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Washington, DC 20548

October 16, 2017

Mr. Samuel L. Burke, Chair
AICPA Professional Ethics Executive Committee
American Institute of Certified Public Accountants
1211 Avenue of the Americas
New York, New York 10036-8775

GAO's Response to the American Institute of Certified Public Accountants Professional Ethics Division's July 2017 Exposure Draft, *Proposed Interpretation and Other Guidance: State and Local Government Entities (Formerly Entities Included in State and Local Government Financial Statements)*

Dear Mr. Burke:

This letter provides GAO's comments on the American Institute of Certified Public Accountants (AICPA) Professional Ethics Division's exposure draft entitled *Proposed Interpretation and Other Guidance: State and Local Government Entities (Formerly Entities Included in State and Local Government Financial Statements)*. GAO promulgates generally accepted government auditing standards (GAGAS), which provide professional standards for auditors of government entities in the United States.

We appreciate the AICPA's efforts to obtain a wide range of perspectives on important matters relating to professional ethics in the accountability community. The AICPA Professional Ethics Executive Committee (PEEC) asked for responses to seven specific questions. Our responses follow.

Specific Comments

- 1. Are there any situations in which you believe the framework proposed will not reach the appropriate answer for the general fund? If so, please explain the situation and why you believe the appropriate answer would not be reached.**

We support PEEC's efforts to address auditor independence through enhanced application of a threats and safeguards approach. This approach is consistent with the GAGAS Conceptual Framework Approach to Independence. We do not envision any situations where the proposed framework will not reach an appropriate answer for the general fund.

- 2. Paragraph .03 of the proposed revised interpretation notes that when an interpretation of the "Independence Rule" (ET sec. 1.200.001) is applied in a state or local government environment and the interpretation uses terminology that is not applicable in this environment, the member should use their professional judgement to determine if there is an equivalent term and provides an example of one such situation in which PEEC believes this could occur. Are there any other**

terms or concepts included in the interpretations to the independence rules that PEEC should highlight as an example or consider providing additional application guidance for?

We believe that the example provided in the proposed interpretation is sufficient for generally illustrating the types of situations in which an auditor might need to apply professional judgment in applying the “Independence Rule.” The use of professional judgment in such situations is consistent with GAGAS paragraph 3.64, which notes that “Using professional judgment is important to auditors in carrying out all aspects of their professional responsibilities, including following the independence standards and related conceptual framework.”

3. Are the entities that would be included in the proposed definition of a *primary government* in paragraph .04a the entities that should be evaluated for independence purposes? If not, what entities should be evaluated for independence purposes, and should the term *primary government* be used to describe these entities?

We agree that the entities defined in paragraph .04a are the entities that should be evaluated for independence purposes.

4. PEEC believes that the criteria necessary to undertake the “more than minimal influence evaluation” in paragraph .14 is already available to the auditor as a result of other audit procedures. Do you believe that there are circumstances in which this information is not readily available to the auditor? If so, provide examples of circumstances in which a member may have difficulty in performing this evaluation.

We agree that in general the auditor should be able to perform an evaluation of the “more than minimal influence” criteria as a result of other audit procedures.

5. The “more than minimal influence over the accounting or financial reporting process over that fund or component unit” concept would require an analysis that is intended to be different than the analysis required for determining which entities are in a primary government’s financial reporting entity. In the context of the proposed guidance, is that objective clear? If not, how would you better describe the analysis?

We believe that the objective to determine the “more than minimal influence over the accounting or financial reporting process over that fund or component unit” is clearly presented in the proposed interpretation.

6. Paragraph .13 provides a “best efforts” provision that addresses those situations in which a member is unable to obtain the information necessary to identify investments held by a financial statement attest client. Are there any other situations in which you believe a best efforts provision would be necessary, either upstream or downstream, because the financial statement attest client may have difficulty identifying all the entities required to be included in the financial reporting entity?

We are not aware of other situations in which a best efforts provision would be necessary.

7. Is it clear that the interpretation does not apply to an entity that provides grant funds to the financial statement attest client (or vice versa) unless that entity is a fund or component unit that would otherwise be covered by the interpretation? If not, provide examples of situations in which you believe additional guidance is needed.

We believe that it is clear that the interpretation does not apply in the circumstances described in question 7. We are not aware of situations in which additional guidance is needed.

Thank you for the opportunity to comment. If you have questions about this letter or wish to discuss any of our responses, please feel free to 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