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Washington, DC 20548

May 12, 2017

Ms. Lisa A. Snyder
Senior Director, Professional Ethics Division
American Institute of Certified Public Accountants
1211 Avenue of the Americas
New York, NY 10036-8775

GAO's Response to the American Institute of Certified Public Accountants' Professional Ethics Division March 2017 Proposed Interpretation, *Responding to Non-Compliance with Laws and Regulations*

Dear Ms. Snyder:

This letter provides GAO's comments on the proposed interpretation entitled *Responding to Non-Compliance with Laws and Regulations*, which was prepared by the American Institute of Certified Public Accountants (AICPA). GAO promulgates generally accepted government auditing standards (GAGAS), which provide professional standards for auditors of government entities in the United States.

We support the AICPA's efforts to develop guidance setting forth members' responsibilities when encountering non-compliance with laws and regulations (NOCLAR). The AICPA requested responses to the following questions. Our responses and additional comments on the applicability of the proposed interpretation to auditors in the public sector environment follow. We limited our comments to the interpretation for members in public practice, as we anticipate that auditors of government entities may have to comply with both that interpretation and GAGAS.

Responses to Questions Included in the Proposed Interpretation

- 1. Should members in public practice who provide only nonattest services to a client be required to document certain aspects of the NOCLAR? Or, rather, should they be encouraged to document certain aspects of the NOCLAR?**

We believe that members in public practice who provide only nonattest services should be required to document certain aspects of NOCLAR. Documentation provides evidence that NOCLAR has been considered.

- 2. Is a one year transition period for the effective date appropriate? If not, what is an appropriate time period and why?**

We believe that a 1-year transition period for the effective date is appropriate.

Other Comments

In addition to our responses to the questions, we suggest that the AICPA also consider incorporating guidance on the applicability of the proposed interpretation in a government environment. Stakeholders for audits of government funds include the citizens to whom the governments are accountable. This is true whether the funds are spent by the governments themselves or by entities that received the funds through grant awards. For this reason, engagements conducted in accordance with GAGAS include steps to help ensure that those charged with overseeing expenditures of government funds have the information necessary to perform that oversight effectively. In our view, the interpretation would be more comprehensive if it included the principle of accountability for public funds. The following are some examples of how the interpretation could incorporate guidance that helps auditors of government funds address the accountability concerns that accompany government-provided funding.

- GAGAS provides that in certain situations, auditors should report NOCLAR to external parties, the relevant funding agency, or both. Also, AICPA's *Codification of Statements on Auditing Standards* (AU-C) Section 250, *Consideration of Laws and Regulations in an Audit of Financial Statements*, and AICPA's *Codification of Statements on Standards for Attestation Engagements* (AT-C) Section 205, *Examination Engagements*, provide guidance to auditors and practitioners to consider requirements for communicating NOCLAR when performing an audit or an examination engagement in the government environment. For example, AU-C 250.A28 provides that "a duty to notify parties outside the entity may exist . . . in compliance with requirements for the audits of entities that receive financial assistance from a government agency." AU-C 250.A29 provides that "the auditor of a governmental entity may be required to report on compliance with laws, regulations, and provisions of contracts or grant agreements as part of the audit of the governmental entity's financial statements (for example, in an audit conducted in accordance with *Government Auditing Standards*). The auditor also may be required to communicate instances of noncompliance to appropriate oversight bodies and funding agencies." We suggest that the AICPA include guidance consistent with AU-C 250 and AT-C 205 to assist members in public practice in determining how to respond to NOCLAR and when to disclose NOCLAR to third parties in the government environment.
- Paragraph .35 of proposed interpretation, section 1.170.010, discusses documentation requirements related to identified or suspected significant NOCLAR. Members could be reminded that in audits of government funds, such documentation may be subject to inspection by government auditors.
- Auditors of government funds would benefit from guidance on appropriate steps to take after becoming aware of possible or suspected non-compliance with the terms of contracts or grant agreements. GAGAS extends the applicability of U.S. audit requirements pertaining to auditors' responsibilities for laws and regulations to consideration of compliance with provisions of contracts and grant agreements.

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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 fluid and cursive, with a prominent initial "J" and a long horizontal stroke at the end.

James R. Dalkin
Director
Financial Management and Assurance