



DEFENSE CONTRACT AUDIT AGENCY
DEPARTMENT OF DEFENSE
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IN REPLY REFER TO

PAS 730.3.B.3

February 5, 2008
08-PAS-003(R)

MEMORANDUM FOR REGIONAL DIRECTORS, DCAA
DIRECTOR, FIELD DETACHMENT, DCAA

SUBJECT: Audit Guidance on the July 2007 Revision to the Generally Accepted Government Auditing Standards (Yellow Book)

Summary

This memorandum summarizes the significant changes to the generally accepted government auditing standards (GAGAS) as a result of the July 2007 revision to the Yellow Book and provides guidance on implementing those changes. In summary:

- The results of routine nonaudit services performed by FAOs (e.g., memorandum to requestor) should state that the work performed does not constitute an audit or attestation engagement under GAGAS;
- If an impairment to independence is identified after the audit report is issued, the FAO should assess the impact and coordinate with the region on its assessment;
- Guidance on documentation related to identifying potential personal independence impairments has been enhanced to include (1) documenting the accomplishment of the mandatory annual independence training and signing of independence statements and (2) where to file auditor independence statements and recusal/disqualification letters;
- Auditors should communicate with the appropriate contractor representatives during the audit, hold the annual program plan meeting at major contractor locations with top contractor representatives, and at CAC locations invite the contractor's audit committee to attend; and
- The audit report shells for operations audits (activity codes 10501, 10502, and 10503) have been revised to include new GAGAS audit report language for performance audits.

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Background

On July 27, 2007, the Comptroller General of the United States issued the 2007 Revision of Government Auditing Standards (the Yellow Book), which supersedes the 2003 Revision. For financial audits and attestation engagements, the new standards are effective for audits of periods beginning on or after January 1, 2008. For performance audits (e.g., operations audits), the revised standards are effective for audits beginning on or after January 1, 2008. Early implementation is permissible and encouraged. This guidance is effective immediately.

Guidance

A brief summary of the significant changes to the GAGAS and the implementing guidance is presented below. GAGAS changes related to assessing the independence of external technical specialists and reporting internal control deficiencies will be covered in separate guidance memorandums.

Nonaudit Services

When an audit organization performs nonaudit services for an entity for which it also performs GAGAS engagements, the revised standards require the audit organization to communicate to certain parties, as appropriate, that the work does not constitute an audit under GAGAS (GAGAS 1.33).

Current DCAA guidance already states that correspondence regarding nonaudit services should not assert that the nonaudit services were conducted in accordance with GAGAS (CAM 2-106). To comply with the revised standards, the following statement has been added to the Other Audit Guidance (OAG) pro forma memorandum for nonmajor incurred cost desk reviews that is delivered by APPS and available on the DCAA Intranet. Memorandums to contracting officers on the results of other nonaudit services performed by FAOs should also include the following statement.

The scope of the work performed does not constitute an audit or attestation engagement under generally accepted government auditing standards.

Independence Impairments Identified after Report Issuance

If an impairment to the auditor's independence is identified after the audit report is issued, the revised standards require audit organizations to assess the impact and communicate the impairment to certain parties if the audit organization determines that it did not comply with GAGAS and the audit report was impacted (GAGAS 3.06).

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It is DCAA's policy that auditors with an impairment to independence will not work on the affected assignment (CAM 2-203c). In the rare event that an independence impairment is identified after the audit report is issued, the FAO will assess the impact and coordinate its assessment with the regional office, which should coordinate with Headquarters, Policy, Auditing Standards Division (PAS). If it is determined that the FAO did not comply with GAGAS and that the audit report was impacted, the impairment will generally be communicated to the parties included on the report distribution.

Documentation Related to Independence

The revised standards added an explicit requirement for audit organizations to maintain documentation of steps taken to identify potential personal independence impairments (GAGAS 3.08f).

DCAA's Quality Control System already contains policies and procedures to identify impairments and requires FAOs to document resolution of impairments (CAM 2-S103.1b(5)). To enhance compliance with the standards, that guidance will be revised to include the following requirements:

- Regional Directors will be required to provide an annual certification on the accomplishment of the mandatory annual independence training and signing of the independence statements to the Director. This certification will be included as a separate statement as part of the annual CPE certification of compliance issued in accordance with DCAAM 1400.1, Personnel Management Manual (PMM), Chapter 21, Section 1-5g.
- FAOs will maintain the most current independence statements as a part of the FAO's Supervisory Personnel Records under file code series 371.2 (see Chapter 71 of the DCAAM PMM and DCAAM 5015.1, Files Maintenance and Disposition Manual).
- Auditor recusal/disqualification letters will also be maintained as a part of the FAO's Supervisory Personnel Records. When the circumstances that result in an independence impairment under GAGAS also result in a conflict of interest under Government ethics regulations, DCAA General Counsel (DL) procedures require that a copy of the recusal/disqualification letter also be provided to the Agency's Ethics Official (i.e., DL).

Chapter 21 and Appendix A of Chapter 71 of the DCAA PMM will be revised accordingly.

Auditor Communication

Communications with contractor personnel during an audit that were required to be made to appropriate officials of the audited entity under the 2003 Revision of GAGAS now must be made to "those charged with governance," as well as entity management. Those charged with

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governance may be comprised of the same individuals of entity management that are responsible for overseeing the financial reporting process, subject matter, or program under audit and related internal controls (GAGAS 6.07 and 6.56).

General audit guidance concerning auditor communication with the contractor is in CAM 4-300. We will clarify that section, as well as related sections of CAM, to enhance our compliance with the standards. Auditors should hold audit conferences (e.g., entrance and exit conferences) with the appropriate contractor representatives. This will generally be the corporate controller, chief financial officer or their designated representative, e.g., audit liaison. Draft audit results should be provided to contractor officials with the authority to resolve those issues. The annual program plan meeting at major contractor locations will be held with top contractor representatives; e.g., the corporate controller or chief financial officer. At CAC locations, the contractor's audit committee should also be invited to attend the annual program plan meeting.

Report Language for Operations Audits

DCAA operations audits are performed under the GAGAS standards for performance audits. The audit report language regarding the auditors' compliance with GAGAS has been revised for performance audits. The revised language specifically states that the audit was planned and performed to obtain sufficient, appropriate evidence to provide a reasonable basis for the findings and conclusions based on the audit objectives (GAGAS 8.30). The audit report shells for activity codes 10501, 10502, and 10503 have been revised to include the new GAGAS audit report language.

FAO personnel should direct questions to their regional POCs, and regional personnel should direct any questions to Auditing Standards Division, at (703) 767-3274.

/Signed/

Kenneth J. Saccoccia
Assistant Director
Policy and Plans

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