February 14, 2014

James Dalkin
Director, Financial Management and Assurance
U.S. Government Accountability Office
441 G Street, NW
Washington, DC 20548

Dear Mr. Dalkin:

The American Institute of Certified Public Accountants (AICPA) is the world's largest member association representing the accounting profession, with more than 394,000 members in 128 countries and a 126 year heritage of serving the public interest. AICPA members represent many areas of practice, including business and industry, public practice, government, education and consulting. The AICPA sets ethical standards for the profession and U.S. auditing standards for audits of private companies, non-profit organizations, federal, state, and local governments. It also develops and grades the Uniform CPA Examination and offers specialty credentials for CPAs who concentrate on personal financial planning; fraud and forensics; business valuation; and information technology.

On behalf of the AICPA and its Governmental Audit Quality Center, we appreciate the opportunity to comment on the 2013 Exposure Draft (ED) of *Standards for Internal Control in the Federal Government* (Green Book). The AICPA supports the GAO's efforts to update the Green Book to reflect major changes in the accountability and financial management profession and to emphasize specific considerations applicable to the government environment, including the adaption of the Committee of Sponsoring Organizations of the Treadway Commission's *Internal Control—Integrated Framework* (COSO). However, we do have several concerns, observations, and recommendations that we would like to bring to the attention of GAO, particularly in light of the recent grant reform regulation issued by the U.S. Office of Management (OMB) titled, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Grant Guidance), which may expand the use of the Green Book by non-federal entities (e.g., states, local governments, and non-profit organizations). The remainder of this letter summarizes our detailed comments.

Adaptations of COSO Should be Limited to Government Environment Differences Only to Avoid Confusion. While the Green Book applies by statute to federal agencies, it now appears to have been made more directly applicable to non-federal entities by the Uniform Grant Guidance which states that non-federal entities must "establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms

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and conditions of the Federal award." The Uniform Grant Guidance goes on to indicate that non-federal entities should be in compliance with guidance in COSO and the Green Book. While OMB has stated publicly that its intent in identifying both the COSO and Green Book frameworks as recommended criteria was not intended to be presumptively mandatory, it appears there is a much broader constituency of entities, including some very small local governments and not-for-profit organizations, that may apply the Green Book. For this reason, we believe it is even more important that the Green Book only diverge from COSO for situations where the government environment is truly different. We noted a number of areas in the ED where GAO diverged from COSO language and it was unclear why a modification was needed for the government environment. For example consider the following:

> *Definition of Internal Control.* The definition of internal control in the ED differs from the widely accepted definition in COSO, AICPA standards, and other national and international standards. It is unclear what aspect of the government environment resulted in a need for GAO to modify the COSO definition.
>
> *Rewording of Principles*. In a number of cases, the various principles under each component of internal control were reworded. It is not apparent why some of those changes were needed to address the government environment. For example, as it relates to the risk assessment component, COSO includes a principle that states: "The organization <u>identifies</u> and <u>assesses</u> changes that could significantly impact the system of internal control." The Green Book principle states: "Management should <u>identify</u>, <u>analyze</u>, and <u>respond to significant changes</u> in the internal control system." There were a number of other principles that were similarly modified and the intent of these modifications is unclear.

To avoid confusion for both federal and non-federal entities, we recommend GAO re-examine the definitional and wording modifications that were made to the Green Book to determine whether there truly is a need for the change. If a determination is made that a change is necessary to address the government environment, it would be helpful if the Green Book could include a summary or appendix that identifies the rationale for the difference and how that difference would be operationalized differently than COSO. Another approach the GAO could take is to conform the Green Book framework more directly to the COSO framework and then include application material and illustrations that illustrate how a government environment may differ.

Clarification About "Requirements" Contained in the Green Book. The foreword to the ED indicates that the Green Book's internal control framework may be applied to entities other than federal agencies such as state and local governments, as well as not-for-profit organizations. It also states that management of these entities would determine how to adapt the framework. However, section O4.10 (page 18) states that if management elects to use the Green Book as criteria, management follows all applicable requirements presented in the Green Book. These two sections seem inconsistent. GAO should clarify the language in the foreword and section O4.10, particularly in light of the issuance of the Uniform Grant

Guidance. Additionally, clarification should be provided regarding the use of "must" and "should" throughout the document. As it reads currently, it is not clear whether the Green Book is a framework or a set of standards that require all elements to be followed in order for an entity to be in compliance with the Green Book. A related area of concern is in section O2.05 (page 6) which indicates that the Green Book uses "should" to "denote a principle or attribute statement" implying that the term "should" merely categorizes these elements while the "How to Use the Green Book" section (page 5) indicates that "should" and "must" mark requirements throughout the Green Book. GAO should clarify the use of "should" and whether all principles and attributes must be complied with.

Level of Detail Needed Seems to be Significant. The Green Book requirements for an effective internal control system appear to be at a more detailed level than COSO. That is, COSO only requires that each of the five components and relevant principles be present and functioning while the Green Book seems to indicate that relevant attributes are also required. Section O3.09 (page 15) states, "The Green Book describes each attribute in general terms. For each attribute, management considers the elements underlying the attribute and whether controls are properly designed, implemented, and operating effectively to achieve each element of the attribute. If one or more of the elements are not achieved, then a deficiency in internal control exists." This difference between COSO and the Green Book would seem to have the potential to lead to a significant level of detail. Is this the GAO's intent? Section O2.06 (page 6) suggests that relevance can be a filter at the components, principles, and attributes level, but it is not clear how relevance determinations are to be made at the attributes level for "elements" or if the same context exists. It is also not clear how cost benefit considerations inform relevance determinations. These are all areas that GAO should consider clarifying to ensure an appropriate understanding.

Application of the Green Book to Smaller Entities. Now that the Green Book may be applied by smaller non-federal entities, including non-profits, GAO should consider adding application material that "downsizes" or makes more practical the framework for smaller entities.

Level of Documentation Required. The minimum level of documentation is set forth in O4.08 (page 17) of the ED for only five attributes. Section O4.09 (page 17) and section 3.14 (page 29) discuss management using professional judgment in terms of the extent of documentation otherwise. While we support the use of judgment, in light of the fact that large federal entities down to small governments and non-profits will be applying the Green Book framework, we believe it would be helpful for GAO to consider adding additional guidance to assist management in applying its judgment.

Consider Adding Illustrations or Application Material that Focuses on Internal Control over Compliance. With the issuance of the new Uniform Grant Guidance, the GAO should consider more directly addressing internal control over compliance (e.g., the requirements established in the Uniform Grant Guidance) for grant recipients in the Green Book. For example, the addition of application material or an appendix on internal control over compliance would help grantees and auditors who may be familiar with COSO and internal

control over financial reporting to more fully comprehend how internal control over compliance falls into the Green Book framework.

Green Book Should More Directly Identify Application Material. Section O2.07 states that the Green Book contains additional information in the form of application material. It also goes on to state that the words "may," "might," and "could" are used to describe examples of procedures that may be appropriate for an entity to apply. The Green Book's usability could be improved if GAO considered identifying more specifically, where the application material appears. For example, a specific identification of where the sections containing application material appear could be included in an Appendix.

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We appreciate the opportunity to provide these comments to the GAO. If you would like to further discuss these comments, you can contact us at [redacted] or at [redacted]

Sincerely,

[redacted]

[redacted]

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