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AICPA Proposed Statement on Standards for Attestation Engagements: Reporting on an Examination of Controls at a Service Organization Relevant to User Entities’ Internal Control Over Financial Reporting: Clarification and Recodification

Dear Ms. Macey:

This letter provides the U.S. Government Accountability Office’s comments on the American Institute of Certified Public Accountants’ (AICPA) exposure draft on examining controls at service organizations.

We support the AICPA’s efforts to clarify the attestation standards regarding examining controls at service organizations. We are providing comments on the application of the definition of fraud to service organization audits, proposed language relating to “intentional acts,” and on enhancing practitioners’ consideration of fraud during a service organization audit.

Definition of Fraud

As we considered how the definition of fraud proposed in Concepts Common to All Attestation Engagements would apply to an examination of controls at a service organization, we observed that the definition may not sufficiently clarify the parties to which it applies. The exposure draft of Concepts Common to All Attestation Engagements defines fraud as “an intentional act involving the use of deception that results in a misstatement on the subject matter or the assertion.” We understand that this chapter is still in draft form. We believe that the clarified attestation standards as a whole would benefit from a definition that indicates whether fraud includes fraud committed by third parties. Such an indication would provide valuable assistance to practitioners, including service auditors, as they plan and perform procedures related to fraud. We encourage the AICPA to consider revising the definition accordingly.

Intentional Acts and Fraud

Given the proposed requirements relating to the practitioner’s consideration of fraud in the proposed chapter Examination Engagements, we believe that the AICPA should consider whether intentional acts as discussed in the Examination of Controls at a Service Organization exposure draft should be referred to as fraud. According to paragraph 8.A39, the risks and control objectives related to service organization controls encompass
intentional and unintentional acts that threaten the achievement of the control objectives. Referring to these acts as fraud may add clarity to the requirements for service auditors.

**Requirements Related to Consideration of Intentional Acts or Fraud**

Regardless of whether references to “intentional acts” are changed to “fraud,” we believe that service auditors would benefit from an extended discussion of how such acts could affect a service organization’s ability to meet its control objectives. Given that service organization reports are intended for use by user entity auditors in conducting financial statement audits, we believe that the AICPA should consider whether the service auditor should perform certain procedures consistent with AU-C 240, *Consideration of Fraud in a Financial Statement Audit*, to identify the risk of material misstatement. These procedures could include the following:

- Discuss, among the members of the service audit team, the potential that the stated control objectives will not be achieved because of fraud.
- Make inquiries of management and others within the service organization to obtain their views about the risks that the stated control objectives will not be achieved because of fraud and how they are addressed.
- Consider whether one or more fraud risk factors exist.
- Consider other information that may be helpful in identifying risks that the stated control objectives will not be achieved because of fraud.

In addition, we believe that the application and other explanatory material would benefit from a discussion of the types of intentional acts or fraud (along with related risk factors) that may be relevant to a service audit, such as (1) management override of the controls specified in the description of the service organization’s system, (2) misappropriation of user entity assets by service organization personnel, and (3) false or misleading records or documents provided to user organizations for the transactions processed by the service organization that are the subject of the engagement.

We thank you for considering our comments on these important issues, and we would be pleased to clarify our responses to the exposure draft.

Sincerely yours,

James R. Dalkin
Director
Financial Management and Assurance