

THE PPC

GOVERNMENTAL UPDATE

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New SAS and SSAE on Materiality

In December 2019, the AICPA Auditing Standards Board (ASB) issued SAS No. 138, *Amendments to the Description of the Concept of Materiality*, as well as SSAE No. 20, with the same name.

Why Change?

The new SAS and SSAE make subtle changes to the definition of *materiality* so that it more closely aligns with those of the United States judicial system, SEC, PCAOB, and other U.S. standard setters. The new definition doesn't match any one definition exactly, but rather moves the definition closer to the definition currently used in practice by the various entities. The ASB doesn't believe that adoption of the new standards will significantly change current practice.

Old Definitions

The extant definition from AU-C 320.02 is "misstatements, including omissions, are considered material if they, individually or in the aggregate, could reasonably be expected to influence the economic decisions of users made on the basis of the

financial statements." The extant definition at AT-C 205.A17 and AT-C 210.A16 is "misstatements, including omissions, are considered to be material if, individually or in the aggregate, they could reasonably be expected to influence relevant decisions of intended users that are made based on the subject matter." The extant definitions were consistent with those used by the International Accounting Standards Board and the International Auditing and Assurance Standards Board.

New Definitions

The amended definition at AU-C 320.02 is "misstatements, including omissions, are considered to be material if there is a substantial likelihood that, individually or in the aggregate, they would influence the judgment made by a reasonable user based on the financial statements." The amended definition at AT-C 205.A17 and AT-C 210.A16 is "misstatements, including omissions, are considered to be material if there is a substantial likelihood that, individually or in the aggregate, they would influence the judgment made by intended users based on the subject matter."

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Reasonable User

AU-C 320.04 includes assumptions the auditor may make about what determines a reasonable user. Those assumptions aren't substantially changed by SAS No. 138.

Opinion Unit Concept

Remember that for audits of governmental entities, materiality is considered by the auditor individually for each opinion unit, and there are generally several of them. Auditors will want to consider how the materiality definition change applies to each opinion unit.

When Are the Changes Effective?

SAS No. 138 is effective for audits of financial statements for periods ending on or after December 15, 2020. SSAE No. 20 is effective for practitioners' examination and review reports dated on or after December 15, 2020. Early implementation is permitted.

Practical Consideration:

The full text of SAS No. 138 and SSAE No. 20 is available on Checkpoint at www.checkpoint.riag.com for users that subscribe to the content, and at www.aicpa.org.



Reporting SAS ED

The Auditing Standards Board continues to be fast and furious in the issuance of new auditing standards. In December 2019, the AICPA issued yet another proposed SAS, *Amendments to AU-C Sections 725, 730, 930, 935, and 940*. The proposal would primarily amend these sections to conform with recent changes to auditor reporting and developments in compliance auditing and other unique areas.

Recent Auditor Reporting Changes

In case you're struggling to keep up, the AICPA recently issued the following auditing standards that amend auditors' reporting:

- SAS No. 134, *Auditor Reporting and Amendments, including Amendments Addressing Disclosures in the Audit of Financial Statements*, which changes the form and content of the auditor's report. (For more information, see "**Future Changes to Auditor's Report**" in the December 2019 newsletter.)

- SAS No. 137, *The Auditor's Responsibilities Relating to Other Information Included in Annual Reports*, which amends guidance on the auditor's responsibility for other information as well as amends auditor's reporting related to other information. (For more information, see "**AICPA Issues SAS No. 137 on Other Information**" in the January 2020 newsletter.)
- SAS No. 138, *Amendments to the Description of the Concept of Materiality*, which makes subtle changes to the definition of *materiality* to converge it with the definitions used by the FASB and PCAOB, amends wording in the auditor's report related to materiality. (See the article in this newsletter.)

These standards are effective for financial statements of periods ending on or after December 15, 2020. SAS Nos. 134 and 137 do not permit early implementation.

Proposed Changes

AU-C-930, Interim Financial Information

Some governmental entities obtain reviews of their interim financial statements. The proposed changes to the reporting requirements in AU-C 930 include placing the auditor's review conclusion at the beginning of the review report on interim financial information. The proposed SAS would also revise the requirements for dating the review report.

AU-C-935, Compliance Audits

Compliance audits are common to governmental entities, as many are required to comply with *Government Auditing Standards* (the Yellow Book) or expend federal grants that require a single audit. In addition to conforming amendments for the issuance of SAS Nos. 134, 137, and 138, AU-C 935 would be revised for recent developments in the compliance area. Significant changes in the proposal include:

- Updated reporting requirements for reports on compliance and reports on internal control over compliance. The amendments address combined and separate reports, with an emphasis on combined reports, as these are most common in practice.
- Revised definition of *material noncompliance* to align with the description of materiality in SAS No. 138.
- Updated Uniform Guidance references (versus OMB Circular A-133).
- Revisions due to issuance of *Government Auditing Standards, 2018 Revision* (2018 Yellow Book) and

the OMB Compliance Supplement, including the types of requirements subject to audit.

- Refreshed appendix for the issuance of SAS Nos. 131 to 137.

AU-C-940, An Audit of Internal Control Over Financial Reporting That Is Integrated with an Audit of Financial Statements

Though not typically applicable to governmental entities, the proposed amendments to AU-C 940 revise the form and content of the auditor's report on internal control over financial reporting (ICFR) to also require the "Auditor's Responsibilities for the Audit of ICFR" section to include a statement that internal control over financial reporting is not effective if a material weakness exists. The proposed SAS includes referencing requirements when issuing a separate report on ICFR. Requirements are revised on reporting when there is a scope limitation. The proposed SAS also addresses situations when management includes additional information in management's report or in a document containing management's report and the related auditor's report.

Required Supplementary Information (AU-C 730) and Supplementary Information (AU-C 725)

Government financial statements often include required supplementary information and supplementary information. AU-C 725, *Supplementary Information in Relation to the Financial Statements as a Whole*, and AU-C 730, *Required Supplementary Information*, would be amended to conform with changes in SAS No. 137 on other information. The proposed revisions would require the auditor's report to refer to a separate section in the report (i.e., supplementary information, required supplementary information) rather than an other-matter paragraph.

Proposed Effective Dates

The exposure draft proposes the following effective dates, none of which may be early implemented:

- AU-C 725 and 730 amendments will be effective for audits of financial statements for periods ending on or after December 15, 2020, with early implementation not permitted.
- AU-C 930 amendments will be effective for reviews of interim financial information for interim periods of fiscal years beginning on or after December 15, 2020, with early implementation not permitted.
- AU-C 935 amendments will be effective for compliance audits for fiscal periods ending on or after December 15, 2020, with early implementation not permitted.

- AU-C 940 amendments will be effective for integrated audits for periods ending on or after December 15, 2020, with early implementation not permitted.

Practical Consideration:

As always, PPC will keep you informed of future developments related to this proposal in future newsletter articles.



Uniform Guidance Proposed Changes

On January 22, 2020, the Office of Management and Budget (OMB) published proposed revisions to sections of Title 2 of the Code of Federal Regulations (CFR) Subtitle A—OMB Guidance for Grants and Agreements. OMB states that the purpose of the proposed revisions is to reduce the burden on grant recipients; provide guidance on implementing new statutory requirements; and improve federal financial assistance management, transparency, and oversight.

Key Proposed Changes

Selected proposed changes important to auditors are as follows:

- Move all definitions to a new section, 2 CFR section 200.1, and replace CFDA number with *assistance listing number*.
- Clarify the meaning of *must* and *may*. (200.101)
- Clarify budget periods and expand the authority of agencies to terminate awards for noncompliance. (200.211)
- Prohibit federal awarding agencies from including references to non-binding guidance in the terms and conditions of federal awards. (200.211)
- Add regulations for agencies and non-federal entities to implement "Never Contract with the Enemy" for grants and cooperative agreements that are expected to exceed \$50,000. (200.215)
- Prohibit using government funds for contracts with entities that use covered technology. (200.216)
- Clarify how federal awarding agencies must measure a federal award recipient's performance. (200.301)
- Add informal procurement methods when the value of the procurement for property or services under a federal award does not exceed the simplified acquisition threshold. (200.319)

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- Add a new method that gives a nonfederal entity the responsibility for determining appropriate micro-purchase and simplified acquisition thresholds based on internal controls, an evaluation of risk, and its documented procurement procedures if its micro-purchase and simplified acquisition thresholds are different from the Federal Acquisition Regulation (FAR). (200.319)
- Add a domestic item preference for procurements. (200.321)
- Add a requirement that a pass-through entity is not required to use a *de minimis* indirect cost rate if the subrecipient has a federally approved rate. (200.331)
- Expand the monitoring requirement of a pass-through entity by adding that the pass-through entity is only responsible for resolving audit findings that are specifically related to their subaward. The pass-through entity is not required to address all of the subrecipient's audit findings. (200.331)
- Add that a pass-through entity may rely on the subrecipient's auditors and the cognizant agency's oversight for routine audit follow-up and management decisions. (200.331)
- Extend the final report submission and obligation liquidation periods from 90 calendar days to 120 calendar days for direct recipients and add measures that must be taken if the reports are not submitted on time. The submission periods for subawards (subrecipients submitting reports to the pass-through entity) would remain at 90 days. (200.343)
- Allow the use of the *de minimis* rate of 10% of modified total direct costs to all nonfederal entities (with certain exceptions). [Currently, the *de minimis* rate can only be

used for nonfederal entities that have never received a negotiated indirect cost rate. This change would expand the use of the *de minimis* rate for non-federal entities that have negotiated an indirect cost rate previously, but for some circumstances, the negotiated rates have expired (for example, due to breaks in Federal relationships and grant funding, or lack of resources for preparing an indirect cost proposal).] (200.414)

- Clarify the following: the applicability and documentation requirements when a nonfederal entity elects to charge the *de minimis* indirect cost rate, the pass-through entity responsibilities related in indirect cost rates and audits, and the applicability of 2 CFR to FAR-based contracts. (Various)

Auditors should be alert for the release of the final revisions. Guidance on the effective date of the final changes is expected to be included in the final Federal Register release.

Practical Consideration:

A tracked changes version of the proposed revisions and other 2 CFR proposed revisions resources are available at www.performance.gov/CAP/grants/. Access the tracked changes directly at www.performance.gov/CAP/innovation-sessions/Grants-CAP-Goal-Proposed-2CFR-Revision1.pdf.

