

**U.S. Department of Housing and Urban Development  
Office of the Inspector General**

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**SPECIAL ATTENTION OF:**

Office of Multifamily Development and  
Real Estate Assessment Center

**TRANSMITTAL**

Handbook No: 2000.04, REV-2, CHG-8  
Chapter Number: 2, Examples B, B-1 & B-2  
Issued: January 22, 2010

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1. This transmits Handbook 2000.04, REV-2, CHG-8, chapter 2, example B, example B-1, and example B-2, *Consolidated Audit Guide for Audits of HUD Programs* (Guide).
2. **Summary:** The Office of the Inspector General is in the process of updating the handbook and will release each chapter as it is completed. When all of the individual chapters of the Guide are revised, they will be consolidated into a revised Guide and issued as Handbook No. 2000.04, REV-3.

This handbook chapter's examples are a change to Handbook 2000.04, REV-2, chapter 2, examples B and B-1, issued March 2007. A change was necessary to comply with the requirements of American Institute of Certified Public Accountants Statement on Auditing Standards (SAS) 115 and to provide updated illustrations of the **Independent Auditor's Report on Internal Control Combined Report Applicable to Internal Control over Financial Reporting Based on an Audit of Financial Statements and Internal Control over Compliance for HUD-Assisted Programs**.

Example B-2 was added to illustrate how auditors would report when they have both material weaknesses and significant deficiencies.

This change serves as a reference for auditors who perform audits of U.S. Department of Housing and Urban Development (HUD) programs.

**3. Filing Instructions:**

The issuance of these examples cancels examples B and B-1 contained in chapter 2.

**Remove**

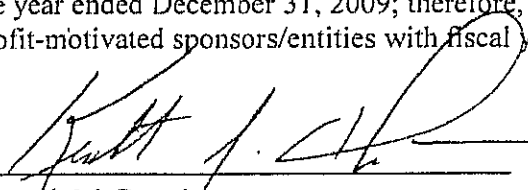
Examples B and B-1,  
chapter 2, dated March 2007

**Insert**

Example B, B-1, and B-2,  
chapter 2, dated January 22, 2010

**4. Effective Date:**

This change is effective immediately and should be used upon issuance. SAS 115 is effective for the year ended December 31, 2009; therefore, examples B, B-1, and B-2 shall apply to audits of profit-motivated sponsors/entities with fiscal years ending on or after December 31, 2009.

  
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Kenneth M. Donohue  
Inspector General, G

Example B

**Independent Auditor's Report on Internal Control  
Combined Report Applicable to Internal Control over Financial Reporting Based on an  
Audit of Financial Statements and Internal Control over Compliance for HUD-Assisted  
Programs**

**No Material Weaknesses, No Significant Deficiencies Identified<sup>1 2</sup>**

[Addressee]

We have audited the financial statements of [the entity] as of and for the year ended [date], and have issued our report thereon, dated [date]. We have also audited [the entity's] compliance with requirements applicable to major<sup>3</sup> U.S. Department of Housing and Urban Development (HUD)-assisted programs for the year ended [date], and have issued our reports thereon, dated [date].

We conducted our audits in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the *Consolidated Audit Guide for Audits of HUD Programs* (Guide), issued by the HUD Office of the Inspector General. Those standards and the Guide require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether [the entity] complied with laws and regulations, noncompliance with which would be material to a major HUD-assisted program.

Management of [the entity] is responsible for establishing and maintaining effective internal control over financial reporting and internal control over compliance. In planning and performing our audits of the financial statements and compliance, we considered [the entity's] internal control over financial reporting and its internal control over compliance with requirements that could have a direct and material effect on a major HUD-assisted program as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements and compliance but not for the purpose of expressing an opinion on the effectiveness of [the entity's] internal control over financial reporting and internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of [the entity's] internal control over financial reporting and internal control over compliance.

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<sup>1</sup> See example B-1 for an illustration of a report in which significant deficiencies were identified by the auditor but no material weaknesses were identified. See example B-2 for an illustration of a report in which both material weaknesses and significant deficiencies were identified. Example B-2 would also be used by the auditor for situations in which there were material weaknesses but no significant deficiencies were identified.

<sup>2</sup> Note that this combined report format is illustrative of one possible presentation. Auditors may choose to issue separate reports on internal control over financial reporting and internal control over compliance.

<sup>3</sup> The reference to major HUD-assisted programs here and throughout this report is used because the auditor's opinion on compliance runs to the major programs. However, when required by the *Consolidated Audit Guide for Audits of HUD Programs*, the auditor still has the responsibility to test compliance with specific requirements applicable to nonmajor HUD-assisted program transactions and issue the related nonmajor report, "Report on Compliance with Specific Requirements Applicable to Nonmajor HUD-Assisted Programs."

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct (1) misstatements of the entity's financial statements or (2) noncompliance with applicable requirements of a HUD-assisted program on a timely basis. A material weakness is a deficiency or combination of deficiencies in internal control such that there is a reasonable possibility that (1) a material misstatement of the entity's financial statements or (2) material noncompliance with applicable requirements of a HUD-assisted program will not be prevented or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting and internal control over compliance was for the limited purpose described in the third paragraph of this report and was not designed to identify all deficiencies in internal control that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control that we consider to be material weaknesses as defined above.

[We noted certain matters that we reported to management of [the entity] in a separate letter, dated [date].<sup>4</sup>]

This report is intended solely for the information and use of management, *[identify the body or individuals charged with governance]*, others within the entity, and HUD and is not intended to be and should not be used by anyone other than these specified parties.

[Signature]

[Date]

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<sup>4</sup> Certain chapters of the Guide require mention of the management letter in the independent auditor's report. Consult the Guide for further information.

## Example B-1

**Independent Auditor's Report on Internal Control  
Combined Report Applicable to Internal Control over Financial Reporting Based on an  
Audit of Financial Statements and Internal Control over Compliance for HUD-Assisted  
Programs  
Significant Deficiencies Were Identified--No Material Weaknesses Identified <sup>1</sup>**

[Addressee]

We have audited the financial statements of [the entity] as of and for the year ended [date], and have issued our report thereon, dated [date]. We have also audited [the entity's] compliance with requirements applicable to major<sup>2</sup> U.S. Department of Housing and Urban Development (HUD)-assisted programs for the year ended [date], and have issued our reports thereon, dated [date].

We conducted our audits in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the *Consolidated Audit Guide for Audits of HUD Programs* (Guide), issued by the HUD Office of the Inspector General. Those standards and the Guide require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether [the entity] complied with laws and regulations, noncompliance with which would be material to a major HUD-assisted program.

Management of [the entity] is responsible for establishing and maintaining effective internal control over financial reporting and internal control over compliance. In planning and performing our audits of the financial statements and compliance, we considered [the entity's] internal control over financial reporting and its internal control over compliance with requirements that could have a direct and material effect on a major HUD-assisted program as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements and compliance but not for the purpose of expressing an opinion on the effectiveness of [the entity's] internal control over financial reporting and internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of [the entity's] internal control over financial reporting and internal control over compliance.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct (1) misstatements of the entity's financial statements or (2) noncompliance with applicable requirements of a HUD-assisted program on a timely basis. A material weakness is a deficiency or combination of deficiencies in internal control such that

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<sup>1</sup> Note that this combined report format is illustrative of one possible presentation. Auditors may choose to issue separate reports on internal control over financial reporting and internal control over compliance.

<sup>2</sup> The reference to major HUD-assisted programs here and throughout this report is used because the auditor's opinion on compliance runs to the major programs. However, when required by the *Consolidated Audit Guide for Audits of HUD Programs*, the auditor still has the responsibility to test compliance with specific requirements applicable to nonmajor HUD-assisted program transactions and issue the related nonmajor report, "Report on Compliance with Specific Requirements Applicable to Nonmajor HUD-Assisted Programs."

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there is a reasonable possibility that (1) a material misstatement of the entity's financial statements or (2) material noncompliance with applicable requirements of a HUD-assisted program will not be prevented or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting and internal control over compliance was for the limited purpose described in the third paragraph of this report and was not designed to identify all deficiencies in internal control that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control that we consider to be material weaknesses as defined above. However, we identified certain deficiencies in internal control that we consider to be significant deficiencies. A significant deficiency is a deficiency or a combination of deficiencies in internal control that is less severe than a material weakness in internal control over financial reporting or a material weakness in internal control over compliance yet important enough to merit attention by those charged with governance. We consider the deficiencies described below to be significant deficiencies.

[Describe the significant deficiencies that were identified.]<sup>3</sup>

[The entity's] responses to the significant deficiencies identified in our audit are described above [or in the accompanying schedule of findings]. We did not audit [the entity's] responses, and, accordingly, we express no opinion on the responses.

[We noted certain matters that we reported to management of [the entity] in a separate letter, dated [date].]<sup>4</sup>

This report is intended solely for the information and use of management, [identify the body or individuals charged with governance], others within the entity, and HUD and is not intended to be and should not be used by anyone other than these specified parties.

[Signature]

[Date]

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<sup>3</sup> If the auditor includes the findings in a separate schedule versus in the body of the report, the third sentence of the previous paragraph would be replaced with language similar to the following:

However, we identified certain deficiencies in internal control that we consider to be significant deficiencies as described in the accompanying schedule of findings as items [list the reference numbers of the related findings, for example findings 1, 2, and 3].

<sup>4</sup> Certain chapters of the Guide require mention of the management letter in the independent auditor's report. Consult the Guide for further information.

## Example B-2

**Independent Auditor's Report on Internal Control  
Combined Report Applicable to Internal Control over Financial Reporting Based on an  
Audit of Financial Statements and Internal Control over Compliance for HUD-Assisted  
Programs  
Material Weaknesses and Significant Deficiencies Were Identified<sup>1 2</sup>**

[Addressee]

We have audited the financial statements of [the entity] as of and for the year ended [date], and have issued our report thereon, dated [date]. We have also audited [the entity's] compliance with requirements applicable to major<sup>3</sup> U.S. Department of Housing and Urban Development (HUD)-assisted programs for the year ended [date], and have issued our reports thereon, dated [date].

We conducted our audits in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the *Consolidated Audit Guide for Audits of HUD Programs* (Guide), issued by the HUD Office of the Inspector General. Those standards and the Guide require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether [the entity] complied with laws and regulations, noncompliance with which would be material to a major HUD-assisted program.

Management of [the entity] is responsible for establishing and maintaining effective internal control over financial reporting and internal control over compliance. In planning and performing our audits of the financial statements and compliance, we considered [the entity's] internal control over financial reporting and its internal control over compliance with requirements that could have a direct and material effect on a major HUD-assisted program as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements and on compliance but not for the purpose of expressing an opinion on the effectiveness of [the entity's] internal control over financial reporting and internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of [the entity's] internal control over financial reporting and internal control over compliance.

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<sup>1</sup> See example B for an illustration of a report in which no material weaknesses or significant deficiencies were identified by the auditor. See example B-1 for an illustration of a report in which significant deficiencies were identified but no material weaknesses were identified. Note that this example (B-2) illustrates the reporting when both material weaknesses and significant deficiencies were identified. Example B-2 would also be used by the auditor for situations in which there were material weaknesses but no significant deficiencies were identified.

<sup>2</sup> Note that this combined report format is illustrative of one possible presentation. Auditors may choose to issue separate reports on internal control over financial reporting and internal control over compliance.

<sup>3</sup> The reference to major HUD-assisted programs here and throughout this report is used because the auditor's opinion on compliance runs to the major programs. However, when required by the *Consolidated Audit Guide for Audits of HUD Programs*, the auditor still has the responsibility to test compliance with specific requirements applicable to nonmajor HUD-assisted program transactions and to issue the related nonmajor report, "Report on Compliance with Specific Requirements Applicable to Nonmajor HUD-Assisted Programs."

Our consideration of internal control over financial reporting and internal control over compliance was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be significant deficiencies or material weaknesses, and, therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as discussed below, we identified certain deficiencies in internal control that we consider to be material weaknesses and other deficiencies that we consider to be significant deficiencies.<sup>4</sup>

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct (1) misstatements of the entity's financial statements or (2) noncompliance with applicable requirements of a HUD-assisted program on a timely basis. A material weakness is a deficiency or combination of deficiencies in internal control such that there is a reasonable possibility that (1) a material misstatement of the entity's financial statements or (2) material noncompliance with applicable requirements of a HUD-assisted program will not be prevented or detected and corrected on a timely basis. We consider the following deficiencies in [the entity's] internal control to be material weaknesses:

[Describe the material weaknesses that were identified.]<sup>5</sup>

A significant deficiency is a deficiency or a combination of deficiencies in internal control that is less severe than a material weakness in internal control over financial reporting or a material weakness in internal control over compliance yet important enough to merit attention by those charged with governance. We consider the following deficiencies in [the entity's] internal control to be significant deficiencies.<sup>6</sup>

[Describe the significant deficiencies that were identified.]<sup>7</sup>

[The entity's] responses to the material weaknesses [and significant deficiencies] identified in our audit are described above *[or in the accompanying schedule of findings]*. We did not audit [the entity's] responses, and, accordingly, we express no opinion on the responses.

<sup>4</sup> If no significant deficiencies were identified, this sentence would read as follows:

However, as discussed below, we identified certain deficiencies in internal control that we consider to be material weaknesses.

<sup>5</sup> If the auditor includes the findings in a separate schedule versus in the body of the report, the last sentence of the previous paragraph would be replaced with language similar to the following:

However, we identified certain deficiencies in internal control that we consider to be material weaknesses as described in the accompanying schedule of findings as items *[list the reference numbers of the related findings, for example, findings 1, 2, and 3]*.

<sup>6</sup> If no significant deficiencies were identified, this paragraph would be deleted along with the paragraph below as there would be no significant deficiencies to identify.

<sup>7</sup> If the auditor includes the findings in a separate schedule versus in the body of the report, the last sentence of the previous paragraph would be replaced with language similar to the following:

We identified certain deficiencies in internal control that we consider to be significant deficiencies as described in the accompanying schedule of findings as items *[list the reference numbers of the related findings, for example, findings 1, 2, and 3]*.

[We noted certain matters that we reported to management of [the entity] in a separate letter, dated [date].]<sup>8</sup>

This report is intended solely for the information and use of management, *[identify the body or individuals charged with governance]*, others within the entity, and HUD and is not intended to be and should not be used by anyone other than these specified parties.

[Signature]

[Date]

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<sup>8</sup> Certain chapters of the *Consolidated Audit Guide for Audits of HUD Programs* (the "Guide") require mention of the management letter in the independent auditor's report. Consult the Guide for further information.