Reporting Confidential or Sensitive Information

5.39 If certain pertinent information is prohibited from public disclosure or is excluded from a report due to the confidential or sensitive nature of the information, auditors should disclose in the report that certain information has been omitted and the reason or other circumstances that make the omission necessary.

5.40 Certain information may be classified or may otherwise be prohibited from general disclosure by federal, state, or local laws or regulations. In such circumstances, auditors may issue a separate, classified, or limited use report containing the information and distribute the report only to persons authorized by law or regulation to receive it.

5.41 Additional circumstances associated with public safety and security concerns could also justify the exclusion of certain information from a publicly available or widely distributed report. For example, detailed information related to computer security for a particular program may be excluded from publicly available reports because of the potential damage that could be caused by the misuse of this information. In such circumstances, auditors may issue a limited use report containing such information and distribute the report only to those parties responsible for acting on the auditors' recommendations. The auditors may consult with legal counsel regarding any requirements or other circumstances that may necessitate the omission of certain information.

5.42 Considering the broad public interest in the program or activity under review assists auditors when deciding whether to exclude certain information from publicly available reports. When circumstances call for omission of certain information, auditors should evaluate whether this omission could distort the audit results or conceal improper or illegal practices.

5.43 When audit organizations are subject to public records laws, auditors should determine whether public records laws could impact the availability of classified or limited use reports and determine whether other means of communicating with management and those charged with governance would be more appropriate. For example, the auditors may communicate general information in a written report and communicate detailed information verbally. The auditors may consult with legal counsel regarding applicable public records laws.

Distributing Reports

5.44 Distribution of reports completed under GAGAS depends on the relationship of the auditors to the audited organization and the nature of the information contained in the report. If the subject of the audit involves material that is classified for security purposes or contains confidential or sensitive information, auditors may limit the report distribution. Auditors should document any limitation on report distribution. The following discussion outlines distribution for reports completed under GAGAS:

a. Audit organizations in government entities should distribute audit reports to those charged with governance, to the appropriate officials of the audited entity, and to the appropriate oversight bodies or organizations requiring or arranging for the audits. As appropriate, auditors should also distribute copies of the reports to other officials who have legal oversight authority or who may be responsible for acting on audit findings and recommendations, and to others authorized to receive such reports.

b. Internal audit organizations in government entities may follow the Institute of Internal Auditors (IIA) *International Standards for the Professional Practice of Internal Auditing.* Under GAGAS and IIA standards, the head of the internal audit organization should communicate results to the parties who can ensure that the results are given due consideration. If not otherwise mandated by statutory or regulatory requirements, prior to releasing results to parties outside the organization, the head of the internal audit organization should: (1) assess the potential risk to the organization, (2) consult with senior management and/or legal counsel as appropriate, and (3) control dissemination by indicating the intended users in the report.

c. Public accounting firms contracted to perform an audit under GAGAS should clarify report distribution responsibilities with the engaging organization. If the contracted firm is to make the distribution, it should reach agreement with the party contracting for the audit about which officials or organizations will receive the report and the steps being taken to make the report available to the public.

General, Field Work, and Reporting Standards for Attestation Engagements

Introduction

6.01 This chapter establishes standards and provides guidance for attestation engagements conducted in accordance with generally accepted government auditing standards (GAGAS). For attestation engagements, GAGAS incorporate the American Institute of Certified Public Accountants (AICPA) general standard on criteria, and the field work and reporting standards and the related Statements on Standards for Attestation Engagements (SSAE), unless specifically excluded or modified by GAGAS.[77,78] This chapter identifies the AICPA general standard on criteria[79] and the field work and reporting standards for attestation engagements and prescribes additional standards for attestation engagements performed in accordance with GAGAS.

6.02 For attestation engagements performed in accordance with GAGAS, chapters 1 through 3 and 6 apply.

AICPA General and Field Work Standards for Attestation Engagements

6.03 The AICPA general standard related to criteria is as follows:

The practitioner [auditor] must have reason to believe that the subject matter is capable of evaluation against criteria that are suitable and available to users.

6.04 The two AICPA field work standards for attestation engagements are as follows:

[77]To date, the Comptroller General has not excluded any field work standards, reporting standards, or SSAE.

[78]See AT Section 50, *SSAE Hierarchy.*

[79]GAGAS incorporate only one of the AICPA general standards for attestation engagements.

a. The practitioner [auditor] must adequately plan the work and must properly supervise any assistants.

b. The practitioner [auditor] must obtain sufficient evidence to provide a reasonable basis for the conclusion that is expressed in the report.

Additional Government Auditing Standards

6.05 GAGAS establish attestation engagement field work standards in addition to the requirements contained in the AICPA standards. Auditors should comply with these additional standards when citing GAGAS in their attestation engagement reports. The additional government auditing standards relate to

a. auditor communication during planning (see paragraphs 6.06 through 6.08);

b. previous audits and attestation engagements (see paragraph 6.09);

c. internal control (see paragraphs 6.10 through 6.12);

d. fraud, illegal acts, violations of provisions of contracts or grant agreements, or abuse that could have a material effect on the subject matter (see paragraphs 6.13 and 6.14);

e. developing elements of a finding (see paragraphs 6.15 through 6.19); and

f. documentation (see paragraphs 6.20 through 6.26).

Auditor Communication During Planning

6.06 Under AICPA standards and GAGAS, auditors should establish an understanding with the entity regarding the services to be performed for each engagement. Auditors also should obtain written acknowledgment or other evidence of the entity's responsibilities for the subject matter or the written assertion as it relates to the objectives of the engagement. GAGAS broaden the parties included in the communications during planning and contain additional items in the communications.

6.07 Under GAGAS, when planning the engagement, auditors should communicate certain information, including their understanding of the services to be performed for each engagement, in writing to entity management, those charged with governance,[80] and to the individuals contracting for or requesting the engagement. When auditors perform the engagement pursuant to a law or regulation or they conduct the work for the legislative committee that has oversight of the entity, auditors should communicate with the legislative committee. In those situations where there is not a single individual or group that both oversees the strategic direction of the entity and the fulfillment of its accountability obligations or in other situations where the identity of those charged with governance is not clearly evident, the auditors should document the process followed and conclusions reached for identifying the appropriate individuals to receive the required auditor communications. Auditors should communicate the following additional information under GAGAS:

a. the nature, timing, and extent of planned testing and reporting;

b. the level of assurance the auditor will provide; and

[80]Those charged with governance are those responsible for overseeing the strategic direction of the entity and the entity's fulfillment of its obligations related to accountability. (See appendix I, paragraph A1.05 through A1.07 for additional information.)

c. any potential restriction on the auditors' reports, in order to reduce the risk that the needs or expectations of the parties involved may be misinterpreted.

6.08 If an engagement is terminated before it is completed and a report is not issued, auditors should document the results of the work to the date of termination and why the engagement was terminated. Determining whether and how to communicate the reason for terminating the engagement to those charged with governance, appropriate officials of the entity, the entity contracting for or requesting the engagement, and other appropriate officials will depend on the facts and circumstances and, therefore, is a matter of professional judgment.

Previous Audits and Attestation Engagements

6.09 Auditors should evaluate whether the audited entity has taken appropriate corrective action to address findings and recommendations from previous engagements that could have a material effect on the subject matter. When planning the engagement, auditors should ask entity management to identify previous audits, attestation engagements, and other studies that directly relate to the subject matter of the attestation engagement being undertaken, including whether related recommendations have been implemented. Auditors should use this information in assessing risk and determining the nature, timing, and extent of current work, including determining the extent to which testing the implementation of the corrective actions is applicable to the current engagement objectives.

Internal Control

6.10 In planning examination-level attestation engagements, auditors should obtain a sufficient understanding of internal control that is material to the subject matter in order to plan the engagement and design procedures to achieve the objectives of the attestation engagement.

6.11 In planning an examination-level attestation engagement, auditors should obtain an understanding of internal control as it relates to the subject matter to which the auditors are attesting. The subject matter may be financial or nonfinancial. (See paragraph 1.23 for a discussion of possible attestation engagement subject matters.)

6.12 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, detect, or correct errors in assertions made by management on a timely basis. A deficiency in design exists when (1) a control necessary to meet the control objective is missing or (2) an existing control is not properly designed so that, even if the control operates as designed, the control objective is not met. A deficiency in operation exists when a properly designed control does not operate as designed, or when the person performing the control does not possess the necessary authority or qualifications to perform the control effectively.

Fraud, Illegal Acts, Violations of Provisions of Contracts or Grant Agreements, or Abuse That Could Have a Material Effect on the Subject Matter

6.13 The auditors' responsibility with regard to fraud,[81] illegal acts, violations of provisions of contracts or grant agreements, or abuse for attestation engagements performed in accordance with GAGAS is as follows:

a. Examination-level engagements: In planning, auditors should design the engagement to provide reasonable assurance of detecting fraud, illegal acts, or violations of provisions of contracts or grant agreements that could have a material effect on the subject matter of the attestation engagement. Thus, auditors should assess the risk and possible effects of material fraud, illegal acts, or violations of provisions of contracts or grant agreements on the subject matter of the attestation engagement. When risk factors are identified, auditors should document the risk factors identified, the auditors' response to those risk factors individually or in combination, and the auditors' conclusions.

b. Review-level and agreed-upon-procedures-level engagements: If during the course of the engagement, information comes to the auditors' attention indicating that fraud, illegal acts, or violations of provisions of contracts or grant agreements that could have a material effect on the subject matter may have occurred, auditors should perform procedures as necessary to (1) determine if fraud, illegal acts, or violations of provisions of contracts or grant agreements are likely to have occurred and, if so, (2) determine their effect on the results of the attestation engagement. Auditors are not expected to provide assurance of detecting potential fraud, illegal acts, or violations of provisions of

[81] Fraud is a type of illegal act involving the obtaining of something of value through willful misrepresentation. Although not applicable to attestation engagements, the AICPA Statements on Auditing Standards (SAS) may provide useful guidance related to fraud for auditors performing attestation engagements in accordance with GAGAS.

contracts or grant agreements for these types of engagements unless it is specified in the procedures.

c. For all levels of attestation engagements: If during the course of the engagement, auditors become aware of abuse that could be quantitatively or qualitatively material, auditors should apply procedures specifically directed to ascertain the potential effect on the subject matter or other data significant to the engagement objectives. After performing additional work, auditors may discover that the abuse represents potential fraud or illegal acts. Because the determination of abuse is subjective, auditors are not required to provide reasonable assurance of detecting abuse in attestation engagements.

6.14 Abuse involves behavior that is deficient or improper when compared with behavior that a prudent person would consider reasonable and necessary business practice given the facts and circumstances. Abuse also includes misuse of authority or position for personal financial interests or those of an immediate or close family member or business associate. Abuse does not necessarily involve fraud, violation of laws, regulations, or provisions of a contract or grant agreement.

Developing Elements of a Finding

6.15 Audit findings may involve deficiencies in internal control, fraud, illegal acts, violations of provisions of contracts or grant agreements, and abuse. The elements needed for a finding depend entirely on the engagement objectives. Thus a finding or set of findings is complete to the extent that the engagement objectives are satisfied. When auditors identify deficiencies, auditors should plan and perform procedures to develop the elements of the findings that are relevant and necessary to achieve the engagement objectives. The elements of a finding are discussed in paragraphs 6.16 through 6.19.

6.16 Criteria: The laws, regulations, contracts, grant agreements, standards, measures, expected performance, defined business practices, and benchmarks against which performance is compared or evaluated. Criteria identify the required or desired state or expectation with respect to the program or operation. Criteria provide a context for evaluating evidence and understanding the findings.

6.17 Condition: Condition is a situation that exists. The condition is determined and documented during the engagement.

6.18 Cause: The cause identifies the reason or explanation for the condition or the factor or factors responsible for the difference between the situation that exists (condition) and the required or desired state (criteria), which may also serve as a basis for recommendations for corrective actions. Common factors include poorly designed policies, procedures, or criteria; inconsistent, incomplete, or incorrect implementation; or factors beyond the control of program management. Auditors may assess whether the evidence provides a reasonable and convincing argument for why the stated cause is the key factor or factors contributing to the difference.

6.19 Effect or potential effect: The effect is a clear, logical link to establish the impact or potential impact of the difference between the situation that exists (condition) and the required or desired state (criteria). The effect or potential effect identifies the outcomes or consequences of the condition. When the engagement objectives include identifying the actual or potential consequences of a condition that varies (either positively or negatively) from the criteria identified in the engagement, "effect" is a measure of those consequences. Effect or potential effect may be used to demonstrate the need for corrective action in response to identified problems or relevant risks.

Attest Documentation

6.20 Under GAGAS, auditors must prepare attest documentation in connection with each engagement in sufficient detail to provide a clear understanding of the work performed (including the nature, timing, extent, and results of engagement procedures performed); the evidence obtained and its source; and the conclusions reached. Documentation provides the principal support for

a. the statement in the engagement report that the auditors performed the attestation engagement in accordance with GAGAS and any other standards cited and

b. the auditors' conclusion.

6.21 Auditors should prepare attest documentation in sufficient detail to enable an experienced auditor,[82] having no previous connection to the attestation engagement, to understand from the documentation the nature, timing, extent, and results of procedures performed and the evidence obtained and its source and the conclusions reached, including evidence that supports the auditors' significant judgments and conclusions. Auditors should prepare attest documentation that contains support for findings,

[82]An experienced auditor means an individual (whether internal or external to the audit organization) who possesses the competencies and skills that would have enabled him or her to perform the attestation engagement. These competencies and skills include an understanding of (1) attestation engagement processes, (2) GAGAS and applicable legal and regulatory requirements, (3) the subject matter that the auditor is engaged to report on, (4) the suitability and availability of criteria, and (5) issues related to the audited entity's environment.

conclusions, and recommendations before they issue their report.

6.22 Auditors also should document the following for attestation engagements performed under GAGAS:

a. the objectives, scope, and methodology of the attestation engagement;

b. the work performed to support significant judgments and conclusions, including descriptions of transactions and records examined;[83]

c. evidence of supervisory review, before the engagement report is issued, of the work performed that supports findings, conclusions, and recommendations contained in the engagement report; and

d. the auditors' consideration that the planned procedures be designed to achieve objectives of the attestation engagement when (1) evidence obtained is dependent on computerized information systems, (2) such evidence is material to the objective of the engagement, and (3) the auditors are not relying on the effectiveness of internal control over those computerized systems that produced the evidence. Auditors should document (1) the rationale for determining the nature, timing, and extent of planned procedures; (2) the kinds and competence of available evidence produced outside a computerized information system, or plans for direct testing of data produced from a computerized information system; and (3) the effect on the attestation engagement report if evidence to be

[83]Auditors may meet this requirement by listing file numbers, case numbers, or other means of identifying specific documents they examined. They are not required to include copies of documents they examined as part of the attest documentation, nor are they required to list detailed information from those documents.

gathered does not afford a reasonable basis for achieving the objectives of the engagement.

6.23 When auditors do not comply with applicable GAGAS requirements due to law, regulation, scope limitations, restrictions on access to records, or other issues impacting the engagement, the auditors should document the departure, the impact on the engagement and on the auditors' conclusions. This applies to departures from mandatory requirements and presumptively mandatory requirements where alternative procedures performed in the circumstances were not sufficient to achieve the objectives of the standard. (See paragraphs 1.12 and 1.13.)

6.24 Audit organizations should establish policies and procedures for the safe custody and retention of documentation for a time sufficient to satisfy legal, regulatory, and administrative requirements for records retention. Whether engagement documentation is in paper, electronic, or other media, the integrity, accessibility, and retrievability of the underlying information could be compromised if the documentation is altered, added to, or deleted without the auditors' knowledge, or if the documentation is lost or damaged. For attest documentation that is retained electronically, the audit organization should establish information systems controls concerning accessing and updating the attest documentation.

6.25 Underlying GAGAS engagements is the premise that audit organizations in federal, state, and local governments and public accounting firms engaged to perform an engagement in accordance with GAGAS cooperate in performing attestation engagements of programs of common interest so that auditors may use others' work and avoid duplication of efforts. Subject to applicable laws and regulations, auditors should make appropriate individuals, as well as attest documentation, available upon request and in a timely manner to other auditors or reviewers to satisfy these objectives. The use of auditors' work by other auditors may be facilitated by contractual arrangements for GAGAS engagements that provide for full and timely access to appropriate individuals, as well as attest documentation.

6.26 Audit organizations should develop policies to deal with requests by outside parties to obtain access to attest documentation, especially when an outside party attempts to obtain information indirectly through the auditor rather than directly from the entity. In developing such policies, audit organizations should determine what laws and regulations apply, if any.

Additional Considerations for GAGAS Attestation Engagements

6.27 Due to the engagement objectives and public accountability of GAGAS engagements, there may be additional considerations for attestation engagements completed in accordance with GAGAS. These considerations relate to

a. materiality in GAGAS attestation engagements (see paragraph 6.28) and

b. ongoing investigations or legal proceedings (see paragraph 6.29).

Materiality in GAGAS Attestation Engagements

6.28 The concept of materiality recognizes that some matters, either individually or in the aggregate, are important for fair presentation of a subject matter or an assertion about a subject matter, while other matters are not important. In performing the engagement, matters that, either individually or in the aggregate, could be material to the subject matter are a primary consideration. In engagements performed in accordance with GAGAS, auditors may find it appropriate to use lower materiality levels as compared with the materiality levels used in non-GAGAS engagements because of the public accountability of government entities and entities receiving government funding, various legal and regulatory requirements, and the visibility and sensitivity of government programs.

Ongoing Investigations or Legal Proceedings

6.29 Avoiding interference with investigations or legal proceedings is important in pursuing indications of fraud, illegal acts, violations of provisions of contracts or grant agreements, or abuse. Laws, regulations, or policies might require auditors to report indications of certain types of fraud, illegal acts, violations of provisions of contracts or grant agreements, or abuse to law enforcement or investigatory authorities before performing additional procedures. When investigations or legal proceedings are initiated or in process, auditors should evaluate the impact on the current engagement. In some cases, it may be appropriate for the auditors to work with investigators and/or legal authorities, or withdraw from or defer further work on the engagement or a portion of the engagement to avoid interfering with an investigation.

AICPA Reporting Standards for Attestation Engagements

6.30 The four AICPA reporting standards that apply to all levels of attestation engagements are as follows:[84]

a. The practitioner [auditor] must identify the subject matter or the assertion being reported on and state the character of the engagement in the report.

b. The practitioner [auditor] must state the practitioner's [auditor's] conclusion about the subject matter or the

[84]Under AT Section 50, *SSAE Hierarchy*, the reporting standards apply when the practitioner issues a report. The reporting standards do not apply when the practitioner declines to issue a report as a result of the engagement.

assertion in relation to the criteria against which the subject matter was evaluated in the report.

c. The practitioner [auditor] must state all of the practitioner's [auditor's] significant reservations about the engagement, the subject matter, and, if applicable, the assertion related thereto in the report.

d. The practitioner [auditor] must state in the report that the report is intended for use by specified parties under the following circumstances:

(1) When the criteria used to evaluate the subject matter are determined by the practitioner [auditor] to be appropriate only for a limited number of parties who either participated in their establishment or can be presumed to have an adequate understanding of the criteria.

(2) When the criteria used to evaluate the subject matter are available only to specified parties.

(3) When reporting on subject matter and a written assertion has not been provided by the responsible party.

(4) When the report is on an attest engagement to apply agreed-upon procedures to the subject matter.

Additional Government Auditing Standards

6.31 GAGAS establish reporting standards for attestation engagements in addition to the requirements contained in the AICPA standards. Auditors should comply with these additional standards when citing GAGAS in their attestation engagement reports. The additional government auditing standards relate to

a. reporting auditors' compliance with GAGAS (see paragraph 6.32);

b. reporting deficiencies in internal control, fraud, illegal acts, violations of provisions of contracts or grant agreements, and abuse (see paragraphs 6.33 through 6.43);

c. reporting views of responsible officials (see paragraphs 6.44 through 6.50);

d. reporting confidential or sensitive information (see paragraphs 6.51 through 6.55); and

e. distributing reports (see paragraph 6.56).

Reporting Auditors' Compliance with GAGAS

6.32 When auditors comply with all applicable GAGAS requirements, they should include a statement in the attestation report that they performed the engagement in accordance with GAGAS. (See paragraphs 1.12 and 1.13 for additional requirements on citing compliance with GAGAS.) GAGAS do not prohibit auditors from issuing a separate report conforming only to the requirements of other standards.

Reporting Deficiencies in Internal Control, Fraud, Illegal Acts, Violations of Provisions of Contracts or Grant Agreements, and Abuse

6.33 For attestation engagements, auditors should report, as applicable to the objectives of the engagement, and based upon the work performed, (1) significant deficiencies in internal control, identifying those considered to be material weaknesses; (2) all instances of fraud and illegal acts unless inconsequential; and (3) violations of provisions of contracts or grant agreements and abuse that could have a material effect on the subject matter of the engagement.

Deficiencies in Internal Control

6.34 For all attestation engagements, auditors should report the following deficiencies in internal control:

a. Significant deficiency: a deficiency in internal control, or combination of deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report data reliably in accordance with the applicable criteria or framework such that there is more than a remote[85] likelihood that a misstatement of the subject matter that is more than inconsequential[86] will not be prevented or detected.

b. Material weakness: a significant deficiency or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the subject matter will not be prevented or detected.

6.35 Determining whether and how to communicate to entity officials internal control deficiencies that have an inconsequential effect on the subject matter is a matter of professional judgment. Auditors should document such communications.

Fraud, Illegal Acts, Violations of Provisions of Contracts or Grant Agreements, and Abuse

6.36 Under GAGAS, when auditors conclude, based on sufficient, appropriate evidence, that any of the following either has occurred or is likely to have occurred, they should include in their report the relevant information about

[85]The term "more than remote" used in the definitions for significant deficiency and material weakness means "at least reasonably possible." The following definitions apply: (1) Remote—The chance of the future events occurring is slight. (2) Reasonably possible—The chance of the future events or their occurrence is more than remote but less than likely. (3) Probable—The future events are likely to occur.

[86]"More than inconsequential" indicates an amount that is less than material, yet has significance. A misstatement is "inconsequential" if a reasonable person would conclude that the misstatement, either individually or when aggregated with other misstatements, would clearly be immaterial to the subject matter. If a reasonable person would not reach such a conclusion, that misstatement is "more than inconsequential."

a. fraud and illegal acts[37] that have an effect on the subject matter that is more than inconsequential,

b. violations of provisions of contracts or grant agreements that have a material effect on the subject matter, and

c. abuse that is material to the subject matter, either quantitatively or qualitatively. (See paragraphs 6.13 and 6.14 for a discussion of abuse.)

6.37 When auditors detect violations of provisions of contracts or grant agreements or abuse that have an effect on the subject matter that is less than material but more than inconsequential, they should communicate those findings in writing to entity officials. Determining whether and how to communicate to entity officials fraud, illegal acts, violations of provisions of contracts or grant agreements, or abuse that is inconsequential is a matter of professional judgment. Auditors should document such communications.

6.38 When fraud, illegal acts, violations of provisions of contracts or grant agreements, or abuse either have occurred or are likely to have occurred, auditors may consult with authorities or legal counsel about whether publicly reporting such information would compromise investigative or legal proceedings. Auditors may limit their public reporting to matters that would not compromise those proceedings and, for example, report only on information that is already a part of the public record.

[37]Whether a particular act is, in fact, illegal may have to await final determination by a court of law or other adjudicative body. Disclosing matters that have led auditors to conclude that an illegal act is likely to have occurred is not a final determination of illegality.

Reporting Findings Directly to Parties Outside the Entity

6.39 Auditors should report known or likely fraud, illegal acts, violations of provisions of contracts or grant agreements, or abuse directly to parties outside the audited entity in the following two circumstances.[88]

a. When entity management fails to satisfy legal or regulatory requirements to report such information to external parties specified in law or regulation, auditors should first communicate the failure to report such information to those charged with governance. If the audited entity still does not report this information to the specified external parties as soon as practicable after the auditors' communication with those charged with governance, then the auditors should report the information directly to the specified external parties.

b. When entity management fails to take timely and appropriate steps to respond to known or likely fraud, illegal acts, violations of provisions of contracts or grant agreements, or abuse that (1) is likely to have a material effect on the subject matter and (2) involves funding received directly or indirectly from a government agency, auditors should first report management's failure to take timely and appropriate steps to those charged with governance. If the audited entity still does not take timely and appropriate steps as soon as practicable after the auditors' communication with those charged with governance, then the auditors should report the entity's failure to take timely and appropriate steps directly to the funding agency.

6.40 The reporting in paragraph 6.39 is in addition to any legal requirements to report such information directly to parties outside the entity. Auditors should

[88]Internal audit organizations do not have a duty to report outside the entity unless required by law, rule, regulation, or policy. (See paragraph 6.56b for reporting standards for internal audit organizations when reporting externally.)

comply with these requirements even if they have resigned or been dismissed from the engagement prior to its completion.

6.41 Auditors should obtain sufficient, appropriate evidence, such as confirmation from outside parties, to corroborate assertions by entity management that it has reported such findings in accordance with laws, regulations, and funding agreements. When auditors are unable to do so, they should report such information directly as discussed in paragraph 6.39.

Presenting Findings in the Auditors' Report

6.42 In presenting findings such as deficiencies in internal control, fraud, illegal acts, violations of provisions of contracts or grant agreements, and abuse, auditors should develop the elements of the findings to the extent necessary to achieve the engagement objectives. Clearly developed findings, as discussed in paragraphs 6.15 through 6.19, assist management or oversight officials in understanding the need for taking corrective action. If auditors are able to sufficiently develop the elements of a finding, they may provide recommendations for corrective action.

6.43 Auditors should place their findings in perspective by describing the nature and extent of the issues being reported and the extent of the work performed that resulted in the finding. To give the reader a basis for judging the prevalence and consequences of these findings, auditors should, as applicable, relate the instances identified to the population or the number of cases examined and quantify the results in terms of dollar value or other measures, as appropriate. If the results cannot be projected, auditors should limit their conclusions appropriately.

Reporting Views of Responsible Officials

6.44 If the attestation engagement report discloses deficiencies in internal control, fraud, illegal acts, violations of provisions of contracts or grant agreements, or abuse, auditors should obtain and report the views of responsible officials concerning the findings, conclusions, and recommendations, as well as planned corrective actions.

6.45 Providing a draft report with findings for review and comment by responsible officials of the audited entity and others helps the auditors develop a report that is fair, complete, and objective. Including the views of responsible officials results in a report that presents not only the auditors' findings, conclusions, and recommendations, but also the perspectives of the responsible officials of the audited entity and the corrective actions they plan to take. Obtaining the comments in writing is preferred, but oral comments are acceptable.

6.46 When auditors receive written comments from the responsible officials, they should include in their report a copy of the officials' written comments, or a summary of the comments received. When the responsible officials provide oral comments only, auditors should prepare a summary of the oral comments and provide a copy of the summary to the responsible officials to verify that the comments are accurately stated.

6.47 Auditors should also include in the report an evaluation of the comments, as appropriate. In cases in which the audited entity provides technical comments in addition to its written or oral comments on the report, auditors may disclose in the report that such comments were received.

6.48 Obtaining oral comments may be appropriate when, for example, there is a reporting date critical to meeting a user's needs; auditors have worked closely with the responsible officials throughout the conduct of the work and the parties are familiar with the findings and issues addressed in the draft report; or the auditors do not expect major disagreements with the findings, conclusions, and recommendations in the draft report, or major controversies with regard to the issues discussed in the draft report.

6.49 When the entity's comments are inconsistent or in conflict with the findings, conclusions, or recommendations in the draft report, or when planned corrective actions do not adequately address the auditors' recommendations, the auditors should evaluate the validity of the audited entity's comments. If the auditors disagree with the comments, they should explain in the report their reasons for disagreement. Conversely, the auditors should modify their report as necessary if they find the comments valid and supported with sufficient, appropriate evidence.

6.50 If the entity refuses to provide comments or is unable to provide comments within a reasonable period of time, the auditors may issue the report without receiving comments from the entity. In such cases, the auditors should indicate in the report that the audited entity did not provide comments.

Reporting Confidential or Sensitive Information

6.51 If certain pertinent information is prohibited from public disclosure or is excluded from a report due to the confidential or sensitive nature of the information, auditors should disclose in the report that certain information has been omitted and the reason or other circumstances that make the omission necessary.

6.52 Certain information may be classified or may be otherwise prohibited from general disclosure by federal, state, or local laws or regulations. In such circumstances, auditors may issue a separate classified or limited use report containing such information and distribute the report only to persons authorized by law or regulation to receive it.

6.53 Additional circumstances associated with public safety and security concerns could also justify the exclusion of certain information from a publicly available or widely distributed report. For example, detailed information related to computer security for a particular program may be excluded from publicly available reports because of the potential damage that could be caused by the misuse of this information. In such circumstances, auditors may issue a limited use report containing such information and distribute the report only to those parties responsible for acting on the auditors' recommendations. The auditors may consult with legal counsel regarding any requirements or other circumstances that may necessitate the omission of certain information.

6.54 Considering the broad public interest in the program or activity under review assists auditors when deciding whether to exclude certain information from publicly available reports. When circumstances call for omission of certain information, auditors should evaluate whether this omission could distort the engagement results or conceal improper or illegal practices.

6.55 When audit organizations are subject to public records laws, auditors should determine whether public records laws could impact the availability of classified or limited use reports and determine whether other means of communicating with management and those charged with governance would be more appropriate. For example, the auditors may communicate general information in a written report and communicate detailed information verbally. The auditor may consult with legal counsel regarding applicable public records laws.

Distributing Reports

6.56 Distribution of reports completed under GAGAS depends on the relationship of the auditors to the entity and the nature of the information contained in the report. If the subject matter or the assertion involves material that is classified for security purposes or contains confidential or sensitive information, auditors may limit the report distribution. Auditors should document any limitation on report distribution. The following discussion outlines distribution for reports completed under GAGAS:

a. Audit organizations in government entities should distribute reports to those charged with governance, to the appropriate entity officials, and to the appropriate oversight bodies or organizations requiring or arranging for the engagements. As appropriate, auditors should also distribute copies of the reports to other officials who have legal oversight authority or who may be responsible for acting on engagement findings and recommendations, and to others authorized to receive such reports.

b. Internal audit organizations in government entities may follow the Institute of Internal Auditors (IIA) *International Standards for the Professional Practice of Internal Auditing.* Under GAGAS and IIA standards, the head of the internal audit organization should communicate results to the parties who can ensure that the results are given due consideration. If not otherwise mandated by statutory or regulatory requirements, prior to releasing results to parties outside the organization, the head of the internal audit organization should: (1) assess the potential risk to the organization, (2) consult with senior management and/or legal counsel as appropriate, and (3) control dissemination by indicating the intended users in the report.

c. Public accounting firms contracted to perform an engagement under GAGAS should clarify report distribution responsibilities with the engaging organization. If the contracting firm is to make the distribution, it should reach agreement with the party contracting for the engagement about which officials or organizations will receive the report and the steps being taken to make the report available to the public.

Field Work Standards for Performance Audits

Introduction

7.01 This chapter establishes field work standards and provides guidance for performance audits conducted in accordance with generally accepted government auditing standards (GAGAS). The field work standards for performance audits relate to planning the audit; supervising staff; obtaining sufficient, appropriate evidence; and preparing audit documentation. The concepts of reasonable assurance, significance, and audit risk form a framework for applying these standards and are included throughout the discussion of performance audits.

7.02 For performance audits performed in accordance with GAGAS, chapters 1 through 3 and 7 and 8 apply.

Reasonable Assurance

7.03 Performance audits that comply with GAGAS provide reasonable assurance that evidence is sufficient and appropriate to support the auditors' findings and conclusions. Thus, the sufficiency and appropriateness of evidence needed and tests of evidence will vary based on the audit objectives, findings, and conclusions. Objectives for performance audits range from narrow to broad and involve varying types and quality of evidence. In some engagements, sufficient, appropriate evidence is available, but in others, information may have limitations. Professional judgment assists auditors in determining the audit scope and methodology needed to address the audit objectives, while providing the appropriate level of assurance that the obtained evidence is sufficient and appropriate to address the audit objectives. (See paragraphs 7.55 through 7.71 for a discussion about assessing the sufficiency and appropriateness of evidence.)

Significance in a Performance Audit

7.04 The concept of significance[89] assists auditors throughout a performance audit, including when deciding the type and extent of audit work to perform, when evaluating results of audit work, and when developing the report and related findings and conclusions. Significance is defined as the relative importance of a matter within the context in which it is being considered, including quantitative and qualitative factors. Such factors include the magnitude of the matter in relation to the subject matter of the audit, the nature and effect of the matter, the relevance of the matter, the needs and interests of an objective third party with knowledge of the relevant information, and the impact of the matter to the audited program or activity. Professional judgment assists auditors when evaluating the significance of matters within the context of the audit objectives.

Audit Risk

7.05 Audit risk is the possibility that the auditors' findings, conclusions, recommendations, or assurance may be improper or incomplete, as a result of factors such as evidence that is not sufficient and/or appropriate, an inadequate audit process, or intentional omissions or misleading information due to misrepresentation or fraud. The assessment of audit risk involves both qualitative and quantitative considerations. Factors such as the time frames, complexity, or sensitivity of the work; size of the program in terms of dollar amounts and number of citizens served; adequacy of the audited entity's systems and processes to detect inconsistencies, significant errors, or fraud; and auditors' access to records, also impact audit risk. Audit risk includes the risk that

[89] In the performance audit standards, the term "significant" is comparable to the term "material" as used in the context of financial statement audits.

auditors will not detect a mistake, inconsistency, significant error, or fraud in the evidence supporting the audit. Audit risk can be reduced by taking actions such as increasing the scope of work; adding experts, additional reviewers, and other resources to the audit team; changing the methodology to obtain additional evidence, higher quality evidence, or alternative forms of corroborating evidence; or aligning the findings and conclusions to reflect the evidence obtained.

Planning

7.06 Auditors must adequately plan and document the planning of the work necessary to address the audit objectives.

7.07 Auditors must plan the audit to reduce audit risk to an appropriate level for the auditors to provide reasonable assurance that the evidence is sufficient and appropriate to support the auditors' findings and conclusions. This determination is a matter of professional judgment. In planning the audit, auditors should assess significance and audit risk and apply these assessments in defining the audit objectives and the scope and methodology to address those objectives.[90] Planning is a continuous process throughout the audit. Therefore, auditors may need to adjust the audit objectives, scope, and methodology as work is being completed.

7.08 The objectives are what the audit is intended to accomplish. They identify the audit subject matter and performance aspects to be included, and may also include the potential findings and reporting elements that the auditors expect to develop. Audit objectives can

[90] In situations where the audit objectives are established by statute or legislative oversight, auditors may not have latitude to define the audit objectives or scope.

be thought of as questions about the program[91] that the auditors seek to answer based on evidence obtained and assessed against criteria.

7.09 Scope is the boundary of the audit and is directly tied to the audit objectives. The scope defines the subject matter that the auditors will assess and report on, such as a particular program or aspect of a program, the necessary documents or records, the period of time reviewed, and the locations that will be included.

7.10 The methodology describes the nature and extent of audit procedures for gathering and analyzing evidence to address the audit objectives. Audit procedures are the specific steps and tests auditors will carry out to address the audit objectives. Auditors should design the methodology to obtain sufficient, appropriate evidence to address the audit objectives, reduce audit risk to an acceptable level, and provide reasonable assurance that the evidence is sufficient and appropriate to support the auditors' findings and conclusions. Methodology includes both the nature and extent of audit procedures used to address the audit objectives.

7.11 Auditors should assess audit risk and significance within the context of the audit objectives by gaining an understanding of the following:

a. the nature and profile of the programs and the needs of potential users of the audit report (see paragraphs 7.13 through 7.15);

[91]The term "program" is used in this document to include government entities, organizations, programs, activities, and functions.

b. internal control as it relates to the specific objectives and scope of the audit (see paragraphs 7.16 through 7.22);

c. information systems controls for purposes of assessing audit risk and planning the audit within the context of the audit objectives (see paragraphs 7.23 through 7.27);

d. legal and regulatory requirements, contract provisions or grant agreements, potential fraud, or abuse that are significant within the context of the audit objectives (see paragraphs 7.28 through 7.35); and

e. the results of previous audits and attestation engagements that directly relate to the current audit objectives (see paragraph 7.36).

7.12 During planning, auditors also should

a. identify the potential criteria needed to evaluate matters subject to audit (see paragraphs 7.37 and 7.38);

b. identify sources of audit evidence and determine the amount and type of evidence needed given audit risk and significance (see paragraphs 7.39 and 7.40);

c. evaluate whether to use the work of other auditors and experts to address some of the audit objectives (see paragraphs 7.41 through 7.43);

d. assign sufficient staff and specialists with adequate collective professional competence and identify other resources needed to perform the audit (see paragraphs 7.44 and 7.45);

e. communicate about planning and performance of the audit to management officials, those charged with governance, and others as applicable (see paragraphs 7.46 through 7.49); and

f. prepare a written audit plan (see paragraphs 7.50 and 7.51).

Nature and Profile of the Program and User Needs

7.13 Auditors should obtain an understanding of the nature of the program or program component under audit and the potential use that will be made of the audit results or report as they plan a performance audit. The nature and profile of a program include

a. visibility, sensitivity, and relevant risks associated with the program under audit;

b. age of the program or changes in its conditions;

c. the size of the program in terms of total dollars, number of citizens affected, or other measures;

d. level and extent of review or other forms of independent oversight;

e. program's strategic plan and objectives; and

f. external factors or conditions that could directly affect the program.

7.14 One group of users of the auditors' report is government officials who may have authorized or requested the audit. Other important users of the auditors' report are the entity being audited, those responsible for acting on the auditors' recommendations, oversight organizations, and legislative bodies. Other potential users of the auditors' report include government legislators or officials (other than those who may have authorized or requested the audit), the media, interest groups, and individual citizens. In addition to an interest in the program, potential users may have an ability to influence the conduct of the program. An awareness of these potential users' interests and influence can help auditors judge whether possible findings could be significant to relevant users.

7.15 Obtaining an understanding of the program under audit helps auditors to assess the relevant risks associated with the program and the impact on the audit objectives, scope, and methodology. The auditors' understanding may come from knowledge they already have about the program or knowledge they gain from inquiries and observations they make in planning the audit. The extent and breadth of those inquiries and observations will vary among audits based on the audit objectives, as will the need to understand individual aspects of the program, such as the following.

a. Laws, regulations, and provisions of contracts or grant agreements: Government programs are usually created by law and are subject to specific laws and regulations. Laws and regulations usually set forth what is to be done, who is to do it, the purpose to be achieved, the population to be served, and related funding guidelines or restrictions. Government programs may also be subject to provisions of contracts and grant agreements. Thus, understanding the laws and legislative history establishing a program and the provisions of any contracts or grant agreements can be essential to understanding the program itself. Obtaining that understanding is also a necessary step in identifying the provisions of laws, regulations, contracts, or grant agreements that are significant within the context of the audit objectives.

b. Purpose and goals: Purpose is the result or effect that is intended or desired from a program's operation. Legislatures usually establish the program's purpose when they provide authority for the program. Entity officials may provide more detailed information on the program's purpose to supplement the authorizing legislation. Entity officials are sometimes asked to set goals for program performance and operations, including both output and outcome goals. Auditors may use the stated program purpose and goals as criteria for assessing program performance or may develop additional criteria to use when assessing performance.

c. Internal control: Internal control, sometimes referred to as management control, in the broadest sense includes the plan, policies, methods, and procedures adopted by management to meet its missions, goals, and objectives. Internal control includes the processes for planning, organizing, directing, and controlling program operations. It includes the systems for measuring, reporting, and monitoring program performance. Internal control serves as a defense in safeguarding assets and in preventing and detecting errors; fraud; violations of laws, regulations, and provisions of contracts and grant agreements; or abuse. Paragraphs 7.16 through 7.22 contain guidance pertaining to internal control.

d. Efforts: Efforts are the amount of resources (in terms of money, material, personnel, etc.) that are put into a program. These resources may come from within or outside the entity operating the program. Measures of efforts can have a number of dimensions, such as cost, timing, and quality. Examples of measures of efforts are dollars spent, employee-hours expended, and square feet of building space.

e. Program operations: Program operations are the strategies, processes, and activities management uses to convert efforts into outputs. Program operations may be subject to internal control.

f. Outputs: Outputs represent the quantity of goods or services produced by a program. For example, an output measure for a job training program could be the number of persons completing training, and an output measure for an aviation safety inspection program could be the number of safety inspections completed.

g. Outcomes: Outcomes are accomplishments or results of a program. For example, an outcome measure for a job training program could be the percentage of trained persons obtaining a job and still in the work place after a specified period of time. An example of an outcome measure for an aviation safety inspection program could be the percentage reduction in safety problems found in subsequent inspections or the percentage of problems deemed corrected in follow-up inspections. Such outcome measures show the progress made in achieving the stated program purpose of helping unemployable citizens obtain and retain jobs, and improving the safety of aviation operations. Outcomes may be influenced by cultural, economic, physical, or technological factors outside the program. Auditors may use approaches drawn from other disciplines, such as program evaluation, to isolate the effects of the program from these other influences. Outcomes also include unexpected and/or unintentional effects of a program, both positive and negative.

Internal Control

7.16 Auditors should obtain an understanding of internal control[92] that is significant within the context of the audit objectives. For internal control that is significant within the context of the audit objectives, auditors should assess whether internal control has been properly designed and implemented. For those internal controls that are deemed significant within the context of the audit objectives, auditors should plan to obtain sufficient, appropriate evidence to support their assessment about the effectiveness of those controls. Information systems controls are often an integral part of an entity's internal control. Thus, when obtaining an understanding of internal control significant to the audit objectives, auditors should also determine whether it is necessary to evaluate information systems controls. (See paragraphs 7.23 through 7.27 for additional discussion on evaluating the effectiveness of information systems controls.)

7.17 Auditors may modify the nature, timing, or extent of the audit procedures based on the auditors' assessment of internal control and the results of internal

[92]Refer to the internal control guidance contained in *Internal Control--Integrated Framework*, published by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). As discussed in the COSO framework, internal control consists of five interrelated components, which are (1) control environment, (2) risk assessment, (3) control activities, (4) information and communication, and (5) monitoring. The objectives of internal control relate to (1) financial reporting, (2) operations, and (3) compliance. Safeguarding of assets is a subset of these objectives. In that respect, management designs internal control to provide reasonable assurance that unauthorized acquisition, use, or disposition of assets will be prevented or timely detected and corrected. In addition to the COSO document, the publication, *Standards for Internal Control in the Federal Government*, GAO/AIMD-00-21.3.1 (Washington, D.C.: November 1999), which incorporates the relevant guidance developed by COSO, provides definitions and fundamental concepts pertaining to internal control at the federal level and may be useful to other auditors at any level of government. The related *Internal Control Management and Evaluation Tool*, GAO-01-1008G (Washington, D.C.: August 2001), based on the federal internal control standards, provides a systematic, organized, and structured approach to assessing the internal control structure.

control testing. For example, poorly controlled aspects of a program have a higher risk of failure, so auditors may choose to focus their efforts in these areas. Conversely, effective controls at the audited entity may enable the auditors to limit the extent and type of audit testing needed.

7.18 Auditors may obtain an understanding of internal control through inquiries, observations, inspection of documents and records, review of other auditors' reports, or direct tests. The procedures auditors perform to obtain an understanding of internal control may vary among audits based on audit objectives and audit risk. The extent of these procedures will vary based on the audit objectives, known or potential internal control risks or problems, and the auditors' knowledge about internal control gained in prior audits.

7.19 The following discussion of the principal types of internal control objectives is intended to help auditors better understand internal controls and determine whether or to what extent they are significant to the audit objectives.

a. Effectiveness and efficiency of program operations: Controls over program operations include policies and procedures that the audited entity has implemented to provide reasonable assurance that a program meets its objectives, while considering cost-effectiveness and efficiency. Understanding these controls can help auditors understand the program operations that convert inputs and efforts to outputs and outcomes.

b. Relevance and reliability of information: Controls over the relevance and reliability of information include policies, procedures, and practices that officials of the audited entity have implemented to provide themselves reasonable assurance that operational and financial information they use for decision making and reporting externally is relevant and reliable and fairly disclosed in reports. Understanding these controls can help auditors (1) assess the risk that the information gathered by the entity may not be relevant or reliable and (2) design appropriate tests of the information considering the audit objectives.

c. Compliance with applicable laws and regulations and provisions of contracts or grant agreements: Controls over compliance include policies and procedures that the audited entity has implemented to provide reasonable assurance that program implementation is in accordance with laws, regulations, and provisions of contracts or grant agreements. Understanding the relevant controls concerning compliance with those laws and regulations and provisions of contracts or grant agreements that the auditors have determined are significant within the context of the audit objectives can help them assess the risk of illegal acts, violations of provisions of contracts or grant agreements, or abuse.

7.20 A subset of these categories of internal control objectives is the safeguarding of assets and resources. Controls over the safeguarding of assets and resources include policies and procedures that the audited entity has implemented to reasonably prevent or promptly detect unauthorized acquisition, use, or disposition of assets and resources.

7.21 In performance audits, 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, detect, or correct (1) impairments of effectiveness or efficiency of operations, (2) misstatements in financial or performance information, or (3) violations of laws and regulations, on a timely basis. A deficiency in design exists when (a) a control necessary to meet the control objective is missing or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective is not met. A deficiency in operation exists when a properly designed control does not operate as designed, or when the person performing the control does not possess the necessary authority or qualifications to perform the control effectively.

7.22 Internal auditing[93] is an important part of overall governance, accountability, and internal control. A key role of many internal audit organizations is to provide assurance that internal controls are in place to adequately mitigate risks and achieve program goals and objectives. When an assessment of internal control is needed, the auditor may use the work of the internal auditors in assessing whether internal controls are effectively designed and operating effectively, and to prevent duplication of effort. (See paragraphs 7.41 through 7.43 for standards and guidance for using the work of other auditors.)

Information Systems Controls

7.23 Understanding information systems controls is important when information systems are used extensively throughout the program under audit and the fundamental business processes related to the audit objectives rely on information systems. Information systems controls consist of those internal controls that are dependent on information systems processing and include general controls and application controls. Information systems general controls are the policies and procedures that apply to all or a large segment of an entity's information systems. General controls help

[93]Many government entities identify these internal auditing activities by other names, such as inspection, appraisal, investigation, organization and methods, or management analysis. These activities assist management by reviewing selected functions.

ensure the proper operation of information systems by creating the environment for proper operation of application controls. General controls include security management, logical and physical access, configuration management, segregation of duties, and contingency planning. Application controls, sometimes referred to as business process controls, are those controls that are incorporated directly into computer applications to help ensure the validity, completeness, accuracy, and confidentiality of transactions and data during application processing. Application controls include controls over input, processing, output, master data, application interfaces, and data management system interfaces.

7.24 An organization's use of information systems controls may be extensive; however, auditors are primarily interested in those information systems controls that are significant to the audit objectives. Information systems controls are significant to the audit objectives if auditors determine that it is necessary to evaluate the effectiveness of information systems controls in order to obtain sufficient, appropriate evidence. When information systems controls are determined to be significant to the audit objectives, auditors should then evaluate the design and operating effectiveness of such controls. This evaluation would include other information systems controls that impact the effectiveness of the significant controls or the reliability of information used in performing the significant controls. Auditors should obtain a sufficient understanding of information systems controls necessary to assess audit risk and plan the audit within the context of the audit objectives.[94]

[94]Refer to additional criteria and guidance in *Federal Information Controls Audit Manual* (FISCAM), GAO/AIMD-12.19.6 (Washington, D.C.: January 1999) and *IS Standards, Guidelines and Procedures for Auditing and Control Professionals*, published by the Information Systems Audit and Control Association (ISACA).

7.25 Audit procedures to evaluate the effectiveness of significant information systems controls include (1) gaining an understanding of the system as it relates to the information and (2) identifying and evaluating the general controls and application controls that are critical to providing assurance over the reliability of the information required for the audit.

7.26 The evaluation of information systems controls may be done in conjunction with the auditors' consideration of internal control within the context of the audit objectives (see paragraphs 7.16 through 7.22), or as a separate audit objective or audit procedure, depending on the objectives of the audit. Depending on the significance of information systems controls to the audit objectives, the extent of audit procedures to obtain such an understanding may be limited or extensive. In addition, the nature and extent of audit risk related to information systems controls are affected by the nature of the hardware and software used, the configuration of the entity's systems and networks, and the entity's information systems strategy.

7.27 Auditors should determine which audit procedures related to information systems controls are needed to obtain sufficient, appropriate evidence to support the audit findings and conclusions. The following factors may assist auditors in making this determination:

a. The extent to which internal controls that are significant to the audit depend on the reliability of information processed or generated by information systems.

b. The availability of evidence outside the information system to support the findings and conclusions: It may not be possible for auditors to obtain sufficient, appropriate evidence without evaluating the effectiveness of relevant information systems controls.

For example, if information supporting the findings and conclusions is generated by information systems or its reliability is dependent on information systems controls, there may not be sufficient supporting or corroborating information or documentary evidence that is available other than that produced by the information systems.

c. The relationship of information systems controls to data reliability: To obtain evidence about the reliability of computer-generated information, auditors may decide to evaluate the effectiveness of information systems controls as part of obtaining evidence about the reliability of the data. If the auditor concludes that information systems controls are effective, the auditor may reduce the extent of direct testing of data.

d. Evaluating the effectiveness of information systems controls as an audit objective: When evaluating the effectiveness of information systems controls is directly a part of an audit objective, auditors should test information systems controls necessary to address the audit objectives. For example, the audit may involve the effectiveness of information systems controls related to certain systems, facilities, or organizations.

Legal and Regulatory Requirements, Provisions of Contracts or Grant Agreements, Fraud, or Abuse

Legal and Regulatory Requirements, Contracts, and Grants

7.28 Auditors should determine which laws, regulations, and provisions of contracts or grant agreements are significant within the context of the audit objectives and assess the risk that violations of those laws, regulations, and provisions of contracts or grant agreements could occur. Based on that risk assessment, the auditors should design and perform procedures to provide reasonable assurance of detecting instances of violations of legal and regulatory requirements or violations of provisions of contracts or grant agreements that are significant within the context of the audit objectives.

7.29 The auditors' assessment of audit risk may be affected by such factors as the complexity or newness of the laws, regulations, and provisions of contracts or grant agreements. The auditors' assessment of audit risk also may be affected by whether the entity has controls that are effective in preventing or detecting violations of laws, regulations, and provisions of contracts or grant agreements. If auditors obtain sufficient, appropriate evidence of the effectiveness of these controls, they can reduce the extent of their tests of compliance.

Fraud

7.30 In planning the audit, auditors should assess risks of fraud[95] occurring that is significant within the context of the audit objectives. Audit team members should discuss among the team fraud risks, including factors such as individuals' incentives or pressures to commit fraud, the opportunity for fraud to occur, and rationalizations or attitudes that could allow individuals to commit fraud. Auditors should gather and assess information to identify risks of fraud that are significant within the scope of the audit objectives or that could affect the findings and conclusions. For example, auditors may obtain information through discussion with officials of the audited entity or through other means to determine the susceptibility of the program to fraud, the status of internal controls the entity has

[95]Fraud is a type of illegal act involving the obtaining of something of value through willful misrepresentation. Whether an act is, in fact, fraud is a determination to be made through the judicial or other adjudicative system and is beyond auditors' professional responsibility.

established to detect and prevent fraud, or the risk that officials of the audited entity could override internal control. An attitude of professional skepticism in assessing these risks assists auditors in assessing which factors or risks could significantly affect the audit objectives.

7.31 When auditors identify factors or risks related to fraud that has occurred or is likely to have occurred that they believe are significant within the context of the audit objectives, they should design procedures to provide reasonable assurance of detecting such fraud. Assessing the risk of fraud is an ongoing process throughout the audit and relates not only to planning the audit but also to evaluating evidence obtained during the audit.

7.32 When information comes to the auditors' attention indicating that fraud that is significant within the context of the audit objectives may have occurred, auditors should extend the audit steps and procedures, as necessary, to (1) determine whether fraud has likely occurred and (2) if so, determine its effect on the audit findings. If the fraud that may have occurred is not significant within the context of the audit objectives, the auditors may conduct additional audit work as a separate engagement, or refer the matter to other parties with oversight responsibility or jurisdiction.

Abuse

7.33 Abuse involves behavior that is deficient or improper when compared with behavior that a prudent person would consider reasonable and necessary business practice given the facts and circumstances. Abuse also includes misuse of authority or position for personal financial interests or those of an immediate or close family member or business associate. Abuse does not necessarily involve fraud, violation of laws, regulations, or provisions of a contract or grant agreement.

7.34 If during the course of the audit, auditors become aware of abuse that could be quantitatively or qualitatively significant to the program under audit, auditors should apply audit procedures specifically directed to ascertain the potential effect on the program under audit within the context of the audit objectives. After performing additional work, auditors may discover that the abuse represents potential fraud or illegal acts. Because the determination of abuse is subjective, auditors are not required to provide reasonable assurance of detecting abuse.

Ongoing Investigations or Legal Proceedings

7.35 Avoiding interference with investigations or legal proceedings is important in pursuing indications of fraud, illegal acts, violations of provisions of contracts or grant agreements, or abuse. Laws, regulations, or policies might require auditors to report indications of certain types of fraud, illegal acts, violations of provisions of contracts or grant agreements, or abuse to law enforcement or investigatory authorities before performing additional audit procedures. When investigations or legal proceedings are initiated or in process, auditors should evaluate the impact on the current audit. In some cases, it may be appropriate for the auditors to work with investigators and/or legal authorities, or withdraw from or defer further work on the audit or a portion of the audit to avoid interfering with an investigation.

Previous Audits and Attestation Engagements

7.36 Auditors should evaluate whether the audited entity has taken appropriate corrective action to address findings and recommendations from previous engagements that are significant within the context of the audit objectives. When planning the audit, auditors should ask management of the audited entity to identify previous audits, attestation engagements, performance audits, or other studies that directly relate to the objectives of the audit, including whether related recommendations have been implemented. Auditors should use this information in assessing risk and determining the nature, timing, and extent of current audit work, including determining the extent to which testing the implementation of the corrective actions is applicable to the current audit objectives.

Identifying Audit Criteria

7.37 Auditors should identify criteria. Criteria represent the laws, regulations, contracts, grant agreements, standards, measures, expected performance, defined business practices, and benchmarks against which performance is compared or evaluated. Criteria identify the required or desired state or expectation with respect to the program or operation. Criteria provide a context for evaluating evidence and understanding the findings, conclusions, and recommendations included in the report. Auditors should use criteria that are relevant to the audit objectives and permit consistent assessment of the subject matter.

7.38 The following are some examples of criteria:

a. purpose or goals prescribed by law or regulation or set by officials of the audited entity,

b. policies and procedures established by officials of the audited entity,

c. technically developed standards or norms,

d. expert opinions,

e. prior periods' performance,

f. defined business practices,

g. contract or grant terms, and

h. performance of other entities or sectors used as defined benchmarks.

Identifying Sources of Evidence and the Amount and Type of Evidence Required

7.39 Auditors should identify potential sources of information that could be used as evidence. Auditors should determine the amount and type of evidence needed to obtain sufficient, appropriate evidence to address the audit objectives and adequately plan audit work.

7.40 If auditors believe that it is likely that sufficient, appropriate evidence will not be available, they may revise the audit objectives or modify the scope and methodology and determine alternative procedures to obtain additional evidence or other forms of evidence to address the current audit objectives. Auditors should also evaluate whether the lack of sufficient, appropriate evidence is due to internal control deficiencies or other program weaknesses, and whether the lack of sufficient, appropriate evidence could be the basis for audit findings. (See paragraphs 7.55 through 7.71 for standards concerning evidence.)

Using the Work of Others

7.41 Auditors should determine whether other auditors have conducted, or are conducting, audits of the program that could be relevant to the current audit objectives. The results of other auditors' work may be useful sources of information for planning and performing the audit. If other auditors have identified areas that warrant further audit work or follow-up, their work may influence the auditors' selection of objectives, scope, and methodology.

7.42 If other auditors have completed audit work related to the objectives of the current audit, the current auditors may be able to use the work of the other auditors to support findings or conclusions for the current audit and, thereby, avoid duplication of efforts.

If auditors use the work of other auditors, they should perform procedures that provide a sufficient basis for using that work. Auditors should obtain evidence concerning the other auditors' qualifications and independence and should determine whether the scope, quality, and timing of the audit work performed by the other auditors is adequate for reliance in the context of the current audit objectives. Procedures that auditors may perform in making this determination include reviewing the other auditors' report, audit plan, or audit documentation, and/or performing tests of the other auditors' work. The nature and extent of evidence needed will depend on the significance of the other auditors' work to the current audit objectives and the extent to which the auditors will use that work.

7.43 Some audits may necessitate the use of specialized techniques or methods that require the skills of a specialist. If auditors intend to use the work of specialists, they should obtain an understanding of the qualifications and independence of the specialists. (See paragraph 3.05 for independence considerations when using the work of others.) Evaluating the professional qualifications of the specialist involves the following:

a. the professional certification, license, or other recognition of the competence of the specialist in his or her field, as appropriate;

b. the reputation and standing of the specialist in the views of peers and others familiar with the specialist's capability or performance;

c. the specialist's experience and previous work in the subject matter; and

d. the auditors' prior experience in using the specialist's work.

Assigning Staff and Other Resources

7.44 Audit management should assign sufficient staff and specialists with adequate collective professional competence to perform the audit. (See paragraph 3.43 for a discussion of using specialists in a GAGAS audit.) Staffing an audit includes, among other things:

a. assigning staff and specialists with the collective knowledge, skills, and experience appropriate for the job,

b. assigning a sufficient number of staff and supervisors to the audit,

c. providing for on-the-job training of staff, and

d. engaging specialists when necessary.

7.45 If planning to use the work of a specialist, auditors should document the nature and scope of the work to be performed by the specialist, including

a. the objectives and scope of the specialist's work,

b. the intended use of the specialist's work to support the audit objectives,

c. the specialist's procedures and findings so they can be evaluated and related to other planned audit procedures, and

d. the assumptions and methods used by the specialist.

Communicating with Management, Those Charged with Governance, and Others

7.46 Auditors should communicate an overview of the objectives, scope, and methodology, and timing of the performance audit[96] and planned reporting (including any potential restrictions on the report) to the following, as applicable:

a. management of the audited entity, including those with sufficient authority and responsibility to implement corrective action in the program or activity being audited;

b. those charged with governance;[97]

c. the individuals contracting for or requesting audit services, such as contracting officials, grantees; and

d. when auditors perform the audit pursuant to a law or regulation or they conduct the work for the legislative committee that has oversight of the audited entity, auditors should communicate with the legislative committee.

7.47 In situations in which those charged with governance are not clearly evident, auditors should document the process followed and conclusions reached for identifying those charged with governance.

7.48 Determining the form, content, and frequency of the communication is a matter of professional judgment, although written communication is preferred. Auditors may use an engagement letter to communicate the information. Auditors should document this communication.

[96]This does not apply when an element of surprise is critical to the audit objective, such as surprise audits, cash counts, or fraud-related procedures.

[97]Those charged with governance are those responsible for overseeing the strategic direction of the entity and the entity's fulfillment of its obligations related to accountability. (See appendix I, paragraphs A1.05 through A1.07.)

7.49 If an audit is terminated before it is completed and an audit report is not issued, auditors should document the results of the work to the date of termination and why the audit was terminated. Determining whether and how to communicate the reason for terminating the audit to those charged with governance, appropriate officials of the audited entity, the entity contracting for or requesting the audit, and other appropriate officials will depend on the facts and circumstances and, therefore, is a matter of professional judgment.

Preparing the Audit Plan

7.50 Auditors must prepare a written audit plan for each audit. The form and content of the written audit plan may vary among audits and may include an audit strategy, audit program, project plan, audit planning paper, or other appropriate documentation of key decisions about the audit objectives, scope, and methodology and the auditors' basis for those decisions. Auditors should update the plan, as necessary, to reflect any significant changes to the plan made during the audit.

7.51 A written audit plan provides an opportunity for the audit organization management to supervise audit planning and to determine whether

a. the proposed audit objectives are likely to result in a useful report,

b. the audit plan adequately addresses relevant risks,

c. the proposed audit scope and methodology are adequate to address the audit objectives,

d. available evidence is likely to be sufficient and appropriate for purposes of the audit, and

e. sufficient staff, supervisors, and specialists with adequate collective professional competence and other resources are available to perform the audit and to meet expected time frames for completing the work.

Supervision

7.52 Audit supervisors or those designated to supervise auditors must properly supervise audit staff.

7.53 Audit supervision involves providing sufficient guidance and direction to staff assigned to the audit to address the audit objectives and follow applicable standards, while staying informed about significant problems encountered, reviewing the work performed, and providing effective on-the-job training.

7.54 The nature and extent of the supervision of staff and the review of audit work may vary depending on a number of factors, such as the size of the audit organization, the significance of the work, and the experience of the staff.

Obtaining Sufficient, Appropriate Evidence

7.55 Auditors must obtain sufficient, appropriate evidence to provide a reasonable basis for their findings and conclusions.

7.56 The concept of sufficient, appropriate evidence is integral to an audit. Appropriateness is the measure of the quality of evidence that encompasses its relevance, validity, and reliability in providing support for findings and conclusions related to the audit objectives. In assessing the overall appropriateness of evidence, auditors should assess whether the evidence is relevant, valid, and reliable. Sufficiency is a measure of the quantity of evidence used to support the findings and conclusions related to the audit objectives. In assessing the sufficiency of evidence, auditors should determine whether enough evidence has been obtained to persuade a knowledgeable person that the findings are reasonable.

7.57 In assessing evidence, auditors should evaluate whether the evidence taken as a whole is sufficient and appropriate for addressing the audit objectives and supporting findings and conclusions. Audit objectives may vary widely, as may the level of work necessary to assess the sufficiency and appropriateness of evidence to address the objectives. For example, in establishing the appropriateness of evidence, auditors may test its reliability by obtaining supporting evidence, using statistical testing, or obtaining corroborating evidence. The concepts of audit risk and significance assist auditors with evaluating the audit evidence.

7.58 Professional judgment assists auditors in determining the sufficiency and appropriateness of evidence taken as a whole. Interpreting, summarizing, or analyzing evidence is typically used in the process of determining the sufficiency and appropriateness of evidence and in reporting the results of the audit work. When appropriate, auditors may use statistical methods to analyze and interpret evidence to assess its sufficiency.

Appropriateness

7.59 Appropriateness is the measure of the quality of evidence that encompasses the relevance, validity, and reliability of evidence used for addressing the audit objectives and supporting findings and conclusions. (See appendix I, paragraph A7.03 for additional guidance regarding assessing the appropriateness of evidence in relation to the audit objectives.)

a. Relevance refers to the extent to which evidence has a logical relationship with, and importance to, the issue being addressed.

b. Validity refers to the extent to which evidence is based on sound reasoning or accurate information.

c. Reliability refers to the consistency of results when information is measured or tested and includes the concepts of being verifiable or supported.

7.60 There are different types and sources of evidence that auditors may use, depending on the audit objectives. Evidence may be obtained by observation, inquiry, or inspection. Each type of evidence has its own strengths and weaknesses. (See appendix I, paragraph A7.02 for additional guidance regarding the types of evidence.) The following contrasts are useful in judging the appropriateness of evidence. However, these contrasts are not adequate in themselves to determine appropriateness. The nature and types of evidence to support auditors' findings and conclusions are matters of the auditors' professional judgment based on the audit objectives and audit risk.

a. Evidence obtained when internal control is effective is generally more reliable than evidence obtained when internal control is weak or nonexistent.

b. Evidence obtained through the auditors' direct physical examination, observation, computation, and inspection is generally more reliable than evidence obtained indirectly.

c. Examination of original documents is generally more reliable than examination of copies.

d. Testimonial evidence obtained under conditions in which persons may speak freely is generally more reliable than evidence obtained under circumstances in which the persons may be intimidated.

e. Testimonial evidence obtained from an individual who is not biased and has direct knowledge about the area is generally more reliable than testimonial evidence obtained from an individual who is biased or has indirect or partial knowledge about the area.

f. Evidence obtained from a knowledgeable, credible, and unbiased third party is generally more reliable than evidence from management of the audited entity or others who have a direct interest in the audited entity.

7.61 Testimonial evidence may be useful in interpreting or corroborating documentary or physical information. Auditors should evaluate the objectivity, credibility, and reliability of the testimonial evidence. Documentary evidence may be used to help verify, support, or challenge testimonial evidence.

7.62 Surveys generally provide self-reported information about existing conditions or programs. Evaluation of the survey design and administration assists auditors in evaluating the objectivity, credibility, and reliability of the self-reported information.

7.63 When sampling is used, the method of selection that is appropriate will depend on the audit objectives. When a representative sample is needed, the use of statistical sampling approaches generally results in stronger evidence than that obtained from nonstatistical techniques. When a representative sample is not needed, a targeted selection may be effective if the auditors have isolated certain risk factors or other criteria to target the selection.

7.64 When auditors use information gathered by officials of the audited entity as part of their evidence, they should determine what the officials of the audited entity or other auditors did to obtain assurance over the reliability of the information. The auditor may find it necessary to perform testing of management's procedures to obtain assurance or perform direct testing of the information. The nature and extent of the auditors' procedures will depend on the significance of the information to the audit objectives and the nature of the information being used.

7.65 Auditors should assess the sufficiency and appropriateness of computer-processed information regardless of whether this information is provided to auditors or auditors independently extract it. The nature, timing, and extent of audit procedures to assess sufficiency and appropriateness is affected by the effectiveness of the entity's internal controls over the information, including information systems controls, and the significance of the information and the level of detail presented in the auditors' findings and conclusions in light of the audit objectives. (See paragraphs 7.23 through 7.27 for additional discussion on assessing the effectiveness of information systems controls.)

Sufficiency

7.66 Sufficiency is a measure of the quantity of evidence used for addressing the audit objectives and supporting findings and conclusions. Sufficiency also depends on the appropriateness of the evidence. In determining the sufficiency of evidence, auditors should determine whether enough appropriate evidence exists to address the audit objectives and support the findings and conclusions.

7.67 The following presumptions are useful in judging the sufficiency of evidence. The sufficiency of evidence required to support the auditors' findings and conclusions is a matter of the auditors' professional judgment.

a. The greater the audit risk, the greater the quantity and quality of evidence required.

b. Stronger evidence may allow less evidence to be used.

c. Having a large volume of audit evidence does not compensate for a lack of relevance, validity, or reliability.

Overall Assessment of Evidence

7.68 Auditors should determine the overall sufficiency and appropriateness of evidence to provide a reasonable basis for the findings and conclusions, within the context of the audit objectives. Professional judgments about the sufficiency and appropriateness of evidence are closely interrelated, as auditors interpret the results of audit testing and evaluate whether the nature and extent of the evidence obtained is sufficient and appropriate. Auditors should perform and document an overall assessment of the collective evidence used to support findings and conclusions, including the results of any specific assessments conducted to conclude on the validity and reliability of specific evidence.

7.69 Sufficiency and appropriateness of evidence are relative concepts, which may be thought of in terms of a continuum rather than as absolutes. Sufficiency and appropriateness are evaluated in the context of the related findings and conclusions. For example, even though the auditors may have some limitations or uncertainties about the sufficiency or appropriateness of some of the evidence, they may nonetheless determine that in total there is sufficient, appropriate evidence to support the findings and conclusions.

7.70 When assessing the sufficiency and appropriateness of evidence, auditors should evaluate the expected significance of evidence to the audit objectives, findings, and conclusions, available corroborating evidence, and the level of audit risk. The steps to assess evidence may depend on the nature of the evidence, how the evidence is used in the audit or report, and the audit objectives.

a. Evidence is sufficient and appropriate when it provides a reasonable basis for supporting the findings or conclusions within the context of the audit objectives.

b. Evidence is not sufficient or not appropriate when (1) using the evidence carries an unacceptably high risk that it could lead to an incorrect or improper conclusion, (2) the evidence has significant limitations, given the audit objectives and intended use of the evidence, or (3) the evidence does not provide an adequate basis for addressing the audit objectives or supporting the findings and conclusions. Auditors should not use such evidence as support for findings and conclusions.

7.71 Evidence has limitations or uncertainties when the validity or reliability of the evidence has not been assessed or cannot be assessed, given the audit objectives and the intended use of the evidence. Limitations also include errors identified by the auditors in their testing. When the auditors identify limitations or uncertainties in evidence that is significant to the audit findings and conclusions, they should apply additional procedures, as appropriate. Such procedures include

a. seeking independent, corroborating evidence from other sources;

b. redefining the audit objectives or limiting the audit scope to eliminate the need to use the evidence;

c. presenting the findings and conclusions so that the supporting evidence is sufficient and appropriate and describing in the report the limitations or uncertainties with the validity or reliability of the evidence, if such disclosure is necessary to avoid misleading the report users about the findings or conclusions (see paragraph 8.15 for additional reporting requirements when there are limitations or uncertainties with the validity or reliability of evidence); or

d. determining whether to report the limitations or uncertainties as a finding, including any related, significant internal control deficiencies.

Developing Elements of a Finding

7.72 Auditors should plan and perform procedures to develop the elements of a finding necessary to address the audit objectives. In addition, if auditors are able to sufficiently develop the elements of a finding, they should develop recommendations for corrective action if they are significant within the context of the audit objectives. The elements needed for a finding depend entirely on the objectives of the audit. Thus, a finding or set of findings is complete to the extent that the audit objectives are addressed and the report clearly relates those objectives to the elements of a finding. For example, an audit objective may be limited to determining the current status or condition of program operations or progress in implementing legislative requirements, and not the related cause or effect. In this situation, developing the condition would address the audit objective and development of the other elements of a finding would not be necessary.

7.73 The element of criteria is discussed in paragraphs 7.37 and 7.38, and the other elements of a finding—condition, effect, and cause–are discussed in paragraphs 7.74 through 7.76.

7.74 Condition: Condition is a situation that exists. The condition is determined and documented during the audit.

7.75 Cause: The cause identifies the reason or explanation for the condition or the factor or factors responsible for the difference between the situation that exists (condition) and the required or desired state (criteria), which may also serve as a basis for recommendations for corrective actions. Common factors include poorly designed policies, procedures, or criteria; inconsistent, incomplete, or incorrect implementation; or factors beyond the control of program management. Auditors may assess whether the evidence provides a reasonable and convincing argument for why the stated cause is the key factor or factors contributing to the difference. When the audit objectives include explaining why a particular type of positive or negative program performance, output, or outcome identified in the audit occurred, they are referred to as "cause." Identifying the cause of problems may assist auditors in making constructive recommendations for correction. Because problems can result from a number of plausible factors or multiple causes, the recommendation can be more persuasive if auditors can clearly demonstrate and explain with evidence and reasoning the link between the problems and the factor or factors they have identified as the cause or causes. Auditors may identify deficiencies in program design or structure as the cause of deficient performance. Auditors may also identify deficiencies in internal control that are significant to the subject matter of the performance audit as the cause of deficient performance. In developing these types of findings, the deficiencies in program design or internal control would be described as the "cause." Often the causes of deficient program performance are complex and involve multiple factors, including fundamental, systemic root causes. Alternatively, when the audit objectives include estimating the program's effect on changes in physical, social, or economic conditions, auditors seek evidence of the extent to which the program itself is the "cause" of those changes.

7.76 Effect or potential effect: The effect is a clear, logical link to establish the impact or potential impact of the difference between the situation that exists (condition) and the required or desired state (criteria). The effect or potential effect identifies the outcomes or consequences of the condition. When the audit objectives include identifying the actual or potential consequences of a condition that varies (either positively or negatively) from the criteria identified in the audit, "effect" is a measure of those consequences. Effect or potential effect may be used to demonstrate the need for corrective action in response to identified problems or relevant risks. When the audit objectives include estimating the extent to which a program has caused changes in physical, social, or economic conditions, "effect" is a measure of the impact achieved by the program. In this case, effect is the extent to which positive or negative changes in actual physical, social, or economic conditions can be identified and attributed to the program.

Audit Documentation

7.77 Auditors must prepare audit documentation related to planning, conducting, and reporting for each audit. Auditors should prepare audit documentation in sufficient detail to enable an experienced auditor,[98] having no previous connection to the audit, to

[98]An experienced auditor means an individual (whether internal or external to the audit organization) who possesses the competencies and skills that would have enabled him or her to perform the performance audit. These competencies and skills include an understanding of (1) the performance audit processes, (2) GAGAS and applicable legal and regulatory requirements, (3) the subject matter associated with achieving the audit objectives, and (4) issues related to the audited entity's environment.

understand from the audit documentation the nature, timing, extent, and results of audit procedures performed, the audit evidence obtained and its source and the conclusions reached, including evidence that supports the auditors' significant judgments and conclusions. Auditors should prepare audit documentation that contains support for findings, conclusions, and recommendations before they issue their report.

7.78 Auditors should design the form and content of audit documentation to meet the circumstances of the particular audit. The audit documentation constitutes the principal record of the work that the auditors have performed in accordance with standards and the conclusions that the auditors have reached. The quantity, type, and content of audit documentation are a matter of the auditors' professional judgment.

7.79 Audit documentation is an essential element of audit quality. The process of preparing and reviewing audit documentation contributes to the quality of an audit. Audit documentation serves to (1) provide the principal support for the auditors' report, (2) aid auditors in conducting and supervising the audit, and (3) allow for the review of audit quality.

7.80 Under GAGAS, auditors should document the following:

a. the objectives, scope, and methodology of the audit;

b. the work performed to support significant judgments and conclusions, including descriptions of transactions and records examined;[99] and

c. evidence of supervisory review, before the audit report is issued, of the work performed that supports findings, conclusions, and recommendations contained in the audit report.

7.81 When auditors do not comply with applicable GAGAS requirements due to law, regulation, scope limitations, restrictions on access to records, or other issues impacting the audit, the auditors should document the departure from the GAGAS requirements and the impact on the audit and on the auditors' conclusions. This applies to departures from both mandatory requirements and presumptively mandatory requirements when alternative procedures performed in the circumstances were not sufficient to achieve the objectives of the standard. (See paragraphs 1.12 and 1.13.)

7.82 Audit organizations should establish policies and procedures for the safe custody and retention of audit documentation for a time sufficient to satisfy legal, regulatory, and administrative requirements for records retention. Whether audit documentation is in paper, electronic, or other media, the integrity, accessibility, and retrievability of the underlying information could be compromised if the documentation is altered, added to, or deleted without the auditors' knowledge, or if the documentation is lost or damaged. For audit documentation that is retained electronically, the audit

[99]Auditors may meet this requirement by listing file numbers, case numbers, or other means of identifying specific documents they examined. They are not required to include copies of documents they examined as part of the audit documentation, nor are they required to list detailed information from those documents.

organization should establish information systems controls concerning accessing and updating the audit documentation.

7.83 Underlying GAGAS audits is the premise that audit organizations in federal, state, and local governments and public accounting firms engaged to perform audits in accordance with GAGAS cooperate in auditing programs of common interest so that auditors may use others' work and avoid duplication of efforts. Subject to applicable laws and regulations, auditors should make appropriate individuals, as well as audit documentation, available upon request and in a timely manner to other auditors or reviewers to satisfy these objectives. The use of auditors' work by other auditors may be facilitated by contractual arrangements for GAGAS audits that provide for full and timely access to appropriate individuals, as well as audit documentation.

7.84 Audit organizations should develop policies to deal with requests by outside parties to obtain access to audit documentation, especially when an outside party attempts to obtain information indirectly through the auditor rather than directly from the audited entity. In developing such policies, audit organizations should determine what laws and regulations apply, if any.

Reporting Standards for Performance Audits

Introduction

8.01 This chapter establishes reporting standards and provides guidance for performance audits conducted in accordance with generally accepted government auditing standards (GAGAS). The reporting standards for performance audits relate to the form of the report, the report contents, and report issuance and distribution.

8.02 For performance audits performed in accordance with GAGAS, chapters 1 through 3 and 7 and 8 apply.

Reporting

8.03 Auditors must issue audit reports communicating the results of each completed performance audit.

8.04 Auditors should use a form of the audit report that is appropriate for its intended use and is in writing or in some other retrievable form. (See paragraph 8.42 for situations when audit organizations are subject to public records laws.) For example, auditors may present audit reports using electronic media that are retrievable by report users and the audit organization. The users' needs will influence the form of the audit report. Different forms of audit reports include written reports, letters, briefing slides, or other presentation materials.

8.05 The purposes of audit reports are to (1) communicate the results of audits to those charged with governance, the appropriate officials of the audited entity, and the appropriate oversight officials; (2) make the results less susceptible to misunderstanding; (3) make the results available to the public, as applicable (see paragraph 8.39 for additional guidance on classified or limited use reports and paragraph 8.43b for distribution of reports for internal auditors); and (4) facilitate follow-up to determine whether appropriate corrective actions have been taken.

8.06 If an audit is terminated before it is completed and an audit report is not issued, auditors should follow the guidance in paragraph 7.49.

8.07 If after the report is issued, the auditors discover that they did not have sufficient, appropriate evidence to support the reported findings or conclusions, they should communicate with those charged with governance, the appropriate officials of the audited entity, and the appropriate officials of the organizations requiring or arranging for the audits, so that they do not continue to rely on the findings or conclusions that were not supported. If the report was previously posted to the auditors' publicly accessible website, the auditors should remove the report and post a public notification that the report was removed. The auditors should then determine whether to conduct additional audit work necessary to reissue the report with revised findings or conclusions.

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8.08 Auditors should prepare audit reports that contain (1) the objectives, scope, and methodology of the audit; (2) the audit results, including findings, conclusions, and recommendations, as appropriate; (3) a statement about the auditors' compliance with GAGAS; (4) a summary of the views of responsible officials; and (5) if applicable, the nature of any confidential or sensitive information omitted.

Objectives, Scope, and Methodology

8.09 Auditors should include in the report a description of the audit objectives and the scope and methodology used for addressing the audit objectives. Report users need this information to understand the purpose of the audit, the nature and extent of the audit work performed, the context and perspective regarding what is reported, and any significant limitations in audit objectives, scope, or methodology.

8.10 Audit objectives for performance audits may vary widely. Auditors should communicate audit objectives in the audit report in a clear, specific, neutral, and unbiased manner that includes relevant assumptions, including why the audit organization undertook the assignment and the underlying purpose of the audit and resulting report. When audit objectives are limited and broader objectives can be inferred by users, stating in the audit report that certain issues were outside the scope of the audit can avoid potential misunderstanding.

8.11 Auditors should describe the scope of the work performed and any limitations, including issues that would be relevant to likely users, so that they could reasonably interpret the findings, conclusions, and recommendations in the report without being misled. Auditors should also report any significant constraints imposed on the audit approach by information limitations or scope impairments, including denials of access to certain records or individuals.

8.12 In describing the work conducted to address the audit objectives and support the reported findings and conclusions, auditors should, as applicable, explain the relationship between the population and the items tested; identify organizations, geographic locations, and the period covered; report the kinds and sources of evidence; and explain any significant limitations or uncertainties based on the auditors' overall assessment of the sufficiency and appropriateness of the evidence in the aggregate.

8.13 In reporting audit methodology, auditors should explain how the completed audit work supports the audit objectives, including the evidence gathering and analysis techniques, in sufficient detail to allow knowledgeable users of their reports to understand how the auditors addressed the audit objectives. When the auditors used extensive or multiple sources of information, the auditors may include a description of the procedures performed as part of their assessment of the sufficiency and appropriateness of information used as audit evidence. Auditors should identify significant assumptions made in conducting the audit; describe comparative techniques applied; describe the criteria used; and, when sampling significantly supports the auditors' findings, conclusions, or recommendations, describe the sample design and state why the design was chosen, including whether the results can be projected to the intended population.

Reporting Findings

8.14 In the audit report, auditors should present sufficient, appropriate evidence to support the findings and conclusions in relation to the audit objectives. Clearly developed findings, as discussed in paragraphs 7.72 through 7.76, assist management or oversight officials of the audited entity in understanding the need for taking corrective action. If auditors are able to sufficiently develop the elements of a finding, they should provide recommendations for corrective action if they are significant within the context of the audit objectives. However, the extent to which the elements for a finding are developed depends on the audit objectives. Thus, a finding or set of findings is complete to the extent that the auditors address the audit objectives.

8.15 Auditors should describe in their report limitations or uncertainties with the reliability or validity of evidence if (1) the evidence is significant to the findings and conclusions within the context of the audit objectives and (2) such disclosure is necessary to avoid misleading the report users about the findings and conclusions. As discussed in chapter 7, even though the auditors may have some uncertainty about the sufficiency or appropriateness of some of the evidence, they may nonetheless determine that in total there is sufficient, appropriate evidence given the findings and conclusions. Auditors should describe the limitations or uncertainties regarding evidence in conjunction with the findings and conclusions, in addition to describing those limitations or uncertainties as part of the objectives, scope, and methodology. Additionally, this description provides report users with a clear understanding regarding how much responsibility the auditors are taking for the information.

8.16 Auditors should place their findings in perspective by describing the nature and extent of the issues being reported and the extent of the work performed that resulted in the finding. To give the reader a basis for judging the prevalence and consequences of these findings, auditors should, as applicable, relate the instances identified to the population or the number of cases examined and quantify the results in terms of dollar value, or other measures, as appropriate. If the results cannot be projected, auditors should limit their conclusions appropriately.

8.17 Auditors may provide selective background information to establish the context for the overall message and to help the reader understand the findings and significance of the issues discussed.[100] When reporting on the results of their work, auditors should disclose significant facts relevant to the objectives of their work and known to them which, if not disclosed, could mislead knowledgeable users, misrepresent the results, or conceal significant improper or illegal practices.

[100]Appropriate background information may include information on how programs and operations work; the significance of programs and operations (e.g., dollars, impact, purposes, and past audit work, if relevant); a description of the audited entity's responsibilities; and explanation of terms, organizational structure, and the statutory basis for the program and operations.

8.18 Auditors should report deficiencies[101] in internal control that are significant within the context of the objectives of the audit, all instances of fraud, illegal acts[102] unless they are inconsequential within the context of the audit objectives, significant violations of provisions of contracts or grant agreements, and significant abuse that have occurred or are likely to have occurred.

Deficiencies in Internal Control

8.19 Auditors should include in the audit report (1) the scope of their work on internal control and (2) any deficiencies in internal control that are significant within the context of the audit objectives and based upon the audit work performed. When auditors detect deficiencies in internal control that are not significant to the objectives of the audit, they may include those deficiencies in the report or communicate those deficiencies in writing to officials of the audited entity unless the deficiencies are inconsequential considering both qualitative and quantitative factors. Auditors should refer to that written communication in the audit report, if the written communication is separate from the audit report. Determining whether or how to communicate to officials of the audited entity deficiencies that are inconsequential within the context of the audit objectives is a matter of professional judgment. Auditors should document such communications.

[101]As discussed in paragraph 7.21, in performance audits, 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 (1) misstatements in financial or performance information, (2) violations of laws and regulations, or (3) impairments of effectiveness or efficiency of operations, on a timely basis.

[102]Whether a particular act is, in fact, illegal may have to await final determination by a court of law or other adjudicative body. Disclosing matters that have led auditors to conclude that an illegal act is likely to have occurred is not a final determination of illegality.

8.20 In a performance audit, auditors may conclude that identified deficiencies in internal control that are significant within the context of the audit objectives are the cause of deficient performance of the program or operations being audited. In reporting this type of finding, the internal control deficiency would be described as the cause.

Fraud, Illegal Acts, Violations of Provisions of Contracts or Grant Agreements, and Abuse

8.21 When auditors conclude, based on sufficient, appropriate evidence, that fraud, illegal acts, significant violations of provisions of contracts or grant agreements, or significant abuse either has occurred or is likely to have occurred, they should report the matter as a finding.

8.22 When auditors detect violations of provisions of contracts or grant agreements, or abuse that are not significant, they should communicate those findings in writing to officials of the audited entity unless the findings are inconsequential within the context of the audit objectives, considering both qualitative and quantitative factors. Determining whether or how to communicate to officials of the audited entity fraud, illegal acts, violations of provisions of contracts or grant agreements, or abuse that is inconsequential is a matter of the auditors' professional judgment. Auditors should document such communications.

8.23 When fraud, illegal acts, violations of provisions of contracts or grant agreements, or abuse either have occurred or are likely to have occurred, auditors may consult with authorities or legal counsel about whether publicly reporting such information would compromise investigative or legal proceedings. Auditors may limit their public reporting to matters that would not compromise those proceedings, and for example, report only on information that is already a part of the public record.

Reporting Findings Directly to Parties Outside the Audited Entity

8.24 Auditors should report known or likely fraud, illegal acts, violations of provisions of contracts or grant agreements, or abuse directly to parties outside the audited entity in the following two circumstances.[103]

a. When entity management fails to satisfy legal or regulatory requirements to report such information to external parties specified in law or regulation, auditors should first communicate the failure to report such information to those charged with governance. If the audited entity still does not report this information to the specified external parties as soon as practicable after the auditors' communication with those charged with governance, then the auditors should report the information directly to the specified external parties.

b. When entity management fails to take timely and appropriate steps to respond to known or likely fraud, illegal acts, violations of provisions of contracts or grant agreements, or abuse that (1) is significant to the findings and conclusions, and (2) involves funding received directly or indirectly from a government agency, auditors should first report management's failure to take timely and appropriate steps to those charged with governance. If the audited entity still does not take timely and appropriate steps as soon as practicable after the auditors' communication with those charged with governance, then the auditors should report the entity's failure to take timely and appropriate steps directly to the funding agency.

8.25 The reporting in paragraph 8.24 is in addition to any legal requirements to report such information directly to parties outside the audited entity. Auditors

[103]Internal audit organizations do not have a duty to report outside the entity unless required by law, rule, regulation, or policy. (See paragraph 8.43b for reporting standards for internal audit organizations when reporting externally.)

should comply with these requirements even if they have resigned or been dismissed from the audit prior to its completion.

8.26 Auditors should obtain sufficient, appropriate evidence, such as confirmation from outside parties, to corroborate assertions by management of the audited entity that it has reported such findings in accordance with laws, regulations, and funding agreements. When auditors are unable to do so, they should report such information directly as discussed in paragraph 8.24.

Conclusions

8.27 Auditors should report conclusions, as applicable, based on the audit objectives and the audit findings. Report conclusions are logical inferences about the program based on the auditors' findings, not merely a summary of the findings. The strength of the auditors' conclusions depends on the sufficiency and appropriateness of the evidence supporting the findings and the soundness of the logic used to formulate the conclusions. Conclusions are stronger if they lead to the auditors' recommendations and convince the knowledgeable user of the report that action is necessary.

Recommendations

8.28 Auditors should recommend actions to correct problems identified during the audit and to improve programs and operations when the potential for improvement in programs, operations, and performance is substantiated by the reported findings and conclusions. Auditors should make recommendations that flow logically from the findings and conclusions, are directed at resolving the cause of identified problems, and clearly state the actions recommended.

8.29 Effective recommendations encourage improvements in the conduct of government programs and operations. Recommendations are effective when they are addressed to parties that have the authority to act and when the recommended actions are specific, practical, cost effective, and measurable.

Reporting Auditors' Compliance with GAGAS

8.30 When auditors comply with all applicable GAGAS requirements, they should use the following language, which represents an unmodified GAGAS compliance statement, in the audit report to indicate that they performed the audit in accordance with GAGAS. (See paragraphs 1.12 and 1.13.)

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

8.31 When auditors do not comply with all applicable GAGAS requirements, they should include a modified GAGAS compliance statement in the audit report. For performance audits, auditors should use a statement that includes either (1) the language in 8.30, modified to indicate the standards that were not followed or (2) language that the auditor did not follow GAGAS. (See paragraphs 1.12 and 1.13 for additional standards on citing compliance with GAGAS.)

Reporting Views of Responsible Officials

8.32 Providing a draft report with findings for review and comment by responsible officials of the audited entity and others helps the auditors develop a report that is fair, complete, and objective. Including the views of responsible officials results in a report that presents not only the auditors' findings, conclusions, and recommendations, but also the perspectives of the responsible officials of the audited entity and the corrective actions they plan to take. Obtaining the comments in writing is preferred, but oral comments are acceptable.

8.33 When auditors receive written comments from the responsible officials, they should include in their report a copy of the officials' written comments, or a summary of the comments received. When the responsible officials provide oral comments only, auditors should prepare a summary of the oral comments and provide a copy of the summary to the responsible officials to verify that the comments are accurately stated.

8.34 Auditors should also include in the report an evaluation of the comments, as appropriate. In cases in which the audited entity provides technical comments in addition to its written or oral comments on the report, auditors may disclose in the report that such comments were received.

8.35 Obtaining oral comments may be appropriate when, for example, there is a reporting date critical to meeting a user's needs; auditors have worked closely with the responsible officials throughout the conduct of the work and the parties are familiar with the findings and issues addressed in the draft report; or the auditors do not expect major disagreements with the findings, conclusions, and recommendations in the draft report, or major controversies with regard to the issues discussed in the draft report.

8.36 When the audited entity's comments are inconsistent or in conflict with the findings, conclusions, or recommendations in the draft report, or when planned corrective actions do not adequately address the auditors' recommendations, the auditors should evaluate the validity of the audited entity's comments. If the auditors disagree with the comments, they should explain in the report their reasons for disagreement. Conversely, the auditors should modify their report as necessary if they find the comments valid and supported with sufficient, appropriate evidence.

8.37 If the audited entity refuses to provide comments or is unable to provide comments within a reasonable period of time, the auditors may issue the report without receiving comments from the audited entity. In such cases, the auditors should indicate in the report that the audited entity did not provide comments.

Reporting Confidential or Sensitive Information

8.38 If certain pertinent information is prohibited from public disclosure or is excluded from a report due to the confidential or sensitive nature of the information, auditors should disclose in the report that certain information has been omitted and the reason or other circumstances that makes the omission necessary.

8.39 Certain information may be classified or may be otherwise prohibited from general disclosure by federal, state, or local laws or regulations. In such circumstances, auditors may issue a separate, classified or limited use report containing such information and distribute the report only to persons authorized by law or regulation to receive it.

8.40 Additional circumstances associated with public safety and security concerns could also justify the exclusion of certain information from a publicly available or widely distributed report. For example, detailed information related to computer security for a particular program may be excluded from publicly available reports because of the potential damage that could be caused by the misuse of this information. In such circumstances, auditors may issue a limited use report containing such information and distribute the report only to those parties responsible for acting on the auditors' recommendations. The auditors may consult with legal counsel regarding any requirements or other circumstances that may necessitate the omission of certain information.

8.41 Considering the broad public interest in the program or activity under review assists auditors when deciding whether to exclude certain information from publicly available reports. When circumstances call for omission of certain information, auditors should evaluate whether this omission could distort the audit results or conceal improper or illegal practices.

8.42 When audit organizations are subject to public records laws, auditors should determine whether public records laws could impact the availability of classified or limited use reports and determine whether other means of communicating with management and those charged with governance would be more appropriate. For example, the auditors may communicate general information in a written report and communicate detailed information verbally. The auditor may consult with legal counsel regarding applicable public records laws.

Distributing Reports

8.43 Distribution of reports completed under GAGAS depends on the relationship of the auditors to the audited organization and the nature of the information contained in the report. If the subject of the audit involves material that is classified for security purposes or contains confidential or sensitive information, auditors may limit the report distribution. (See paragraphs 8.38 through 8.42 for additional guidance on limited report distribution.) Auditors should document any limitation on report distribution. The following discussion outlines distribution for reports completed under GAGAS:

a. Audit organizations in government entities should distribute audit reports to those charged with governance, to the appropriate officials of the audited entity, and to the appropriate oversight bodies or organizations requiring or arranging for the audits. As appropriate, auditors should also distribute copies of the reports to other officials who have legal oversight authority or who may be responsible for acting on audit findings and recommendations, and to others authorized to receive such reports.

b. Internal audit organizations in government entities may follow the Institute of Internal Auditors (IIA) *International Standards for the Professional Practice of Internal Auditing.* Under GAGAS and IIA standards, the head of the internal audit organization should communicate results to parties who can ensure that the results are given due consideration. If not otherwise mandated by statutory or regulatory requirements, prior to releasing results to parties outside the organization, the head of the internal audit organization should: (1) assess the potential risk to the organization, (2) consult with senior management and/or legal counsel as appropriate, and (3) control dissemination by indicating the intended users of the report.

c. Public accounting firms contracted to perform an audit under GAGAS should clarify report distribution responsibilities with the engaging organization. If the contracted firm is to make the distribution, it should reach agreement with the party contracting for the audit about which officials or organizations will receive the report and the steps being taken to make the report available to the public.

Supplemental Guidance

Introduction

A.01 The following sections provide supplemental guidance for auditors and the audited entities to assist in the implementation of generally accepted government auditing standards (GAGAS). The guidance does not establish additional requirements but instead is intended to facilitate auditor implementation of GAGAS in chapters 1 through 8. The supplemental guidance in the first section may be of assistance for all types of audits and engagements covered by GAGAS. Subsequent sections provide supplemental guidance for specific chapters of GAGAS, as indicated.

Overall Supplemental Guidance

A.02 Chapters 4 through 8 discuss the field work and reporting standards for financial audits, attestation engagements, and performance audits. The identification of significant deficiencies in internal control, significant abuse, fraud risks, illegal acts, and significant violations of provisions of contracts or grant agreements are important aspects of government auditing. The following discussion is provided to assist auditors in identifying significant deficiencies in internal control, abuse, and indicators of fraud risk and to assist auditors in determining whether illegal acts and violations of provisions of contracts or grant agreements are significant within the context of the audit objectives.

Examples of Deficiencies in Internal Control

A.03 GAGAS contain requirements for reporting identified deficiencies in internal control.

- For financial audits, see paragraphs 5.10 through 5.14.
- For attestation engagements, see paragraphs 6.33 through 6.35.
- For performance audits, see paragraphs 8.18 through 8.20.

A.04 The following are examples of control deficiencies:

a. Insufficient control consciousness within the organization, for example the tone at the top and the control environment. Control deficiencies in other components of internal control could lead the auditor to conclude that weaknesses exist in the control environment.

b. Ineffective oversight by those charged with governance of the entity's financial reporting, performance reporting, or internal control, or an ineffective overall governance structure.

c. Control systems that did not prevent or detect material misstatements so that it was later necessary to restate previously issued financial statements or operational results. Control systems that did not prevent or detect material misstatements in performance or operational results so that it was later necessary to make significant corrections to those results.

d. Control systems that did not prevent or detect material misstatements identified by the auditor. This includes misstatements involving estimation and judgment for which the auditor identifies potential material adjustments and corrections of the recorded amounts.

e. An ineffective internal audit function or risk assessment function at an entity for which such functions are important to the monitoring or risk assessment component of internal control, such as for a very large or highly complex entity.

f. Identification of fraud of any magnitude on the part of senior management.

g. Failure by management or those charged with governance to assess the effect of a significant deficiency previously communicated to them and either to correct it or to conclude that it will not be corrected.

h. Inadequate controls for the safeguarding of assets.

i. Evidence of intentional override of internal control by those in authority to the detriment of the overall objectives of the system.

j. Deficiencies in the design or operation of internal control that could result in violations of laws, regulations, provisions of contracts or grant agreements, fraud, or abuse having a direct and material effect on the financial statements or the audit objective.

k. Inadequate design of information systems general and application controls that prevent the information system from providing complete and accurate information consistent with financial or performance reporting objectives and other current needs.

l. Failure of an application control caused by a deficiency in the design or operation of an information systems general control.

m. Employees or management who lack the qualifications and training to fulfill their assigned functions.

Examples of Abuse

A.05 GAGAS contain requirements for responding to indications of material abuse and reporting abuse that is material to the audit objectives.

- For financial audits, see paragraphs 4.12 and 4.13 and paragraphs 5.15 through 5.17.

- For attestation engagements, see paragraphs 6.13c and 6.14 and paragraphs 6.36c through 6.38.

- For performance audits, see paragraphs 7.33 and 7.34 and paragraphs 8.21 through 8.23.

A.06 The following are examples of abuse, depending on the facts and circumstances:

a. Creating unneeded overtime.

b. Requesting staff to perform personal errands or work tasks for a supervisor or manager.

c. Misusing the official's position for personal gain (including actions that could be perceived by an objective third party with knowledge of the relevant information as improperly benefiting an official's personal financial interests or those of an immediate or close family member; a general partner; an organization for which the official serves as an officer, director, trustee, or employee; or an organization with which the official is negotiating concerning future employment).

d. Making travel choices that are contrary to existing travel policies or are unnecessarily extravagant or expensive.

e. Making procurement or vendor selections that are contrary to existing policies or are unnecessarily extravagant or expensive.

Examples of Indicators of Fraud Risk

A.07 GAGAS contain requirements relating to evaluating fraud risk.

- For financial audits, see paragraphs 4.27 and 4.28 and paragraphs 5.15 through 5.17.

- For attestation engagements, see paragraphs 6.13a and b and paragraphs 6.36 through 6.38.
- For performance audits, see paragraphs 7.30 through 7.32 and paragraphs 8.21 through 8.23.

A.08 In some circumstances, conditions such as the following might indicate a heightened risk of fraud:

a. the entity's financial stability, viability, or budget is threatened by economic, programmatic, or entity operating conditions;

b. the nature of the audited entity's operations provide opportunities to engage in fraud;

c. inadequate monitoring by management for compliance with policies, laws, and regulations;

d. the organizational structure is unstable or unnecessarily complex;

e. lack of communication and/or support for ethical standards by management;

f. management has a willingness to accept unusually high levels of risk in making significant decisions;

g. a history of impropriety, such as previous issues with fraud, waste, abuse, or questionable practices, or past audits or investigations with findings of questionable or criminal activity;

h. operating policies and procedures have not been developed or are outdated;

i. key documentation is lacking or does not exist;

j. lack of asset accountability or safeguarding procedures;

k. improper payments;

l. false or misleading information;

m. a pattern of large procurements in any budget line with remaining funds at year end, in order to "use up all of the funds available"; and

n. unusual patterns and trends in contracting, procurement, acquisition, and other activities of the entity or program under audit.

Determining Whether Laws, Regulations, or Provisions of Contracts or Grant Agreements Are Significant within the Context of the Audit Objectives

A.09 GAGAS contain requirements for determining whether laws, regulations, or provisions of contracts or grant agreements are significant within the context of the audit objectives.

- For financial audits, see paragraphs 4.10 and 4.11.
- For attestation engagements, see paragraphs 6.13a and b.
- For performance audits, see paragraphs 7.28 and 7.29.

A.10 Government programs are subject to many laws, regulations, and provisions of contracts or grant agreements. At the same time, their significance within the context of the audit objectives varies widely, depending on the objectives of the audit. Auditors may find the following approach helpful in assessing whether laws, regulations, or provisions of contracts or grant agreements are significant within the context of the audit objectives:

a. Express each audit objective in terms of questions about specific aspects of the program being audited (that is, purpose and goals, internal control, inputs, program operations, outputs, and outcomes).

b. Identify laws, regulations, and provisions of contracts or grant agreements that directly relate to specific aspects of the program within the context of the audit objectives.

c. Determine if the audit objectives or the auditors' conclusions could be significantly affected if violations of those laws, regulations, or provisions of contracts or grant agreements occurred. If the audit objectives or audit conclusions could be significantly affected, then those laws, regulations, and provisions of contracts or grant agreements are likely to be significant to the audit objectives.

A.11 Auditors may consult with either their own or management's legal counsel to (1) determine those laws and regulations that are significant to the audit objectives, (2) design tests of compliance with laws and regulations, or (3) evaluate the results of those tests. Auditors also may consult with either their own or management's legal counsel when audit objectives require testing compliance with provisions of contracts or grant agreements. Depending on the circumstances of the audit, auditors may consult with others, such as investigative staff, other audit organizations or government entities that provided professional services to the audited entity, or applicable law enforcement authorities, to obtain information on compliance matters.

Information to Accompany Chapter 1

A1.01 Chapter 1 discusses the use and application of GAGAS and the role of auditing in government accountability. Those charged with governance and management of audited organizations also have roles in government accountability. The discussion that follows is provided to assist auditors in understanding the roles of others in accountability. The following section also contains background information on the laws, regulations, and guidelines that require the use of GAGAS. This information is provided to place GAGAS within the context of overall government accountability.

Laws, Regulations, and Guidelines That Require Use of GAGAS

A1.02 Laws, regulations, contracts, grant agreements, or policies frequently require the use of GAGAS. (See paragraph 1.04.) The following are among the laws, regulations, and guidelines that require the use of GAGAS:

a. The Inspector General Act of 1978, as amended, 5 U.S.C. App. requires that the statutorily appointed federal inspectors general comply with GAGAS for audits of federal establishments, organizations, programs, activities, and functions. The act further states that the inspectors general shall take appropriate steps to assure that any work performed by nonfederal auditors complies with GAGAS.

b. The Chief Financial Officers Act of 1990 (Public Law 101-576), as expanded by the Government Management Reform Act of 1994 (Public Law 103-356), requires that GAGAS be followed in audits of executive branch departments' and agencies' financial statements. The Accountability of Tax Dollars Act of 2002 (Public Law 107-289) extends this requirement to most executive agencies not subject to the Chief Financial Officers Act unless they are exempted for a given year by the Office of Management and Budget (OMB).

c. The Single Audit Act Amendments of 1996 (Public Law 104-156) require that GAGAS be followed in audits of state and local governments and nonprofit entities that receive federal awards.[104] OMB Circular No. A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, which provides the governmentwide guidelines and policies on performing audits to comply with the Single Audit Act, also requires the use of GAGAS.

A1.03 Other laws, regulations, or other authoritative sources may require the use of GAGAS. For example, auditors at the state and local levels of government may be required by state and local laws and regulations to follow GAGAS. Also, auditors may be required by the terms of an agreement or contract to follow GAGAS. Auditors may also be required to follow GAGAS by federal audit guidelines pertaining to program requirements, such as those issued for Housing and Urban Development programs and Student Financial Aid programs. Being alert to such other laws, regulations, or authoritative sources may assist auditors in performing their work in accordance with the required standards.

A1.04 Even if not required to do so, auditors may find it useful to follow GAGAS in performing audits of federal, state, and local government programs as well as in performing audits of government awards administered by contractors, nonprofit entities, and other nongovernment entities. Many audit organizations not formally required to do so, both in the United States of America and in other countries, voluntarily follow GAGAS.

[104]Under the Single Audit Act, as amended, federal awards include federal financial assistance (grants, loans, loan guarantees, property, cooperative agreements, interest subsidies, insurance, food commodities, direct appropriations, or other assistance) and cost-reimbursement contracts.

The Role of Those Charged with Governance in Accountability

A1.05 During the course of GAGAS audits, auditors communicate with those charged with governance.

- For financial audits, see paragraphs 4.05 and 4.06.
- For attestation engagements, see paragraphs 6.06 through 6.08.
- For performance audits, see paragraphs 7.46 through 7.49.

A1.06 Those charged with governance have the duty to oversee the strategic direction of the entity and obligations related to the accountability of the entity. This includes overseeing the financial reporting process, subject matter, or program under audit including related internal controls. In certain entities covered by GAGAS, those charged with governance also may be part of the entity's management. In some audit entities, multiple parties may be charged with governance, including oversight bodies, members or staff of legislative committees, boards of directors, audit committees, or parties contracting for the audit.

A1.07 Because the governance structures of government entities and organizations can vary widely, it may not always be clearly evident who is charged with key governance functions. In these situations, auditors evaluate the organizational structure for directing and controlling operations to achieve the entity's objectives. This evaluation also includes how the government entity delegates authority and establishes accountability for its management personnel.

Management's Role in Accountability

A1.08 Government managers have fundamental responsibilities for carrying out government functions. (See paragraph 1.02.) Management of the audited entity is responsible for

a. using government resources legally, effectively, efficiently, economically, ethically, and equitably to achieve the purposes for which the resources were furnished or the program was established;[105]

b. complying with applicable laws and regulations (including identifying the requirements with which the entity and the official are responsible for compliance);

c. implementing systems designed to achieve compliance with applicable laws and regulations;

d. establishing and maintaining effective internal control to help ensure that appropriate goals and objectives are met; using resources efficiently, economically, effectively, and equitably, and safeguarding resources; following laws and regulations; and ensuring that management and financial information is reliable and properly reported;

e. providing appropriate reports to those who oversee their actions and to the public in order to demonstrate accountability for the resources and authority used to carry out government programs and the results of these programs;

f. addressing the findings and recommendations of auditors, and for establishing and maintaining a process to track the status of such findings and recommendations;

g. following sound procurement practices when contracting for audits and attestation engagements,

[105]This responsibility applies to all resources, both financial and physical, as well as informational resources, whether entrusted to public officials or others by their own constituencies or by other levels of government.

including ensuring procedures are in place for monitoring contract performance; and

h. taking timely and appropriate steps to remedy fraud, illegal acts, violations of provisions of contracts or grant agreements, or abuse that auditors report to it.

Information to Accompany Chapter 3

A3.01 Chapter 3 discusses the general standards applicable to financial audits, attestation engagements, and performance audits under GAGAS. Auditors may also provide professional services, other than audits and attestation engagements, which are sometimes referred to as nonaudit services or consulting services. GAGAS do not cover nonaudit services since such services are not audits or attestation engagements. If an audit organization decides to perform nonaudit services, their independence for performing audits or attestation engagements may be impacted. Nonaudit services which may impair or do impair auditor independence are discussed in chapter 3. (See paragraphs 3.20 through 3.30.) The following supplemental guidance is provided to assist auditors and audited entities in identifying nonaudit services that are often provided by audit organizations in government entities without impairing their independence with respect to entities for which they provide audits or attestation engagements.

Nonaudit Services

A3.02 Audit organizations in government entities frequently provide nonaudit services that differ from the traditional professional services provided by an accounting or consulting firm to or for the audited entity. These types of nonaudit services are often performed in response to a statutory requirement, at the discretion of the authority of the audit organization, or for a legislative oversight body or an independent external organization and do not impair auditor independence. (See paragraphs 3.20 through 3.30 for the requirements for evaluating whether nonaudit services impair auditor independence.)

A3.03 Examples of these types of services include the following:

a. providing information or data to a requesting party without auditor evaluation or verification of the information or data;

b. developing standards, methodologies, audit guides, audit programs, or criteria for use throughout the government or for use in certain specified situations;

c. collaborating with other professional organizations to advance auditing of government entities and programs;

d. developing question and answer documents to promote understanding of technical issues or standards;

e. providing assistance and technical expertise to legislative bodies or independent external organizations and assisting legislative bodies by developing questions for use at a hearing;

f. providing training, speeches, and technical presentations;

g. developing surveys, collecting responses on behalf of others, and reporting results as "an independent third party";

h. providing oversight assistance in reviewing budget submissions;

i. contracting for audit services on behalf of an audited entity and overseeing the audit contract, as long as the overarching principles are not violated and the auditor under contract reports to the audit organization and not to management;

j. identifying good business practices for users in evaluating program or management system approaches, including financial and information management systems; and

k. providing audit, investigative, and oversight-related services that do not involve a GAGAS audit (but which could be performed as an audit, if the audit organization elects to do so), such as

(1) investigations of alleged fraud, violation of contract provisions or grant agreements, or abuse;

(2) review-level work such as sales tax reviews that are designed to review whether governmental entities receive from businesses, merchants, and vendors all of the sales taxes to which they are entitled;

(3) periodic audit recommendation follow-up engagements and reports;

(4) identifying best practices or leading practices for use in advancing the practices of government organizations;

(5) analyzing cross-cutting and emerging issues; and

(6) providing forward-looking analysis involving programs.

System of Quality Control

A3.04 Chapter 3 discusses the elements of an audit organization's system of quality control. The following supplemental guidance is provided to assist auditors and audit organizations in establishing policies and procedures in its system of quality control to address the following elements from paragraph 3.53: (1) audit and attestation engagement performance, documentation, and reporting and (2) monitoring of quality.

a. GAGAS standards for audit and attestation engagement performance, documentation, and reporting are in chapters 4 and 5 for financial audits, chapter 6 for attestation engagements, and chapters 7 and 8 for performance audits. Chapter 3 specifies that an audit organization's quality control system include policies and procedures designed to provide the audit organization with reasonable assurance that audits and attestation engagements are performed and reports are issued in accordance with professional standards and legal and regulatory requirements. (See paragraph 3.52) Examples of such policies and procedures include the following:

(1) communication provided to team members so that they sufficiently understand the objectives of their work and the applicable professional standards;

(2) audit and attestation engagement planning and supervision;

(3) appropriate documentation of the work performed;

(4) review of the work performed, the significant judgments made, and the resulting audit documentation and report;

(5) review of the independence and qualifications of any outside experts or contractors used, as well as a review of the scope and quality of their work;

(6) procedures for resolving difficult or contentious issues or disagreements among team members, including specialists;

(7) obtaining and addressing comments from the audited entity on draft reports; and

(8) reporting supported by the evidence obtained, and in accordance with applicable professional standards and legal and regulatory requirements.

b. Monitoring is an ongoing, periodic assessment of audit and attestation engagements designed to provide management of the audit organization with reasonable assurance that the policies and procedures related to the system of quality control are suitability designed and operating effectively in practice. (See paragraph 3.53f) The following guidance is provided to assist audit organizations with implementing and continuing its monitoring of quality:

(1) Who: Monitoring is most effective when performed by persons who do not have responsibility for the specific activity being monitored (e.g., for specific engagements or specific centralized processes). The staff member or team of staff members assigned with responsibility for the monitoring process collectively need sufficient and appropriate competence and authority in the audit organization to assume that responsibility. Generally the staff member or the team of staff members performing the monitoring are apart from the normal audit supervision associated with individual audits.

(2) How much: The extent of monitoring procedures varies based on the audit organization's circumstances to enable the audit organization to assess compliance with applicable professional standards and the audit organization's quality control policies and procedures. Examples of specific monitoring procedures include

(a) examination of selected administrative and personnel records pertaining to quality control;

(b) review of selected audit and attest documentation, and reports;

(c) discussions with the audit organization's personnel (as applicable and appropriate);

(d) periodic summarization of the findings from the monitoring procedures in writing, (at least annually), and consideration of the systematic causes of findings that indicate improvements are needed;

(e) determination of any corrective actions to be taken or improvements to be made with respect to the specific audits and attestation engagements reviewed or the audit organization's quality control policies and procedures;

(f) communication of the identified findings to appropriate audit organization management with subsequent follow-up; and

(g) consideration of findings by appropriate audit organization management personnel who also determine whether actions necessary, including necessary modifications to the quality control system, are performed on a timely basis.

(3) Review of selected administrative and personnel records: The review of selected administrative and personnel records pertaining to quality control may include tests of

(a) compliance with policies and procedures on independence;

(b) compliance with continuing professional development policies, including training;

(c) procedures related to recruitment and hiring of qualified personnel, including hiring of specialists or consultants when needed;

(d) procedures related to performance evaluation and advancement of personnel;

(e) procedures related to initiation, acceptance, and continuance of audit and attestation engagements;

(f) audit organization personnel's understanding of the quality control policies and procedures, and implementation of these policies and procedures; and

(g) audit organization's process for updating its policies and procedures.

(4) Follow-up on previous findings: Monitoring procedures include an evaluation of whether the audit organization has taken appropriate corrective action to address findings and recommendations from previous monitoring and peer reviews. Personnel involved in monitoring use this information as part of the assessment of risk associated with the design and implementation of the audit organization's quality control system and in determining the nature, timing, and extent of monitoring procedures.

(5) Written report: The audit organization communicates the results of the monitoring of its quality control systems in a written report that allows the audit organization to take prompt and appropriate action where necessary. Information included in this report includes:

(a) a description of the monitoring procedures performed;

(b) the conclusions drawn from the monitoring procedures; and

(c) where relevant, a description of the systemic, repetitive, or other significant deficiencies and of the actions taken to resolve those deficiencies.

A3.05 As discussed in paragraph 3.61, an external audit organization should make its most recent peer review report publicly available. Examples of how to achieve this transparency requirement include posting the peer review report on an external Web site or to a publicly available file. To help the public understand the peer review reports, an audit organization may also include a description of the peer review process and how it applies to its organization. The following provides examples of additional information that audit organizations may include to help users understand the meaning of the peer review report.

a. Explanation of the peer review process.

b. Description of the audit organization's system of quality control.

c. Explanation of the relationship of the peer review results to the audited organization's work.

d. If the peer review report is modified, explanation of the reviewed audit organization's plan for improving quality controls and the status of the improvements.

Information to Accompany Chapter 7

A7.01 Chapter 7 discusses the field work standards for performance audits. An integral concept for performance auditing is the use of sufficient, appropriate evidence based on the audit objectives to support a sound basis for audit findings, conclusions, and recommendations. The following discussion is provided to assist auditors in identifying the various types of evidence and assessing the appropriateness of evidence in relation to the audit objectives.

Types of Evidence

A7.02 In terms of its form and how it is collected, evidence may be categorized as physical, documentary, or testimonial. Physical evidence is obtained by auditors' direct inspection or observation of people, property, or events. Such evidence may be documented in summary memos, photographs, videos, drawings, charts, maps, or physical samples. Documentary evidence is obtained in the form of already existing information such as letters, contracts, accounting records, invoices, spreadsheets, database extracts, electronically stored information, and management information on performance. Testimonial evidence is obtained through inquiries, interviews, focus groups, public forums, or questionnaires. Auditors frequently use analytical processes including computations, comparisons, separation of information into components, and rational arguments to analyze any evidence gathered to determine whether it is sufficient and appropriate. (See paragraphs 7.66 and 7.59 for definitions of sufficient and appropriate.) The strength and weakness of each form of evidence depends on the facts and circumstances associated with the evidence and professional judgment in the context of the audit objectives.

Appropriateness of Evidence in Relation to the Audit Objectives

A7.03 One of the primary factors influencing the assurance associated with a performance audit is the appropriateness of the evidence in relation to the audit objectives. For example:

a. The audit objectives might focus on verifying specific quantitative results presented by the audited entity. In these situations, the audit procedures would likely focus on obtaining evidence about the accuracy of the specific amounts in question. This work may include the use of statistical sampling.

b. The audit objectives might focus on the performance of a specific program or activity in the agency being audited. In these situations, the auditor may be provided with information compiled by the agency being audited in order to answer the audit objectives. The auditor may find it necessary to test the quality of the information, which includes both its validity and reliability.

c. The audit objectives might focus on information that is used for widely accepted purposes and obtained from sources generally recognized as appropriate. For example, economic statistics issued by government agencies for purposes such as adjusting for inflation, or other such information issued by authoritative organizations, may be the best information available. In such cases, it may not be practical or necessary for auditors to conduct procedures to verify the information. These decisions call for professional judgment based on the nature of the information, its common usage or acceptance, and how it is being used in the audit.

d. The audit objectives might focus on comparisons or benchmarking between various government functions or agencies. These types of audits are especially useful for analyzing the outcomes of various public policy decisions. In these cases, auditors may perform analyses, such as comparative statistics of different jurisdictions or changes in performance over time, where it would be impractical to verify the detailed data underlying the statistics. Clear disclosure as to what extent the comparative information or statistics were evaluated or corroborated will likely be necessary to place the evidence in proper context for report users.

e. The audit objectives might focus on trend information based on data provided by the audited entity. In this situation, auditors may assess the evidence by using overall analytical tests of underlying data, combined with a knowledge and understanding of the systems or processes used for compiling information.

f. The audit objectives might focus on the auditor identifying emerging and cross-cutting issues using information compiled or self-reported by agencies. In such cases, it may be helpful for the auditor to consider the overall appropriateness of the compiled information along with other information available about the program. Other sources of information, such as inspector general reports or other external audits, may provide the auditors with information regarding whether any unverified or self-reported information is consistent with or can be corroborated by these other external sources of information.

Information to Accompany Chapter 8

A8.01 Chapter 8 discusses the reporting standards for performance audits. The following discussion is provided to assist auditors in developing and writing their audit report for performance audits.

Report Quality Elements

A8.02 The auditor may use the report quality elements of timely, complete, accurate, objective, convincing, clear, and concise when developing and writing the auditor's report as the subject permits.

a. Accurate: An accurate report is supported by sufficient, appropriate evidence with key facts, figures, and findings being traceable to the audit evidence. Reports that are fact-based, with a clear statement of sources, methods, and assumptions so that report users can judge how much weight to give the evidence reported, assist in achieving accuracy. Disclosing data limitations and other disclosures also contribute to producing more accurate audit reports. Reports also are more accurate when the findings are presented in the broader context of the issue. One way to help audit organizations prepare accurate audit reports is to use a quality control process such as referencing. Referencing is a process in which an experienced auditor who is independent of the audit checks that statements of facts, figures, and dates are correctly reported, that the findings are adequately supported by the evidence in the audit documentation, and that the conclusions and recommendations flow logically from the evidence.

b. Objective: Objective means that the presentation of the report is balanced in content and tone. A report's credibility is significantly enhanced when it presents evidence in an unbiased manner and in the proper context. This means presenting the audit results impartially and fairly. The tone of reports may encourage decision makers to act on the auditors' findings and recommendations. This balanced tone can be achieved when reports present sufficient, appropriate evidence to support conclusions while refraining from using adjectives or adverbs that characterize evidence in a way that implies criticism or unsupported conclusions. The objectivity of audit reports is enhanced when the report explicitly states the source of the evidence and the assumptions used in the analysis. The report may recognize the positive aspects of the program reviewed if applicable to the audit objectives. Inclusion of positive program aspects may lead to improved performance by other government organizations that read the report. Audit reports are more objective when they demonstrate that the work has been performed by professional, unbiased, independent, and knowledgeable staff.

c. Complete: Being complete means that the report contains sufficient, appropriate evidence needed to satisfy the audit objectives and promote an understanding of the matters reported. It also means the report states evidence and findings without omission of significant relevant information related to the audit objectives. Providing report users with an understanding means providing perspective on the extent and significance of reported findings, such as the frequency of occurrence relative to the number of cases or transactions tested and the relationship of the findings to the entity's operations. Being complete also means clearly stating what was and was not done and explicitly describing data limitations, constraints imposed by restrictions on access to records, or other issues.

d. Convincing: Being convincing means that the audit results are responsive to the audit objectives, that the findings are presented persuasively, and that the conclusions and recommendations flow logically from the facts presented. The validity of the findings, the reasonableness of the conclusions, and the benefit of implementing the recommendations are more convincing when supported by sufficient, appropriate evidence. Reports designed in this way can help focus the attention of responsible officials on the matters that warrant attention and can provide an incentive for taking corrective action.

e. Clear: Clarity means the report is easy for the intended user to read and understand. Preparing the report in language as clear and simple as the subject permits assists auditors in achieving this goal. Use of straightforward, nontechnical language is helpful to simplify presentation. Defining technical terms, abbreviations, and acronyms that are used in the report is also helpful. Auditors may use a highlights page or summary within the report to capture the report user's attention and highlight the overall message. If a summary is used, it is helpful if it focuses on the specific answers to the questions in the audit objectives, summarizes the audit's most significant findings and the report's principal conclusions, and prepares users to anticipate the major recommendations. Logical organization of material, and accuracy and precision in stating facts and in drawing conclusions assist in the report's clarity and understanding. Effective use of titles and captions and topic sentences makes the report easier to read and understand. Visual aids (such as pictures, charts, graphs, and maps) may clarify and summarize complex material.

f. Concise: Being concise means that the report is not longer than necessary to convey and support the message. Extraneous detail detracts from a report, may even conceal the real message, and may confuse or distract the users. Although room exists for considerable judgment in determining the content of reports, those that are fact-based but concise are likely to achieve results.

g. Timely: To be of maximum use, providing relevant evidence in time to respond to officials of the audited entity, legislative officials, and other users' legitimate needs is the auditors' goal. Likewise, the evidence provided in the report is more helpful if it is current. Therefore, the timely issuance of the report is an important reporting goal for auditors. During the audit, the auditors may provide interim reports of significant matters to appropriate entity officials. Such communication alerts officials to matters needing immediate attention and allows them to take corrective action before the final report is completed.

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