



STATE OF TENNESSEE
COMPTROLLER OF THE TREASURY
DEPARTMENT OF AUDIT
DIVISION OF COUNTY AUDIT
SUITE 1500
JAMES K. POLK STATE OFFICE BUILDING
NASHVILLE, TENNESSEE 37243-1402
PHONE ()

June 29, 2017

Mr. James Dalkin
Director
Financial and Management Services
U.S. Government Accountability Office

Dear Director Dalkin:

This response is written on behalf of the Tennessee Comptroller of the Treasury, **Division of Local Government Audit (the Division)**. The Division is responsible for auditing or reviewing the audits of approximately 1300 governmental entities and 225 nonprofit entities. The vast majority of these audits are conducted under *Government Auditing Standards*. Our staff comprises 92 auditors. The Division and our audit clients will be directly affected by any proposed change in GAGAS. In general the Division is supportive of the proposed revisions. Our responses to the Exposure Draft discussion items are as follows.

Discussion Items:

1. Generally accepted government auditing standards (GAGAS) is presented in a revised format. This is intended to allow auditors to quickly identify requirements and application guidance related to those requirements. In addition, certain topics are regrouped within the chapters. - Please comment on how the revised format of GAGAS affects the organization and readability of the standards.

Item 1 Response-

The Division believes the revised format is a significant improvement over the previous format. We also believe the topic regrouping is logical and is an improvement over the previous topic and chapter grouping.

2. In chapter 3 (“Ethics, Independence, and Professional Judgment”), additional requirements and guidance are provided concerning the provision of nonaudit services to audited entities, including further explanation of the responsibility to ensure that management of the audited entity possesses the appropriate skills, knowledge, and experience to oversee the nonaudit service and expanding discussion of nonaudit services that should be considered threats or impairments to an external auditor’s independence. (various paras. 3.67 through 3.101) - Please comment on whether the revisions related to nonaudit services sufficiently and clearly explain what is required and prohibited under GAGAS.



STATE OF TENNESSEE
COMPTROLLER OF THE TREASURY
DEPARTMENT OF AUDIT
DIVISION OF COUNTY AUDIT
SUITE 1500
JAMES K. POLK STATE OFFICE BUILDING
NASHVILLE, TENNESSEE 37243-1402
PHONE [REDACTED]

Item 2 Response-

The Division believes the provision of nonaudit services related to preparing accounting records and financial statements would always give rise to a significant threat to independence. Our Division has always applied the previous guidance to come to that conclusion. We believe the proposed guidance is correct and clear based on any honest reading.

However, wording has been added to paragraph 3.67 that was not in the previous version of GAGAS. It has important ramifications for many small governments across the nation. The added wording is "...and be capable of detecting a material error, omission, or misstatement." The application guidance continues in paragraph 3.71 to repeat the same idea but with the additional thought ... "management is not required to possess the expertise to perform or re-perform the services." The requirement in paragraph 3.67 is wholly incongruent with the application guidance in paragraph 3.71.

The requirements in paragraph 3.67 are, in fact, requiring the person with s.k.e. to have the expertise to perform and re-perform the work of the auditor. A person who could merely look at a set of government-wide financial statements and determine a material error, omission, or misstatement, would need to know GAAP. In addition, that person would need to be able apply GAAP to prepare a set of government-wide full accrual financial statements and the notes that go along with them because several amounts on those financial statements are either aggregated or netted and include information from several funds added together in one column and information that can only be gathered from the notes to the financial statements. Consider all the aggregations that are presented on the statement of cash flows alone. That person would be in all respects equal to the auditor. But that is not what paragraph 3.71 requires.

A few words, which seem innocuous at the Federal level, will effect real world costs for local governments. Auditors are able to demonstrate independence under the current guidance. The new wording is unnecessarily burdensome and should be removed.

The Division welcomes the opportunity to explain this more fully should GAO consider that necessary.

3. In chapter 4 ("Competence and Continuing Professional Education"), GAGAS discusses the levels of proficiency required for the roles on an engagement as well as a description of the tasks



**STATE OF TENNESSEE
COMPTROLLER OF THE TREASURY
DEPARTMENT OF AUDIT
DIVISION OF COUNTY AUDIT**

**SUITE 1500
JAMES K. POLK STATE OFFICE BUILDING
NASHVILLE, TENNESSEE 37243-1402
PHONE [REDACTED]**

generally expected to be performed by auditors in these roles. (paras. 4.09 through 4.10) - Do these roles and descriptions clarify the competence required of auditors conducting engagements in accordance with GAGAS? - Is the level of proficiency expected for each of these roles clear?

Item 3 Response-

The Division believes the levels and descriptions are adequate. No amount of detail will suffice to explain the distinctions completely. There will always be a significant degree of subjectivity involved in applying the levels. The Division recommends leaving the levels and descriptions as they are written. (However, refer to item 6 below)

- Chapter 4 (“Competence and Continuing Professional Education”) includes a requirement for auditors to complete at least 4 hours of continuing professional education (CPE) in GAGAS topics (“GAGAS Qualification”). This 4-hour requirement is a subset of the 24-hour CPE requirement and needs to be completed each time a GAGAS revision is issued. Application guidance provides examples of the types of topics that would qualify as GAGAS topics. (paras. 4.15 and 4.23) - Please comment on any additional topics that could be included in the 4-hour GAGAS CPE requirement or other requirements that would enhance auditor proficiency in GAGAS.

Item 4 Response-

The Division recommends adding, “Writing GAGAS Findings.”

- The content from the GAGAS guidance document on CPE (GAO-05-568G) is largely incorporated into chapter 4. We plan to retire the guidance document when the new GAGAS is issued. (paras. 4.26 through 4.50) - Is there any additional application guidance that should be included in the GAGAS revision to enable auditors and audit organizations to effectively implement the CPE requirements given the planned retirement of the CPE guidance document?

Item 5 Response-

The Division believes the proposed revision is adequate and that no additional guidance is required.

- In chapter 5 (“Quality Control and Peer Review”), the sections on quality control and external peer review are expanded to harmonize with other standards and promote consistency in practice across the range of GAGAS auditors. - Are the changes to the quality control and external peer review sections appropriate and reasonable?



STATE OF TENNESSEE
COMPTROLLER OF THE TREASURY
DEPARTMENT OF AUDIT
DIVISION OF COUNTY AUDIT

SUITE 1500
JAMES K. POLK STATE OFFICE BUILDING
NASHVILLE, TENNESSEE 37243-1402
PHONE [REDACTED]

Item 6 Response-

The Division agrees in general with the proposed revisions in Chapter 5. We take exception to the language and requirements in 5.22. "The audit organization should assign responsibility for each engagement to an engagement partner or director." It seems this language is written from the viewpoint of a CPA Firm without regard to the different types of organizations that perform audits of governments. We are a "State Audit Shop". As such, it might be argued that the Department of Audit only has one partner, the Comptroller of the State of Tennessee. Or, looking at it a different way, it might be argued that the Division of Local Government Audit only has one partner, our Director. Or looking at it from still another way, it might be argued that our Division only has one partner, the Assistant Director over all of our audits. In fact, the responsibility you are referencing to a "partner or director" in our organization is delegated to a mid-level manager who directly supervises three or four in-charge field supervisors. Our structure accomplishes exactly what GAGAS is attempting to require, but in a different way. The mid-level managers in our authority structure are very close to the audit process, auditors, and the audit clients.

The language in 5.22 does not seem to allow for alternative authority structures. The language should be changed to allow for alternative authority structures that accomplish the same purpose.

7. In chapter 5 ("Quality Control and Peer Review"), peer review requirements are categorized by requirements for (1) audit organizations affiliated with recognized organizations and (2) other audit organizations. (paras. 5.63 through 5.113) - Are the peer review requirements for each category of audit organization clear?

Item 7 Response-

The language is clear to the Division. We participate in peer review through NSAA. We are not convinced the additional guidance will be clear to audit organizations not affiliated with one of the five recognized organizations.

Page 4 of 6

8. Chapter 7 ("Standards for Attestation Engagements and Reviews of Financial Statements") is expanded to incorporate by reference Statement on Standards for Accounting and Review Services No. 21, section 90, *Review of Financial Statements*, and includes additional requirements and guidance for reviews of financial statements conducted in accordance with GAGAS. (paras. 7.68 through 7.80) - Please comment on the expanded requirements and application guidance.



STATE OF TENNESSEE
 COMPTROLLER OF THE TREASURY
 DEPARTMENT OF AUDIT
 DIVISION OF COUNTY AUDIT
 SUITE 1500
 JAMES K. POLK STATE OFFICE BUILDING
 NASHVILLE, TENNESSEE 37243-1402
 PHONE (██████████)

Item 8 Response-

Our Division does not perform attestation engagements.

9. In chapter 8 (“Fieldwork Standards for Performance Audits”), internal control considerations are expanded to reference the 2014 *Standards for Internal Control in the Federal Government* and *Internal Control – Integrated Framework*. (paras. 8.37 through 8.65) Do these sections clearly describe ways auditors assess internal control on performance audits?

Item 9 Response-

Our Division does not audit under the performance standards.

Additional Responses -

10. *In chapter 6 (“Standards for Financial Audits”), definitions are provided for both “Waste and Abuse, respectively in paragraphs. 6.17 and 6.18. Paragraph 6.18 clearly states that abuse is subjective and auditors are not required to perform procedures to detect abuse in financial audits. This makes good sense. However, paragraph 6.17, which defines waste, does not state that waste is subjective and that auditors are not required to detect waste. This needs to be corrected. Waste, in our judgment, is more subjective than abuse.*

In addition, the Division does not believe there is a clear enough distinction between the definitions of waste and abuse for the average reader to understand or for an auditor to clearly use the terminology in a finding. The definition of abuse covers every part of the definition of waste. We recommend drawing a clearer distinction between the meaning of the two words or simply combining “Waste and Abuse” into a single definition.

11. *Almost all compliance findings have as their basis, a lack of internal controls. By intentionally emphasizing internal controls as a cause, GAO may be unintentionally diminishing the recognition of other causes for noncompliance, for example negligence. Internal controls may become the easy default cause. See various paragraphs (e.g. 6.20).*

Page 5 of 6

12. *The Division supports the idea of a paragraph such as 1.23 to define terms used in GAGAS. This is a good idea. The Division supports expanding the list of terms to include other relevant terms such as, Internal Control, Findings, Waste/Abuse, Material Noncompliance, Attestation Engagement, Performance Audit, Financial Audit, etc. Even though these terms may be adequately defined elsewhere, if you are going to include a list of defined terms, the list should be more inclusive and perhaps included as a preface rather than in the first chapter. We recommend locating every “term” that is defined in each chapter and including those terms in*



STATE OF TENNESSEE
COMPTROLLER OF THE TREASURY
DEPARTMENT OF AUDIT
DIVISION OF COUNTY AUDIT

SUITE 1500
JAMES K. POLK STATE OFFICE BUILDING
NASHVILLE, TENNESSEE 37243-1402
PHONE [REDACTED]

the list which could be then described as a Glossary of Terms used in GAGAS. This would be a helpful tool.

- 13. Based on paragraphs 4.03 and 5.12c (and 4.04 – 4.10), the Division is left to wonder what a CPA Firm, that is just now getting into the governmental audit arena, must document as evidence of competence to perform an audit under GAGAS prior to performing the first audit. Competence is defined as a combination of education and experience (4.07).*
- 14. The Division believes the new flowchart for demonstrating compliance with the conceptual framework is an improvement over the old flowchart.*
- 15. The Division believes including information from the appendixes in the chapters is an improvement.*

If you have questions about the above responses, you may contact Jerry E. Durham at [REDACTED].

A handwritten signature in black ink that reads "Jerry E. Durham".

Jerry E. Durham, CPA, CGFM, CFE
Assistant Director for Research, Compliance, and Contract Review
Tennessee Comptroller of the Treasury
Division of Local Government Audit

On behalf of Jim Arnette, Director, Division of Local Government Audit