



Association of Local Government Auditors

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449 Lewis Hargett Circle
Suite 290
Lexington, KY 40503
Phone: (859) 276-0686
Fax: (859) 278-0507
www.algaonline.org

U.S. Government Accountability Office
YellowBook@gao.gov

Re: Request for Modification of Government Auditing Standards Requirements for
Performing Nonaudit Services

Dear Mr. Dalkin,

The Association of Local Government Auditors (ALGA) is submitting this letter to request modification of the U.S. Government Accountability Office's (GAO) Government Auditing Standards (GAGAS or Yellow Book) requirements for performing nonaudit services. Our organization represents more than 300 audit organizations and about 2,000 members. The 2011 revision of the Yellow Book includes several updates that impact how auditors conduct nonaudit services and has resulted in significant confusion regarding how to apply the standards.

This topic is of interest to us because 70 percent of our members report that they perform nonaudit services. Many of our members are not clear as to the intended meaning of certain provisions related to nonaudit services in the Yellow Book, particularly when nonaudit services are not performed at management's request.

The Yellow Book recognizes that nonaudit services may be initiated by management request or legislative mandates. Examples of this are found in:

- (2.12) Requires communications to "*requestors and those charged with governance*"
- (3.44) "*An auditor in a government entity may be required to perform a nonaudit service ... as a consequence of constitutional or statutory requirements*"

Many government-based audit organizations also self-initiate services that are now, by definition, categorized as nonaudit services.

Modification by the GAO regarding management's responsibilities when nonaudit services are performed by government-based auditors would help improve the consistency of how these requirements are applied. It would also help government auditors protect their independence, which is vital to the credibility of their work.

2011 Yellow Book and Nonaudit Services

GAGAS outlines requirements for auditors based on three categories of work: financial audits, attestation engagements, and performance audits (2.05). All other professional services provided by auditors are defined as nonaudit services, which are not covered by GAGAS (2.12).

Standards, however, are provided to protect the independence of auditors who perform nonaudit services for governments they also audit. According to the revised Yellow Book, a critical component in determining whether the provision of nonaudit services creates a threat to independence is consideration of management's ability to effectively oversee the nonaudit service performed (3.34). This includes evaluating the adequacy of the services performed and accepting responsibility for the results of the services (3.37). In the event that management is unwilling or unable to assume this responsibility, providing the nonaudit service would impair the auditor's independence (3.38).

Auditors in Government and Nonaudit Services

While it may be appropriate for management to oversee nonaudit services they have requested, nonaudit services are at times initiated by government audit organizations where management oversight is inappropriate. For example, many government-based audit organizations have a responsibility to investigate reports of potential fraud, waste, and abuse. Management is sometimes the focus of these investigations.

Further, legislative mandates have also made some government audit organizations responsible for management activities where management oversight and responsibility for the results of the work could be contrary to the mandate. Examples include:

- Oversight of accounts payable, including verification and signing of warrants and checks prior to issuance
- Oversight of payroll functions, including verification of time entry and supporting documentation
- Performance of surprise reconciliations at cash receipting locations
- Review of all contracts

Given these unique circumstances faced by government audit organizations, ALGA believes that the provisions requiring management oversight should only apply when management has requested the nonaudit service. Therefore, we respectfully request the GAO modify the standards addressing nonaudit services by:

1. Adding language to 3.33 which explicitly states that nonaudit services may be initiated by various methods including:
 - a. Legislative or Charter mandates
 - b. Self-initiated by audit organizations that are part of a government
 - c. Requests from those charged with governance, such as a legislative body
 - d. Requests from management

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2. Moving 2.13 to after 3.33, or reiterate after 3.33, that threats to independence must be evaluated for all nonaudit services performed at entities that are also subject to audit by the audit organization – regardless of the method that initiated the work.
3. Adding language in 3.34 to clarify that standards requiring management to oversee nonaudit services **only apply when the service is requested by, or performed on behalf of, management.**
4. Adding language to 3.38 to clarify that providing nonaudit services **that have been requested by management** would impair auditor independence on future audits when management is unwilling or unable to oversee the work.
5. Adding language to 3.44 to recognize that a potential safeguard that audit organizations within government may implement in response to mandated nonaudit services includes segregating the part of their organizational structure that performs nonaudit services from those that perform audits.

We appreciate your consideration of this request for modification and look forward to working with the GAO to resolve these concerns.

Respectfully submitted,



Corrie Stokes
President
Association of Local Government Auditors



Harriet Richardson
Chair, Professional Issues Committee
Association of Local Government Auditors

Key ALGA Contributors:

Craig Kinton, City of Dallas, TX
Harriet Richardson, City of Palo Alto, CA
Larry Stafford, Clark County, WA
Jeffrey Vargas, Allegheny County, PA