



Solutions.

Character.

Depth.

New Yellow Book Standards for Performance Audits

Presentation to Virginia Government Finance
Officers Association

Fall Conference

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The Firm of Choice.



Session Objectives

- Performance audit process
- 2007 Yellow Book Changes
- Case study
- GASB Service Efforts and Accomplishments update





Performance Audit Definition

- A performance audit is an audit of sound financial management, namely of the economy, efficiency and effectiveness with which the audited entity has used its resources in carrying out its responsibilities.





Performance Audit Definition

- **Economy** requires that resources used be made available in due time, in appropriate quantity and quality at the best price
- **Efficiency** is concerned with the best relationship between resources employed and results achieved
- **Effectiveness** is concerned with attaining the specific objectives set and achieving the intended results





Performance Audits

- Examples of performance audits...
 - Were efficiency and effectiveness assessed?
 - Were criteria, or performance measures clearly identified?
 - What were the problems encountered?
 - Was there a relationship between audit objectives and management's assertions?





Yellow Book Chapter 7 - Overview

- **Audit must be planned:**
 - Define audit objectives
 - What the audit is intended to accomplish
 - Subject matter and performance aspects to be included
 - May include the potential findings and reporting elements expected to be developed.





Yellow Book Chapter 7 - Overview

- **Audit must be planned:**
 - Scope of the work
 - The boundary of the audit
 - Time period
 - Program or aspect of a program
 - Locations, documents and records, etc





Yellow Book Chapter 7 - Overview

- **Audit must be planned:**
 - Methodology
 - Nature and extent of audit procedures





Yellow Book Chapter 7 - Overview

- **Planning – the auditor should:**
 - Identify the potential criteria needed to evaluate matters
 - Identify sources of audit evidence and consider the amount and type of evidence needed
 - Evaluate whether to use the work of other auditors or subject matter experts





Yellow Book Chapter 7 - Overview

- **Planning – the auditor should:**
 - Assign sufficient staff and specialists with adequate professional competence
 - Communicate about planning and performance of the audit to management officials and those charged with governance
 - Prepare a written audit plan.





New Yellow Book Standards

- The old yellow book provided a “nuts & bolts” approach to a performance audit giving the minimum standards for planning, execution and reporting





New Yellow Book Standards-Framework

- The 2007 Revision places performance audit standards within a professional framework related to the concepts of:
 - Significance
 - Audit Risk
 - Sufficient appropriate evidence





New Yellow Book Standards - Flexibility

- Auditors are given a lot of latitude to make professional judgments to decide what makes sense in the circumstances based on the overarching requirement that they provide **reasonable assurance**





New Yellow Book Standards - Framework

- The 2007 Revision also requires that Audit objectives align with:
 - Evidence obtained, which must support
 - Findings and conclusions





Concept of Significance

Significance is defined as the relative importance of a matter within the context in which it is being considered, including quantitative and qualitative factors.

Such factors include the **magnitude** in relation to the subject matter of the audit, the **nature** and **effect** of the matter, the **relevance** of the matter, the needs and **interests** of an objective third party with knowledge of relevant information, and the **impact** of the matter to the audited program or activity.





Audit Risk

Audit risk is the possibility that the auditors' findings, conclusions, recommendations, or assurance may be improper or incomplete as a result of factors such as evidence that is not sufficient and/or appropriate, an inadequate audit process, or intentional omissions or misleading information existed due to misrepresentation or fraud.





Audit Risk

Auditors **must** plan the audit to reduce audit risk to an appropriate level for the auditors to provide reasonable assurance that the evidence is sufficient and appropriate to support the auditors' findings and conclusions.





Sufficient, Appropriate Evidence

Appropriateness is defined as a measure of quality of evidence that encompasses the relevance, validity, and reliability of evidence used for addressing the audit objectives and supporting findings and conclusions.

Sufficiency is defined as a measure of quantity of evidence used for addressing the audit objectives and supporting findings and conclusions.





Evidence and Overall Assessment

- Added a section describing the overall assessment of the collective evidence to support the findings and conclusions
 - Assessment of evidence depends on the nature of the evidence, how it is used, and the audit objectives



Evidence and Overall Assessment

- Evidence is not sufficient and appropriate when it:
 - Carries an unacceptably high risk that it could lead to an incorrect or improper conclusion
 - Has significant limitations
 - Does not provide an adequate basis for addressing the audit objectives or supporting the findings and conclusions





Evidence and Overall Assessment

- If the Auditor believes that sufficient evidence will not be available:
 - Revise audit objectives
 - Revise methodology and scope
 - Consider whether the lack of evidence is due to an internal control deficiency



Information Technology

- Added a section on information systems controls for the purpose of assessing audit risk and planning the audit





Risk of Fraud

- In planning the audit, auditors should assess risks of fraud occurring that are significant within the context of the audit objectives.



Legal and regulatory requirements contract provisions or grant agreements

Auditors should determine which laws, regulations, and provisions of contracts or grant agreements are significant within the context of the audit objectives and assess the risk that violations of those laws, regulations, and provisions of contracts or grant agreements could occur.





Audit Report

- Auditors should present sufficient, appropriate evidence to support the findings and conclusions in relation to the audit objectives.
- Auditors should consider the users of the report.





Audit Report

- Auditors should describe any report limitations or uncertainties with the reliability or validity of evidence.
- Auditors should place their findings in perspective.



Reporting Control Deficiencies

- Auditors should describe the scope of their work on internal control and report any deficiencies. Control deficiencies exist when:

“The design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, detect, or correct (1) impairments of effectiveness or efficiency of operations, (2) misstatements in financial or performance information, or (3) violations of laws and regulations, on a timely basis.”





Reporting Control Deficiencies

- A deficiency in **design** exists when:
 - A control necessary to meet the control objective is missing, or
 - An existing control is not properly designed, so that, even if it were to function properly, the control objective is not met.





Reporting Control Deficiencies

- A deficiency in **operation** exists when:
 - A properly designed control does not operate as designed, or
 - When the person performing the control does not possess the necessary authority or qualifications to perform the control effectively.





Reporting Control Deficiencies

- The yellow book also notes that the internal audit function is an important part of overall governance, accountability and internal control.





GAGAS Statement in Auditor's Report

When auditors comply with all applicable GAGAS requirements, they should use the following language in the report:

“We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.”





Effective Date of 2007 Revision

- Effective for performance audits beginning on or after January 1, 2008.





CASE STUDY





Family Violence Prevention Services, Inc. Battered Women and Children's Shelter of Bexar County, Texas – mission statement

- *“The Battered Women and Children's Shelter is a program of Family Violence Prevention Services, Inc., dedicated to breaking the cycle of family violence and strengthening families by providing the necessary tools for self-sufficiency through delivery of emergency shelter, transitional housing, education, effective parenting and early intervention with children and youth.”*





Goals of the program...

- *To provide victims of family violence with a place of safety*
- *To provide transition to self-sufficiency*
- *To provide counseling and support for women, children and families who are victims of family violence and in need of service, but not shelter*
- *To educate the public about family violence*
- *To serve as a catalyst for the prevention and intervention of family violence in the community*





Case Study - the performance audit

- **Audit objective: Evaluate the efficiency and effectiveness of the programs.**
- **Consider:**
 - What are the criteria?
 - What evidence should be obtained?
 - Will there be sufficient evidence to support a conclusion on efficiency and effectiveness?





Case study – criteria and evidence

- *To provide victims of family violence with a place of safety*

Efficiency

- *Operating budget*
- *# families served*
- *Occupancy rate*
- *Cost per day*

Effectiveness

- *Is it a safe place?*
- *Sources of referrals*
- *Is service well known, available to entire service area?*
- *Results of intervention?*
- *Follow-up?*





Case study – criteria and evidence

- *To provide transition to self-sufficiency*

Efficiency

- *Operating budget*
- *# of case files opened, pending and closed*
- *# families served*
- *Average stay at shelter*
- *Counselor case load*

Effectiveness

- *Results of intervention?*
- *Follow-up?*
- *Coordination with other agencies*





Case study – criteria and evidence

- *To provide counseling and support for women, children and families who are victims of family violence and in need of service, but not shelter*

Efficiency

- *Operating budget*
- *# of case files opened, pending and closed*
- *# families served*

Effectiveness

- *Sources of referrals*
- *Is service well known, available to entire service area?*
- *Results of intervention?*
- *Follow-up?*





Case study – criteria and evidence

- *To educate the public about family violence*

Efficiency

- *Operating budget*
- *Types of programs*
- *Outreach*

Effectiveness

- *New sources of referrals?*
- *Is there a decline in domestic violence*





Case study – criteria and evidence

- *To serve as a catalyst for the prevention and intervention of family violence in the community*

Efficiency

- *Operating budget*
- *Types of programs*
- *Outreach*

Effectiveness

- *New sources of referrals?*
- *Is there a decline in domestic violence?*
- *Impact on other agencies?*
- *Comparative data from similar cities?*





GASB PERFORMANCE AUDIT UPDATE

Service Efforts and Accomplishments





GASB Update

- GASB sets standards for financial reporting of governmental entities.
- For 20 years, it has discussed performance reporting or what GASB refers to as “Service Efforts and Accomplishments” reporting, or “SEA.”
- Not everyone agrees that the GASB should have a role in performance reporting...





GASB and the GFOA

- Government Finance Officers Association strongly opposes GASB involvement in SEA reporting
- Public policy statement in 2002:
 - “GFOA must go on record again, opposing in the strongest possible terms, the efforts of the GASB to play a role in the development of performance measures in the public sector.”





GFOA Position

- GFOA notes that performance measurement must be thoroughly integrated into the budgetary process.
- Therefore to be effective, performance measures must be ***specific*** rather than generic. That is, a performance measure is only relevant to the extent it is clearly linked to the goals and objectives of that particular government. These objectives will differ among governments.





GFOA position

- Because performance measures are budgetary, they fall outside the purview of accounting and financial reporting.
- GFOA doesn't buy the "accountability" mantra to justify expanding its jurisdiction.
- GASB would be usurping the powers of the democratically elected governing bodies to set policy. (By dictating measures, you dictate policy).





GFOA position

- GASB standards would be generic measures which would break the crucial link between goals and objectives.
- Involve external auditor, which would increase costs.
- GASB's expertise is limited to accounting and financial reporting. They don't have the expertise to set standards regarding the measure of the quality of services.





GFOA position

- “Voluntary” measures would not really be voluntary. The very existence of benchmarks established by a national standard-setting body would put pressure on governments to conform their own performance measures to GASB model measures.
- There is no such thing as a truly objective or neutral performance measure. What you measure will drive performance. It is unrealistic to believe that GASB mandated performance measures will be solely informational.





GFOA Position

- The GFOA policy document concludes:
 - GASB's efforts will not succeed in helping the cause of performance measurement.
 - Real progress must come from the governments themselves.
- Rather than waste scarce resources on SEA, GASB should return to its proper role as an accounting and financial reporting standard-setting body.





Recent Events

- In November 2006, the Financial Accounting Foundation (FAF) Trustees reaffirmed that GASB has the jurisdictional authority to include Service Efforts and Accomplishments in its financial accounting and reporting standards- setting activities.





Recent Events

- In December 2006, the GASB staff presented results of its Phase VI research to the Board.
- In January of 2007, the GASB held a roundtable meeting on SEA reporting in Washington.
- On April 6, 2007, GASB added project to assist governments that choose to report performance information.





GASB SEA Reporting Project

- Objectives:

- Develop and propose principles-based suggested guidelines that would help improve the *voluntary* reporting of SEA performance information.
- Amend appropriate paragraphs of GASB Concepts Statement 2, which currently refers to creating specific measures rather than guidelines.
- Encourage more state and local governments to voluntarily report such information.





GASB response to Critics

- The roundtable discussion in January 2007 allowed critics to meet directly with the GASB board.
- The GASB noted the opposing view that choosing what performance to measure is a public policy decision that should be made by elected officials based on their mission and goals and not by the GASB.





GASB response to Critics

- Based on that discussion and meetings with other organizations, the GASB decided to amend Concept Statement 2 to highlight that its role is limited to reporting and specifically state that:
 - GASB will not require Governments to report on performance
 - GASB will not establish goals and objectives for governments
 - GASB will not create specific performance measures
 - GASB will not set benchmarks or required levels of performance





GFOA vs. GASB

What do you think?

Expertise may be an issue.

GFOA does not come up with a better way to encourage performance reporting. Performance measurement has been discussed for over 20 years. How many governments have a truly meaningful performance measurement system?

Measuring performance is complex – outputs are misleading, outcomes are very difficult to measure.





GASB

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Yellow Book Performance Audits

QUESTIONS?

