of the various independence requirements;
  - detailed comparisons of the conceptual framework approach and nonattest/nonaudit services topics; and
  - comparison tables with references to the independence interpretations in the AICPA Code of Professional Conduct and the specific paragraph references to the requirements in the Yellow Book.
- GAQC archived no-Continuing Professional Education (CPE) web events that auditors may view for free:
  - [Understanding the Changes to Yellow Book Independence](#)
  - [Considering and Documenting Nonaudit Services under Government Auditing Standards](#)
  - [The 2018 Yellow Book: What You Need to Know](#)
  - [Heard in the Hallways: Commonly Asked Yellow Book Questions](#)
- Other relevant AICPA CPE covering [single audit and relevant learning](#).

*Professional Judgment.* GAGAS requires that auditors use professional judgment in planning and performing audits and in reporting the results. Although this standard is similar to due professional care in GAAS, GAGAS provides its own discussion on the topic in Chapter 3.

*Competence and CPE.* GAGAS includes its own requirements and guidance in the area of competence and CPE. The audit organization's management must assign auditors to perform the audit who, *before beginning the work on the audit*, collectively possess the competence needed to address the audit objectives and perform the work in accordance with GAGAS. Indicators of competence include:

- technical knowledge and skills in areas such as GAGAS, standards, regulations, techniques, tools, and guidance; and
- competence for assigned roles (e.g., supervisory auditor, partner).

Auditors who plan, direct, perform audit procedures for, or report on an audit should develop and maintain their professional competence by completing CPE as required in the Yellow Book.

*Quality Control and Peer Review.* An audit organization performing audits in accordance with GAGAS must establish and maintain a system of quality control that is designed to provide the audit organization with reasonable assurance the organization and its personnel comply with professional standards and applicable legal and regulatory requirements.

GAGAS requires audit organizations performing Yellow Book audits to obtain an external peer review performed by reviewers independent of the audit organization being reviewed. An external audit organization should make its most recent peer review report publicly available. In addition, an audit organization seeking to enter into a contract to perform a Yellow Book audit should provide the most recent peer review report and any subsequent peer review reports received during the period of the contract to the party contracting for such services.

*Planning.* For GAGAS engagements, auditors have additional requirements regarding previous engagements and investigation, or legal proceedings as follows:

- Previous Engagements. GAGAS requires auditors to evaluate whether the audited entity has taken appropriate corrective action to address findings and recommendations from previous engagements that could have a significant effect on the financial statements. Auditors should ask management of the audited entity to identify previous audits, attestation engagements, and other studies that *directly relate to the objectives of the audit*, including whether related recommendations have been implemented, and use this information in:
  - assessing risk;
  - determining the nature, timing, and extent of current audit work; and
  - determining the extent to which testing the implementation of the corrective actions is applicable to the current audit objectives.
- Investigations and Legal Proceeds. Auditors should inquire of management of the audited entity whether any investigations or legal proceedings have been initiated or are in process with respect to the period under audit and should evaluate the effect of initiated or in-process investigations or legal proceedings on the current audit.

*Audit Documentation.* GAGAS requires additional documentation requirements above those in GAAS, including:

- documenting, before the report release date, supervisory review of the evidence that supports the findings and conclusions contained in the auditor’s report;
- documenting any departures from GAGAS, including unconditional and presumptively mandatory requirements when alternative procedures performed were not sufficient to achieve the required objectives; and
- making individuals and audit documentation available upon request, subject to applicable laws and regulations.

*Noncompliance with Contracts and Grant Agreements.* GAGAS states that auditors should extend the GAAS requirements concerning consideration of noncompliance with laws and regulations to include consideration of noncompliance with the provisions of contracts and grant agreements.

*Reporting.* In addition to GAAS requirements for reporting, additional GAGAS requirements relate to:

- stating compliance with GAGAS in the audit report;
- reporting on internal control; compliance with provisions of laws, regulations, contracts, and grant agreements; and instance of fraud;
- presenting findings in the audit report (see related question below);
- obtaining and reporting the views of responsible officials (see related question below);
- reporting confidential or sensitive information; and
- distributing reports.

**My firm has not had much experience performing audits under *Government Auditing Standards*. What do you suggest?**

*Government Auditing Standards* includes the following requirement: “The audit organization’s management must assign auditors to conduct the engagement who before beginning work on the engagement collectively possess the

competence needed to address the engagement objectives and perform their work in accordance with GAGAS.” Thus, auditors must gain the needed competencies or not accept the engagement. If accepting the engagement, a full review of *Government Auditing Standards, 2018 Revision* is critical, as well as obtaining related training. Auditors may also look to the following to learn more on this topic:

- [AICPA GAS-SA Audit Guide](#) (chapters 1-4 cover GAGAS requirements)
- AICPA CPE course titled, [Yellow Book: Staying Compliant with Government Auditing Standards](#)
- GAQC archived no-CPE Web event, [Considering and Documenting Nonaudit Services under Government Auditing Standards](#)
- GAQC archived no-CPE Web event, [Heard in the Hallways: Commonly Asked Yellow Book Questions](#)

### **What are the CPE requirements that an auditor must complete to perform an audit in accordance with GAGAS?**

Chapter 4 of the Yellow Book should be referred to by auditors for a complete understanding of the GAGAS CPE requirements. It includes a complete discussion of the requirements and additional application guidance on CPE topics, including subject matter, specialists, and measurement and monitoring of CPE. The following is a high-level summary of the Yellow Book CPE requirements.

Auditors who plan, direct, perform procedures for, or report on engagements conducted in accordance with GAGAS should complete at least 80 hours of CPE in every 2-year period as follows:

- 24 CPE hours should be in a subject matter directly related to the government environment, government auditing, or the specific or unique environment in which the audited entity operates.
- 56 CPE hours should be in a subject matter that directly enhances the auditors’ professional expertise to conduct audits.

The subject matter categories for the 24-hour requirement may be used to satisfy the 56-hour CPE requirement. CPE used to fulfill the 24-hour requirement may be taken at any time during the 2-year period. However, auditors should complete at least 20 hours of CPE in each year of the 2-year period.

Paragraph 4.26 of the Yellow Book provides an exception from the CPE requirements for *nonsupervisory* auditors who charge less than 40 hours of their time annually to GAGAS engagements. Paragraph 4.25 indicates that auditors who charge less than 20% of their time annually to GAGAS engagements and are only involved in performing engagement procedures (i.e., not involved in planning, directing, or reporting) may be exempted from the 56-hour CPE requirement but not the 24-hour requirement.

### **What are the requirements related to findings in the GAGAS report?**

Findings may involve deficiencies in internal control; noncompliance with provisions of laws, regulations, contracts, and grant agreements; or instances of fraud.

The following are required elements when presenting an audit finding in accordance with GAGAS (see Yellow Book paragraphs 6.25-.28):

- Criteria – The required or desired state or expectation with respect to the program or operation (i.e., what should the auditor have seen?)
- Condition – The situation that exists (i.e., what did the auditor see?)
- Cause – The required or desired state or expectation with respect to the program or operation (i.e., why did the auditor see what was seen?)
- Effect or Potential Effect – The outcome or consequence resulting from the difference between the condition and the criteria (i.e., what is the result of what the auditor saw?)

When auditors identify findings, they should plan and perform procedures to develop the criteria, condition, cause, and effect of the findings to the extent that these elements are relevant and necessary to achieve the audit objectives. Auditors should consider internal control deficiencies in their evaluation of identified findings when developing the cause element of the identified findings.

The auditor should develop the elements of the finding to the extent necessary to assist management or oversight officials in understanding the need for corrective action. Clearly developed findings also assist the auditor in making a recommendation for corrective action, which may be included in the report if the elements of a finding are sufficiently developed. To give the reader a basis for judging the prevalence and consequences of these findings, auditors should, as appropriate, relate the instances identified to the population or the number of cases examined and quantify the results in terms of dollar value or other measures. If the results cannot be projected, auditors should limit their conclusions appropriately.

**What are the requirements regarding reporting the views of responsible officials in a GAGAS financial audit?**

The auditor should obtain and report the views of responsible officials and planned corrective actions of the audited entity concerning the findings, conclusions, and recommendations in the audit report. Obtaining the comments in writing is preferred, but oral comments are acceptable. When written comments are received, the auditor should include a copy in their report. When oral comments are received, the auditor should prepare a summary, provide a summary to the responsible officials to verify the comments are accurately represented, and include the summary in the audit report.