



Federal CFO: GAO's "Yellow Book" 2017 exposure draft asks auditors to report waste

In April 2017, the Government Accountability Office (GAO) released an exposure draft to update the Government Auditing Standards (Yellow Book). The exposure draft is part of GAO's efforts to update audit requirements to meet new challenges and trends in financial reporting. The exposure draft includes proposed updates from continuing professional education (CPE) requirements to fieldwork and reporting. Of all of the changes being proposed, one of the most impactful changes to the Federal CFO is in the area of Fraud, Waste, and Abuse.

Currently, as part of the audit report, auditors are required to report on a number of key areas assessed during the financial statement audit. These include the auditor's opinion, significant deficiencies, material weaknesses, and fraud—if it meets the criteria outlined in the Yellow Book. The new exposure draft proposes auditors add a new element to this reporting—waste. Auditors may be required to report, in writing, findings of waste that are material to the financial statements or the agency's mission during the course of the audit.

Implications of the Updated Guidance for CFOs and Managers

Of the changes for the Yellow Book that are being proposed, Chapter 6: Standard for Financial Audits addresses the new requirements in the area of waste. The proposed changes require external auditors to perform additional procedures if they find instances of waste. Waste primarily relates to mismanagement, inappropriate actions, and inadequate oversight.



The exposure draft does not suggest auditors create specific procedures to identify instances of waste. If waste has been identified during the audit, waste is handled in a manner similar to what happens if instances of fraud have been identified. The independent auditor must determine if the waste is quantitatively or qualitatively material to the financial statements or other financial data significant to audit objectives. If the discovered waste is deemed material, the auditor must report the criteria, condition, cause, and effect of the identified waste. It is important to note that the cause may include factors beyond management's control.

The proposed determination of materiality for waste is unique in concept. Many CFOs consider materiality to be solely a quantitative measure. The exposure draft suggests that the materiality of waste is determined either quantitatively or qualitatively. Qualitative materiality could include organizational structure, employee qualifications, project requirements, etc. The exposure draft did not provide additional information on what would be deemed material qualitative factors.

Considerations and Next Steps for CFOs and Managers

The proposed change can truly affect the operations of an agency. The proposed inclusion of material waste in an independent auditor's report is a way to increase transparency and efficiency in an Agency's operations. This additional requirement can be used by Federal CFOs as a tool to achieve greater transparency in funds execution and tax payer accountability and emphasize compliance with regulations (e.g. GAO Green Book, principle 8).

Federal CFOs should consider the following steps to prepare for this new requirement:

- Review existing projects and identify programs that create material balances to the financial statements
- Prepare program managers with material projects for possible additional discussions with independent auditors
- Communicate to program managers the importance of reducing waste within the organization
- For known programs that may raise questions, prepare discussion points to explain the circumstances around project over-runs

- Review the management internal control programs by assessing the following:
 - Control gaps that can mitigate the risk of waste
 - Compliance with GAO Green Book with particular attention to Principle 8—Assess Fraud Risk
 - Compliance with the Fraud Reduction and Data Analytics Act (FDRAA)
 - Compliance with Improper Payments Elimination and Recovery Improvement Act (IPERIA) to determine if there are any gaps related to Improper Payments
- Review policies and procedures and assess if they sufficiently communicate best practices to avoid waste

With the information that comes from greater transparency, CFOs and Financial Managers can focus on projects and procurements that are at risk for fraud, waste, and abuse. With budgets shrinking, focusing expenditures on items that are vital to the agency mission becomes more crucial.

The comment period for the exposure draft ended July 6, 2017.

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Resources

GAO Yellow Book Exposure Draft: <https://www.gao.gov/products/GAO-17-313SP>

GAO Green Book: <http://www.gao.gov/assets/670/665712.pdf>

FDRAA: <https://www.congress.gov/114/plaws/publ186/PLAW-114publ186.pdf>

IPERIA of 2012: <https://www.gpo.gov/fdsys/pkg/PLAW-112publ248/pdf/PLAW-112publ248.pdf>

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