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U.S. Government Accountability Office
GreenBook@gao.gov

Re: Comments on Exposure Draft: *Standards for Internal Control in the Federal Government*

To Whom It May Concern:

The Association of Local Government Auditors (ALGA) appreciates the opportunity to respond to the GAO's exposure draft, *Standards for Internal Control in the Federal Government*. Our organization represents 300 audit organizations, totaling more than 2,000 members. This topic is of interest to our members, many of whose work involves evaluating internal control in local government agencies or providing assistance to management in establishing effective systems of internal control. We encourage individual audit organizations and members to comment independently, should they choose to do so.

We agree with the format and content of the 2013 exposure draft and believe it will be a useful tool for managers and auditors in government agencies. Our responses to the questions provided in the exposure draft and additional comments are as follows:

1. *Is the hierarchy of components, principles, and attributes clearly explained?*

Yes, we believe hierarchy of components, principles, and attributes is clearly explained and facilitates understanding and implementation of the standards.

2. *Are there any internal control concepts unique to the government environment that should be in the Green Book that are not currently included?*

Generally, no. It recognizes that management determines how to appropriately adapt the framework presented in the Green Book for an entity.

We appreciate the attention the Green Book gives to safeguarding of assets. This is an important issue for governments because their assets are public resources.

In an effort to further improve the standards, we suggest consideration be given to addressing the following concepts:

- Are there any additional challenges, requirements, or considerations for large, complex, and sometimes decentralized governments to help ensure adequate internal controls vs. smaller entities. Paragraph O4.04 discusses challenges for smaller entities only.
- What happens when the oversight body is not adequately performing its oversight responsibilities?

3. *Does the framework provide the necessary information to allow program managers to evaluate the internal controls for their programs?*

Yes. The revised standards are more detailed than the previous Green Book in providing guidance to managers to evaluate internal controls for their programs. The framework, composed of components, principles, and attributes, allows program managers to evaluate internal controls for their programs by providing a set of minimum requirements necessary to achieve the standards of internal control.

In addition, we suggest adding to the glossary a definition for the term “program” that aligns with that in Government Auditing Standards (Yellow Book) 2.10 to clarify the broad nature of activities to which the Standards for Internal Control can be applied.

4. *Does the Green Book provide adequate criteria for auditors?*

We believe that the intent for the Green Book to provide criteria for auditors can be enhanced by adding the following language to the Foreword section of the Overview and to Paragraph O2.02:

“The Green Book may also be used as criteria by auditors in federal, state, local, and quasi-governmental entities, as well as not-for-profit organizations, when evaluating whether internal controls have been properly designed and implemented and are operating effectively.”

We also believe that the ability of the Green Book to provide adequate criteria for auditors can be improved. Please see the response to Question #5 for more details.

5. *Are the requirements for management to design, implement, and operate an internal control system clear, understandable, and adequate?*

The ability of the Green Book to set expectations for managers and provide criteria for auditors can be improved. Specifically, the Green Book states that the requirements have been “clearly marked” by the terms “must” and “should” (page 3, item 2, last paragraph). However, the Green Book does not explain the degree of responsibility imparted by each term as is done in the Yellow Book (i.e., unconditional vs. presumptively mandatory requirements). The lack of explanatory language makes it appear that managers are equally responsible for adhering to standards using either term. In addition, the term “should” is defined a second time under Paragraph O2.05 as denoting “a principle or attribute statement.” This creates an opportunity for confusion, as the first definition imparts responsibility on managers to follow standards while the second implies that the term “should” just helps managers categorize the standards.

Also, the only paragraph in the Green Book that uses the term “must” is O2.01: “An entity **must** have an effective internal control system to comply with the standards.” An effective internal control system is later defined in Paragraph O3.01 as providing reasonable assurance that the organization will achieve its objective, which requires each of the five components, 17 principles, and relevant attributes to be effectively designed, implemented, and operating. Yet Paragraph O2.06 provides managers the ability to determine that a principle or attribute is not relevant and therefore not necessary for an effective internal control system. These sections seem to form a core set of expectations of the standards; however, it is left to the reader to link them together.

To improve clarity for managers and auditors, suggest the following:

- Add language to O2.01 in the third sentence to state, “The standards provide criteria, *but not specific practices*, for assessing ...”
- Remove the language addressing the term “should” from Paragraph O2.05. The structure of the Green Book already clearly identifies principles and attributes of each component without this designation.
- Add explanatory language for the difference in responsibility imparted by the terms “must” and “should” in item 2 under “How to Use the Green Book.” This language could be the same as that used in the Yellow Book for these two terms.
- Add summary language that pulls together the basic architecture of compliance with the standards. This language could be included at the end of the “How to Use the Green Book” section as a primer. Possible language includes:
 - “An entity must have an effective internal control system to comply with these standards. Effective internal control systems must have components, principles, and attributes which are effectively designed, implemented, and operated by management:
 - o All five components **must** be addressed.
 - o All 17 principles and related attributes **should** be addressed unless management determines a particular item is not relevant (see O2.06). Details regarding these requirements and others are explained in the following standards.”

6. Is the evaluation of deficiencies discussion clear, understandable, and adequate?

Overall, yes. Paragraph O3.05 describes the difference of evaluating design of internal controls compared to evaluating implementation, and Paragraph O3.06 describes evaluating the operational effectiveness. Paragraphs O3.07 through O3.11 discuss how to evaluate the identified deficiencies in terms of significance, correlation, and impact of the deficiencies, starting from the attribute, then principle, then component.

Certain improvements are suggested in Question #8 below.

7. Are the roles, divisions, and overlaps of responsibility for the oversight body, management, and personnel clear, understandable, and adequate?

Paragraph O2.14 acknowledges that “the five components are discussed in the context of the management of the entity. However, everyone in the organization has a responsibility for internal control.” The roles and responsibilities of the oversight body and management are clear, understandable, and adequate throughout the document.

We find the description of roles and responsibilities of personnel are more general in the exposure draft and perhaps require more detailed guidance in the form of examples or scenarios. We suggest that consideration be given to the following points:

- Paragraph O2.14 describes generally that “Personnel help management design, implement, and operate an internal control system and are responsible for reporting issues noted in the entity’s operations, compliance, or reporting objectives.” Another general statement is made under the Control Environment component, Principle 4: Management’s Commitment to Competence. This attribute of establishing expectations of competence states that “Personnel need to possess and maintain a level of competence that allows them to accomplish their assigned responsibilities” (Paragraph 4.06).
- Under Principle 12: Implement Control Activities, the attributes are a) to document the responsibilities through policies, and b) to perform periodic review. There is not an attribute to actually implement the activity. If there was another attribute on the actual implementation, one element of that attribute could be a detailed description of the roles and responsibilities of personnel to implement the control activities for their assigned responsibility (which is also the last sentence of Paragraph 12.05).
- Paragraph 14.08 states that personnel “utilize separate reporting lines to go around upward reporting lines when these lines are compromised,” and that, “Laws and regulations may require entities to establish separate lines of communication.” Some government agencies have even formalized the duty of personnel to report allegations of fraud and wrongdoing. Consider rewording to, “Laws and regulation may require entities to establish separate lines of communication and require personnel to report allegations of fraud and wrongdoing.”
- Footnote 7, consider including a reference to Paragraph 14.08 for further discussion of upward reporting lines.
- Paragraph 17.05 says, “Personnel communicate these issues internally to the person in the key role responsible for the internal control or associated process and to at least one level of management above that individual.” Suggest adding the word “should” after “Personnel” to indicate that this is a requirement. Also add language to Paragraph 3.14 stating that the policies and procedures management develops should describe the process for communication of such issues.

8. *Are the documentation requirements included in the Green Book clear, understandable, and adequate?*

Overall, yes. Where documentation is required to demonstrate the design, implementation, and operation of the control attribute, principle, and/or component, the guidance is clear, understandable, and adequate. Further, Paragraphs O4.08 and O4.09 acknowledge that “These attributes represent the minimum level of required documentation in an entity’s internal control system. Management exercises judgment in determining what additional documentation may be required beyond these attributes for an effective internal control system.” We like that the documentation requirements impose on management in governmental entities a requirement similar to that required of corporate executives under the provisions of the Sarbanes-Oxley Act. We believe that requiring government managers to document their system of internal control provides a significant opportunity for strengthening internal control systems in governmental entities.

We suggest, however, improvement to the documentation requirements for the Monitoring component of internal controls. Both of the principles for this component, Principle 16: Perform Monitoring Activities, and Principle 17: Remediate Deficiencies, only briefly describe the requirement to “document the results of ongoing monitoring and separate evaluations to identify internal control issues” (Paragraphs 16.12 and 16.13), to “document internal control issues and determine appropriate corrective actions for internal control deficiencies on a timely basis” (Paragraphs 17.07 and 17.08), and to “document corrective actions to remediate internal control deficiencies on a timely basis” (Paragraphs 17.09 and 17.10). If documentation is critical to effective internal control systems, providing more guidance, perhaps in the form of examples, should be considered. Because documenting internal controls can be time-intensive and costly, the guidance should also be more specific as to the amount of documentation required. We suggest that the guidance allow using a risk-based approach to document the processes that pose the greatest risks that would prevent an entity from achieving its operational, reporting, and compliance objectives.

9. *Is there a need for additional internal control implementation guidance? If so, what form should it take?*

Consideration should be given to providing additional guidance included in responses to Questions #7 and #8 above. We suggest that such guidance be provided in the form of a question and answer document.

10. *Is this Green Book written in such a way to allow state, local, and quasi-governmental entities, as well as not-for-profit organizations, to adapt it for their own use?*

We believe that the Green Book is written in such a way to allow state, local, and quasi-governmental entities, as well as not-for-profit organizations, to adapt it for their own use. Taking the word “federal” out of the internal control reporting objective (Page 4) that was in the 1999 Standards helps achieve this. We also believe that addressing small entities (Paragraph O4.04) helps suggest that the Green Book is applicable to other levels of government since they are generally smaller than the federal government.

We believe, however, that there are several places where the Green Book could better demonstrate its applicability to state, local, and quasi-governmental entities, as well as not-for-profit organizations:

- O1.03 – Suggest deleting the word “federal” from the last sentence.
- O2.01 – Suggest deleting the word “federal” from the second sentence and adding a sentence indicating that these standards may also be used by state and local governments, quasi-governmental agencies, and not-for-profit organizations. Consider adding a sentence indicating that use of the standards is highly recommended for state and local governments, quasi-governmental agencies, and not-for-profit organizations that receive federal funds and have not drafted policies that outline expected internal controls or have not adopted an established internal control framework.
- O2.05 – Suggest deleting the word “federal” from the first sentence.
- O3.04 – Suggest adding a comment that other governmental entities and not-for-profit organizations can similarly prepare such a report.
- 2.07 – Suggest adding examples for other levels of government, such as governors’ offices, state legislatures, city and county councils, mayors, and offices of other elected officials; city managers; county executives; boards and commissions; and boards of directors for not-for-profit organizations.
- 12.07 – After “OBM,” suggest adding “at the federal level; state legislators; and city or county councils.”
- 15.12 – Suggest changing the language to something more generic as is in Paragraph 17.06, for example, “Government organizations not only report to the head of their government, legislators, and regulators, but to the general public as well.”
- Suggest making the title of the Standards more generic, such as “Standards for Internal Control in Government.” This would align with the Yellow Book, which is used by auditors in many state and local governments, although it was originally written for federal government auditors.
- In the third paragraph of the Foreword section of the Overview, consider adding a sentence indicating that these standards may also be used by state and local governments, quasi-governmental agencies, and not-for-profit organizations. Consider adding a sentence indicating that use of the standards is highly recommended for state and local governments, quasi-governmental agencies, and not-for-profit organizations that receive federal funds and have not drafted policies that outline expected internal controls or have not adopted an established internal control framework.

Other Comments: We offer the following additional comments:

- How to Use the Green Book – Suggest adding a reference to the Glossary for terms that are used throughout the Standards.
- O2.15 and Glossary – Suggest adding a definition of “external auditor” to the Glossary that aligns with the definition of an external auditor in GAGAS 3.27 – 3.30 to clarify that an external auditor includes those who are employees of the entity but report to the governing body or an independent audit committee, rather than to management.

- Additional clarity could be provided between the monitoring attributes of Principle 12: Implement Control Activities, and Principle 16: Perform Monitoring Activities. It is not clear whether the attribute at Paragraph 12.06 to perform periodic review of the implementation of control activities is either exclusive from, or related to the monitor internal control element described in Paragraph 16.08: Ongoing Monitoring of the Design and Operating Effectiveness of the Internal Control System. Consider including a footnote reference, if applicable, between Paragraph 12.06 and 16.08.
- 16.10 – Suggest removing “may be mandated by law” from the second sentence and adding a phrase at the beginning of the third sentence that says, “Agencies are encouraged to use audits and other evaluations since they provide...”
- Typographical – In the 4th bullet on pg. 6, insert “of” after “quality.” In the second sentence of the “Establishment” paragraph on pg. 48, insert “to” after “relating.”

We appreciate the opportunity to respond to this proposal.

Respectfully submitted,



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