



## **Audit Committee**

12:00 PM

Via Zoom: (link)

Meeting ID: (ID)

Passcode: (passcode)

Deschutes County Administration Services Building,  
1st Floor, DeArmond Conference Room

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### **I. Call to Order**

### **II. Introductions/Notices**

### **III. Review/Approve minutes from [previous date's] meeting**

1. Review/Approve minutes from the December 8, 2023 meeting

### **IV. Special Topics**

2. a. Fiscal Year 2023 Popular Annual Financial Report (PAFR)
  - b. Audit Committee Survey Results Next Steps
  - c. Newly Updated Government Auditing Standards
    - i. Report Link
    - ii. Presentation Link
  - d. Policy Reviews Memorandum of Understanding
  - e. Proposal to expand transition audits to include departments in addition to elected offices
  - f. New Internal Audit Goals and Objectives
    - i. 2024 Goals and Objectives Crosswalk to 2011 Version
  - g. Fiscal Year 2025 Budget

## V. Internal Audit Report

- 3. a. Fair and Expo Center Cash Handling
  - i. Report Link
  - ii. Presentation Link
- b. Overtime / Compensatory Time
  - i. Report Link
  - ii. Presentation Link
- c. Follow Ups
  - i. Presentation
  - ii. 2023 Global Link Report
  - iii. Personal Information Data Privacy Link
  - iv. Finance / Tax Controls over Receipts Link
- d. Upcoming Audits
  - i. Internal Software Development
  - ii. Health Benefits Third Party Administrator

## VI. General Follow-Up and Department Updates

- 4. a. Internal Audit Status Report
- b. County Updates

c. Committee Information

VII. **Other Discussion Items**

VIII. **Closing & Adjourn**

5. Community Justice Tour for those who are interested



Deschutes County encourages persons with disabilities to participate in all programs and activities. To request this information in an alternate format please call (541) 617-4747.

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Office of the County Internal Auditor

# Audit Committee Survey Next Steps



Audit Committee Meeting | March 8, 2024

# Why Survey

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**Ensure a meaningful  
experience for  
committee  
members**

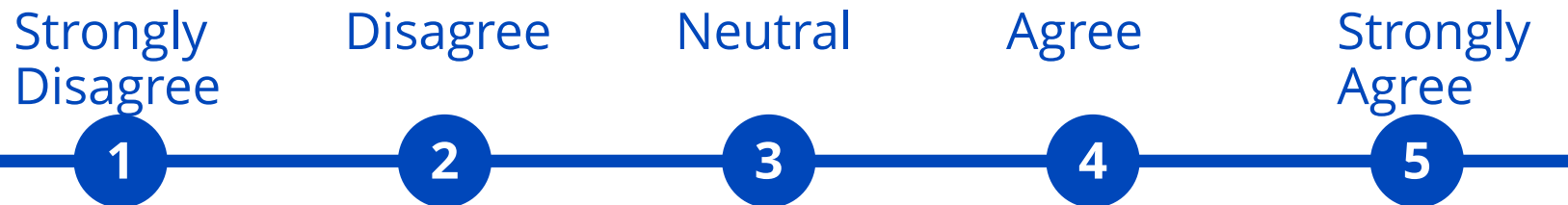
**Improve committee  
effectiveness**



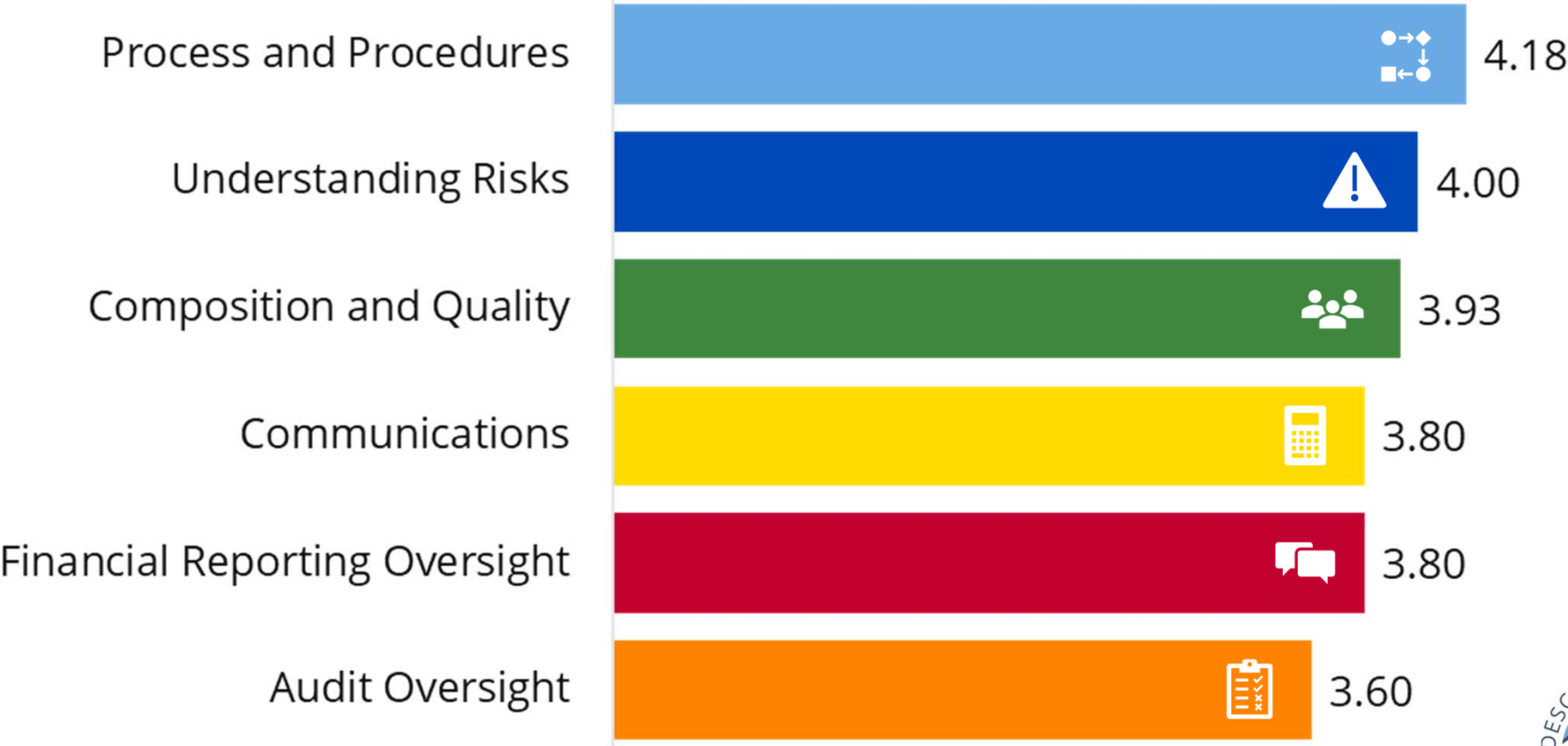
# Contents of Survey

**46** questions

-  **Process and procedures**
-  **Understanding risks**
-  **Composition and quality**
-  **Communication**
-  **Oversight of financial reporting**
-  **Oversight of audit functions**



# 2023 Strengths



# What should we change? Or Not?

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Processes

Understand  
Risk

Committee  
Composition

Improve  
Communication

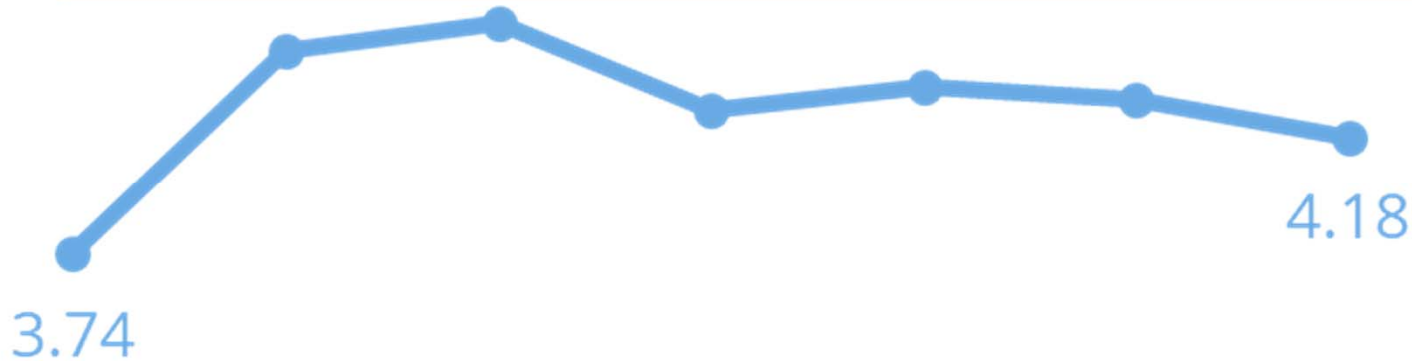
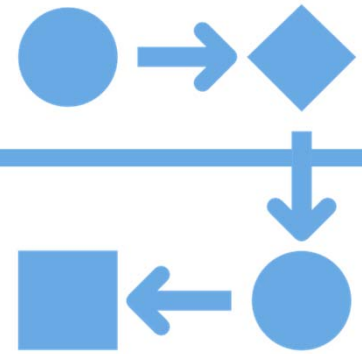
External Audit

Internal Audit





# Policies and Procedures



- Reports to Board of Commissioner
- Dedicated sufficient time and resources
- Develops a calendar
- Members can impact the agenda
- Encourages input on the agenda
- Agenda and materials distributed in advance
- At least quarterly meetings
- Promote open dialog

- Materials not too brief or detailed
- Committee responds appropriately



# Understanding Risks



Understands pressures that may impact quality of financial statements

Understands significant risks to County, including process to identify risk



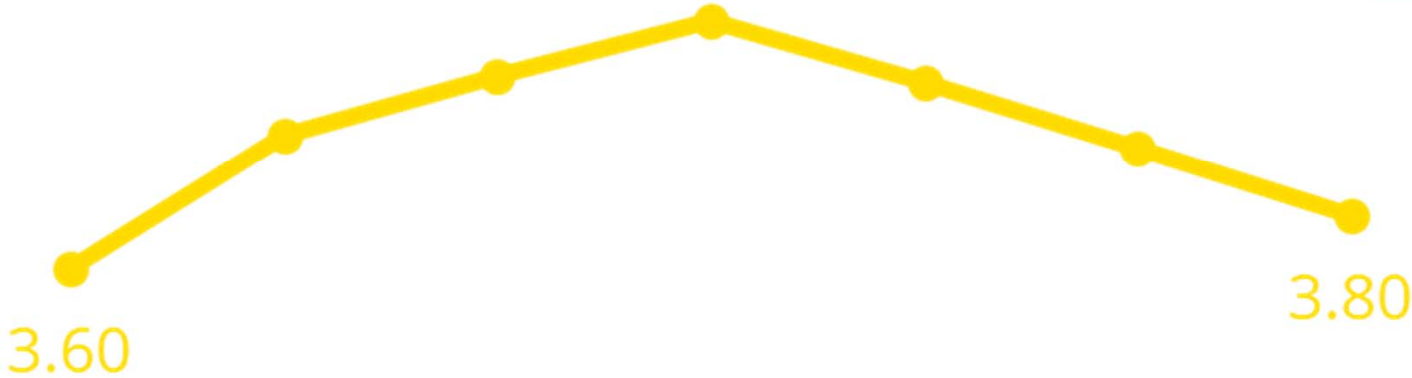
# Composition and Quality



- Nominations: variety of sources, consider qualifications
- Predefined qualifications, financial literacy
- Diversity of experience and backgrounds
- Qualities: integrity, credibility, knowledge, etc.
- Independent
- Reviews charter annually
- Continuing education
- New member orientation
- Successions plans



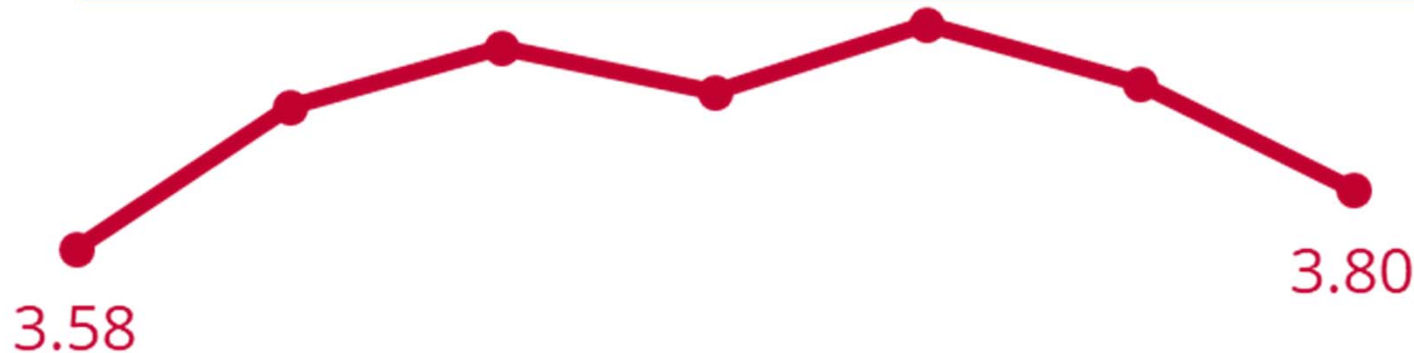
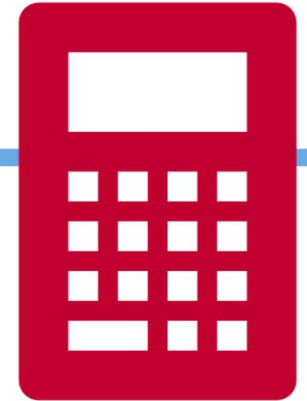
# Communication



- Committee sets “tone at the top”
- Member open lines of communication
- Cooperative relationship with management and auditors
- Receives timely information
- Made aware of alleged violations
- Periodically visit locations



# Oversight Financial Reporting



Considers quality, including disclosures

Process to review significant issues

Information to assess internal controls

Consulted when management seeks a second opinion

Reviews and understands accounting procedures

Asks about experience and sufficiency of finance and audit staff

Ensures recommendations are addressed

Reviews management action plans

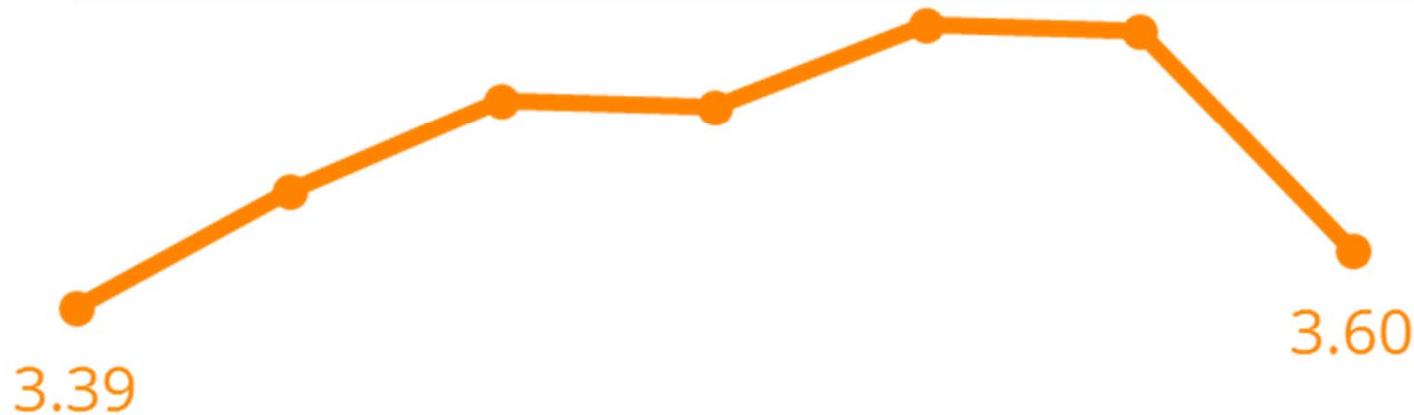
Ensures resolution

Reviews financial adjustments

Understand internal control testing



# Oversight Audit



- Understands external/internal coordination
- Reviews internal audit charter, budget, staffing, etc.
- Process to assess compliance and effectiveness
- Selection and oversight of external auditor
- Considers non-audit services in assessing external auditor independence
- Reviews management representation letters
- Reviews fees paid to external auditor



Office of the County Internal Auditor

# Government Auditing Standards

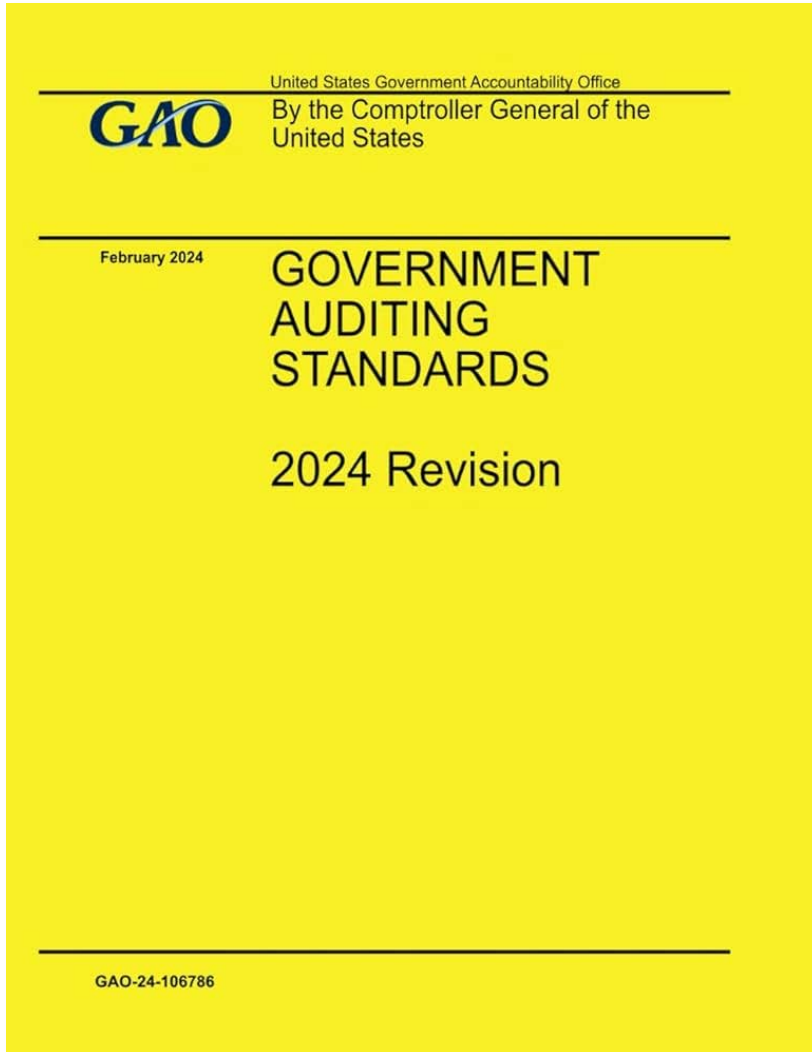
## 2024 Update



March 8, 2024

# Updated Government Auditing Standards

Item 2.



Released February 1, 2024

Implementation December 15, 2025

Includes:

Risk-based approach to quality management

Application guidance for financial audits





# Before: System of Quality Control



Annual independence and compliance statements



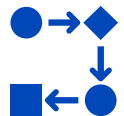
Procedures for adopting an audit plan



Minimum qualifications for staff



Procedures to document continuing professional education



Policies and procedures for conducting audits



Indexing report to evidence and second review



# Before: System of Quality Control



Engagement checklist for each audit



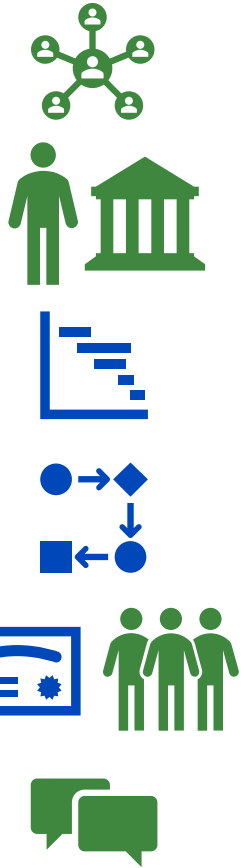
Review by County Internal Auditor annually



Outside peer review every three years



# New: Quality Management



Risk-based approach

Risks to these objectives

- Governance and leadership
- Independence, legal, and ethical requirements
- Acceptance, initiation, and continuance of engagements
- Engagement Performance
- Resources
- Information and communication

Design a system to mitigate for risks identified



# New: Engagement Quality Reviews

Staff not involved with the audit review

We haven't done this because we're both involved in all audits



# Next Steps

2024

1

**Risk Assessment**

2

**Design System of Quality Management**

2025

3

**Implement System**

4

**Review and Report**



# Any thoughts?

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By the Comptroller General of the  
United States

February 2024

# GOVERNMENT AUDITING STANDARDS

## 2024 Revision



By the Comptroller General of the  
United States

February 2024

# GOVERNMENT AUDITING STANDARDS

## 2024 Revision

The 2024 revision of *Government Auditing Standards* supersedes the 2018 Revision Technical Update April 2021 ([GAO-21-368G](#), April 2021).

The 2024 revision of *Government Auditing Standards* is effective for financial audits, attestation engagements, and reviews of financial statements for periods beginning on or after December 15, 2025, and for performance audits beginning on or after December 15, 2025. A system of quality management that complies with *Government Auditing Standards* is required to be designed and implemented by December 15, 2025. An audit organization should complete its evaluation of the system of quality management by December 15, 2026. Early implementation is permitted.



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## Abbreviations

AICPA	American Institute of Certified Public Accountants
AR-C	<i>AICPA Codification of Statements on Standards for Accounting and Review Services</i>
AT-C	<i>AICPA Codification of Statements on Standards for Attestation Engagements</i>
AU-C	<i>AICPA Codification of Statements on Auditing Standards</i>
CPA	certified public accountant
CPE	continuing professional education
GAGAS	generally accepted government auditing standards
IAASB	International Auditing and Assurance Standards Board
IT	information technology
OMB	Office of Management and Budget
PCAOB	Public Company Accounting Oversight Board
SAS	Statements on Auditing Standards
SSAE	Statements on Standards for Attestation Engagements

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Government auditing provides the objective analysis and information needed to help improve government performance and accountability for the benefit of the American people. The professional standards presented in *Government Auditing Standards* 2024 Revision provide a framework for performing high-quality audit work with competence, integrity, objectivity, and independence. Such performance provides accountability and helps improve government operations and services. These standards, commonly referred to as generally accepted government auditing standards (GAGAS), provide the foundation for government auditors to lead by example in the areas of independence, transparency, accountability, and quality through the audit process.

The 2024 revision of *Government Auditing Standards* contains major changes from, and supersedes, *Government Auditing Standards* 2018 Revision Technical Update April 2021. Chapter 5, “Quality Management, Engagement Quality Reviews, and Peer Review,” in the 2024 revision replaces chapter 5, “Quality Control and Peer Review,” in the 2018 revision. In addition, application guidance is added to chapter 6, “Standards for Financial Audits,” in this 2024 revision.

Enhancements that strengthen an audit organization’s framework for conducting high-quality government audits through its system of quality management are reflected in the 2024 revision of *Government Auditing Standards*. An effective system of quality management provides an audit organization with reasonable assurance that it and its personnel fulfill their responsibilities in accordance with professional standards and perform and report on engagements in accordance with such standards and requirements.

This revision emphasizes the responsibility of an audit organization’s leadership for proactively managing quality on its engagements and requires a quality management risk assessment process for designing, implementing, and operating its system of quality management. The 2024 revision also considers that the nature, extent, and formality of an audit organization’s system of quality management will vary based on its circumstances. These include its size, its number of offices and geographic dispersion, the knowledge and experience of its personnel, the nature and complexity of its engagement work, and cost-benefit considerations.

Other changes in this 2024 revision include the following:

- A change in approach from quality control to quality management.
- A flexible approach for an audit organization that is required to use both GAGAS quality management standards for GAGAS engagements and the quality management standards of other standard setters for non-GAGAS engagements. This approach will avoid the potential burden of an audit organization designing, implementing and operating two different systems of quality management.
- Promotion of proactive and effective monitoring activities and increased emphasis on tailoring monitoring activities. These will provide a sufficient basis for the audit organization's evaluation of the system of quality management.
- Provisions for the use of optional engagement quality reviews to address quality risks to achieving quality objectives.
- Application guidance on key audit matters for when this may apply to financial audits of government entities and entities that receive government financial assistance.

The 2024 revision of *Government Auditing Standards* has gone through an extensive deliberative process, including public comments and input from the Comptroller General's Advisory Council on Government Auditing Standards. The Advisory Council consists of experts in financial and performance auditing and reporting from federal, state, and local government; the private sector; and academia. The views of all parties were thoroughly considered in finalizing the standards.

*Government Auditing Standards* 2024 Revision is effective for financial audits, attestation engagements, and reviews of financial statements for periods beginning on or after December 15, 2025, and for performance audits beginning on or after December 15, 2025. A system of quality management that complies with *Government Auditing Standards* is required to be designed and implemented by December 15, 2025. An audit organization should complete its evaluation of the system of quality management by December 15, 2026. Early implementation is permitted.

An electronic version of this document can be accessed at <https://www.gao.gov/yellowbook>.



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I extend special thanks to the members of the Advisory Council for their extensive input and feedback throughout the process of developing and finalizing the standards.

A handwritten signature in black ink that reads "Gene L. Dodaro". The signature is written in a cursive style with a large, prominent "D" at the end.

Gene L. Dodaro  
Comptroller General  
of the United States

# Chapter 1: Foundation and Principles for the Use and Application of Government Auditing Standards

**1.01** This chapter provides guidance for engagements conducted in accordance with generally accepted government auditing standards (GAGAS). This chapter also

- a. explains the types of auditors and audit organizations that may employ GAGAS to conduct their work,
- b. identifies the types of engagements that may be conducted in accordance with GAGAS, and
- c. explains terminology that is commonly used in GAGAS.

## Introduction

**1.02** The concept of accountability for use of public resources and government authority is key to our nation's governing processes. Management and officials entrusted with public resources are responsible for carrying out public functions and providing service to the public effectively, efficiently, economically, ethically, and equitably within the context of the statutory boundaries of the specific government program.

**1.03** As reflected in applicable laws, regulations, agreements, and standards, management and officials of government programs are responsible for providing reliable, useful, and timely information for transparency and accountability of these programs and their operations. Legislators, oversight bodies, those charged with governance, and the public need to know whether (1) management and officials manage government resources and use their authority properly and in compliance with laws and regulations; (2) government programs are achieving their objectives and desired outcomes; and (3) government services are provided effectively, efficiently, economically, ethically, and equitably.

**1.04** "Those charged with governance" refers to the individuals responsible for overseeing 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. Those charged with governance may also be part of the entity's management. In some audited 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 engagement.

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**Chapter 1: Foundation and Principles for the  
Use and Application of Government Auditing  
Standards**

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**1.05** Government auditing is essential in providing accountability to legislators, oversight bodies, those charged with governance, and the public. GAGAS engagements provide an independent, objective, nonpartisan assessment of the stewardship, performance, or cost of government policies, programs, or operations, depending upon the type and scope of the engagement.

**1.06** The professional standards and guidance contained in this document provide a framework for conducting high-quality engagements with competence, integrity, objectivity, and independence. Auditors of government entities, entities that receive government awards, and other entities, as required by law or regulation or as they elect, may use these standards. Overall, GAGAS contains standards for engagements comprising individual requirements that are identified by terminology as discussed in paragraphs 2.02 through 2.10. GAGAS contains requirements and guidance dealing with ethics, independence, auditors' professional judgment and competence, quality management, peer review, conducting the engagement, and reporting.

**1.07** Engagements conducted in accordance with GAGAS provide information used for oversight, accountability, transparency, and improvements of government programs and operations. GAGAS contains requirements and guidance to assist auditors in objectively obtaining and evaluating sufficient, appropriate evidence and reporting the results. When auditors conduct their work in this manner and comply with GAGAS in reporting the results, their work can lead to improved government management, better decision making and oversight, effective and efficient operations, and accountability and transparency for resources and results.

**1.08** Laws, regulations, contracts, grant agreements, and policies frequently require that engagements be conducted in accordance with GAGAS. In addition, many auditors and audit organizations voluntarily choose to conduct their work in accordance with GAGAS. The requirements and guidance in GAGAS in totality apply to engagements pertaining to government entities, programs, activities, and functions, and to government assistance administered by contractors, nonprofit entities, and other nongovernmental entities when the use of GAGAS is required or voluntarily adopted.

**1.09** The following are some of the laws, regulations, and other authoritative sources that require the use of GAGAS:

**Chapter 1: Foundation and Principles for the  
Use and Application of Government Auditing  
Standards**

- a. The Inspector General Act of 1978, as amended (5 U.S.C. App.), requires that the federal inspectors general appointed under that act 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 major executive branch departments' and agencies' financial statements. The Accountability of Tax Dollars Act of 2002 (Public Law 107-289) generally extends this requirement to most executive agencies not subject to the Chief Financial Officers Act.
- c. The Single Audit Act Amendments of 1996 (Public Law 104-156) requires that GAGAS be followed in audits of state and local governments and nonprofit entities that receive federal awards. Subpart F of OMB's *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (2 C.F.R. part 200), which provides the government-wide guidelines and policies on conducting audits to comply with the Single Audit Act, reiterates the requirement to use GAGAS.

**1.10** Other laws, regulations, or authoritative sources may require the use of GAGAS. For example, auditors at the state and local government levels 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. Being aware of such other laws, regulations, or authoritative sources may assist auditors in performing their work in accordance with the required standards.

**1.11** Even if not required to do so, auditors may find it useful to follow GAGAS in conducting engagements pertaining to federal, state, and local government programs as well as engagements pertaining to state and local government awards that contractors, nonprofit entities, and other nongovernmental entities administer. Though not formally required to do so, many audit organizations, both in the United States and in other countries, voluntarily follow GAGAS.

## Types of GAGAS Users

1.12 GAGAS provides standards that are used by a wide range of auditors and audit organizations that audit government entities, entities that receive government awards, and other entities. These auditors and audit organizations may also be subject to additional requirements unique to their environments. Examples of the various types of users who may be required or may elect to use GAGAS include the following:

- a. Contract auditors: audit organizations that specialize in conducting engagements pertaining to government acquisitions and contract administration
- b. Certified public accounting firms: public accounting organizations in the private sector that provide audit, attestation, or review services under contract to government entities or recipients of government funds
- c. Federal inspectors general: government audit organizations within federal agencies that conduct engagements and investigations relating to the programs and operations of their agencies and issue reports both to agency management and to third parties external to the audited entity
- d. Federal agency internal auditors: internal government audit organizations associated with federal agencies that conduct engagements and investigations relating to the programs and operations of their agencies
- e. Municipal auditors: elected or appointed officials in government audit organizations in the United States at the city, county, and other local government levels
- f. State auditors: elected or appointed officials in audit organizations in the governments of the 50 states, the District of Columbia, and the U.S. territories
- g. Supreme audit institutions: national government audit organizations, in the United States or elsewhere, typically headed by a comptroller general or auditor general

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## Types of GAGAS Engagements

**1.13** This section describes the types of engagements that audit organizations may conduct in accordance with GAGAS. This description is not intended to limit or require the types of engagements that may be conducted in accordance with GAGAS.

**1.14** All GAGAS engagements begin with objectives, and those objectives determine the type of engagement to be conducted and the applicable standards to be followed. This document classifies financial audits, attestation engagements, reviews of financial statements, and performance audits, as defined by their objectives, as the types of engagements that are covered by GAGAS.

**1.15** In some GAGAS engagements, the standards applicable to the specific objective will be apparent. For example, if the objective is to express an opinion on financial statements, the standards for financial audits apply. However, some engagements may have objectives that could be met using more than one approach. For example, if the objective is to determine the reliability of performance measures, auditors can perform this work in accordance with either the standards for attestation engagements or performance audits.

**1.16** GAGAS requirements and guidance apply to the types of engagements that auditors may conduct in accordance with GAGAS as follows:

- a. Financial audits: the requirements and guidance in chapters 1 through 6 apply.
- b. Attestation-level examination, review, and agreed-upon procedures engagements and reviews of financial statements: the requirements and guidance in chapters 1 through 5 and 7 apply.
- c. Performance audits: the requirements and guidance in chapters 1 through 5, 8, and 9 apply.

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## Financial Audits

**1.17** Financial audits provide independent assessments of whether entities' reported financial information (e.g., financial condition, results, and use of resources) is presented fairly, in all material respects, in accordance with recognized criteria. Financial audits conducted in accordance with GAGAS include financial statement audits and other related financial audits.

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**Chapter 1: Foundation and Principles for the  
Use and Application of Government Auditing  
Standards**

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- a. Financial statement audits: The primary purpose of a financial statement audit is to provide financial statement users with an opinion by an auditor on whether an entity's financial statements are presented fairly, in all material respects, in accordance with an applicable financial reporting framework. Reporting on financial statement audits conducted in accordance with GAGAS also includes reports on internal control over financial reporting and on compliance with provisions of laws, regulations, contracts, and grant agreements that have a material effect on the financial statements.
- b. Other types of financial audits: Other types of financial audits conducted in accordance with GAGAS entail various scopes of work, including
  - (1) obtaining sufficient, appropriate evidence to form an opinion on a single financial statement or specified elements, accounts, or line items of a financial statement;<sup>1</sup>
  - (2) issuing letters (commonly referred to as comfort letters) for underwriters and certain other requesting parties;<sup>2</sup>
  - (3) auditing applicable compliance and internal control requirements relating to one or more government programs;<sup>3</sup> and
  - (4) conducting an audit of internal control over financial reporting that is integrated with an audit of financial statements (integrated audit).<sup>4</sup>

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<sup>1</sup>See AU-C section 805, *Special Considerations – Audits of Single Financial Statements and Specific Elements, Accounts, or Items of a Financial Statement* (AICPA, Professional Standards).

<sup>2</sup>See AU-C section 920, *Letters for Underwriters and Certain Other Requesting Parties* (AICPA, Professional Standards).

<sup>3</sup>See AU-C section 935, *Compliance Audits* (AICPA, Professional Standards).

<sup>4</sup>See AU-C section 940, *An Audit of Internal Control Over Financial Reporting That Is Integrated With an Audit of Financial Statements* (AICPA, Professional Standards).

## Attestation Engagements and Reviews of Financial Statements

**1.18** Attestation engagements can cover a broad range of financial or nonfinancial objectives about the subject matter or assertion depending on the users' needs. In an attestation engagement, the subject matter or an assertion by a party other than the auditors is measured or evaluated in accordance with suitable criteria. The work the auditors perform and the level of assurance associated with the report vary based on the type of attestation engagement. The three types of attestation engagements are as follows:

- a. **Examination:** An auditor obtains reasonable assurance by obtaining sufficient, appropriate evidence about the measurement or evaluation of subject matter against criteria in order to be able to draw reasonable conclusions on which to base the auditor's opinion about whether the subject matter is in accordance with (or based on) the criteria or the assertion is fairly stated, in all material respects. The auditor obtains the same level of assurance in an examination as in a financial statement audit.
- b. **Review:** An auditor obtains limited assurance by obtaining sufficient, appropriate review evidence about the measurement or evaluation of subject matter against criteria in order to express a conclusion about whether any material modification should be made to the subject matter in order for it to be in accordance with (or based on) the criteria or to the assertion in order for it to be fairly stated. Review-level work does not include reporting on internal control or compliance with provisions of laws, regulations, contracts, and grant agreements. The auditor obtains the same level of assurance in a review engagement as in a review of financial statements.
- c. **Agreed-upon procedures engagement:** An auditor performs specific procedures on subject matter or an assertion and reports the findings without providing an opinion or a conclusion on it. The specified parties to the engagement agree upon and are responsible for the sufficiency of the procedures for their purposes. The specified parties are the intended users to whom use of the report is limited.

**1.19** The subject matter of an attestation engagement may take many forms, including the following:



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- a. historical or prospective performance or condition, historical or prospective financial information, performance measurements, or backlog data;
  - b. physical characteristics, for example, narrative descriptions or square footage of facilities;
  - c. historical events, for example, the price of a market basket of goods on a certain date;
  - d. analyses, for example, break-even analyses;
  - e. systems and processes, for example, internal control; and
  - f. behavior, for example, corporate governance, compliance with laws and regulations, and human resource practices.

**1.20** The objective of the auditor when performing a review of financial statements is to obtain limited assurance as a basis for reporting whether the auditor is aware of any material modifications that should be made to financial statements in order for the financial statements to be in accordance with the applicable financial reporting framework. A review of financial statements does not include obtaining an understanding of the entity's internal control, assessing fraud risk, or certain other procedures ordinarily performed in an audit.

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## Performance Audits

**1.21** Performance audits provide objective analysis, findings, and conclusions to assist management and those charged with governance and oversight with, among other things, improving program performance and operations, reducing costs, facilitating decision making by parties responsible for overseeing or initiating corrective action, and contributing to public accountability.

**1.22** Performance audit objectives vary widely and include assessments of program effectiveness, economy, and efficiency; internal control; compliance; and prospective analyses. Audit objectives may also pertain to the current status or condition of a program. These overall objectives are not mutually exclusive. For example, a performance audit with an objective of determining or evaluating program effectiveness may also involve an additional objective of evaluating the program's internal controls. Key categories of performance audit objectives include the following:

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- a.** Program effectiveness and results audit objectives. These are frequently interrelated with economy and efficiency objectives. Audit objectives that focus on program effectiveness and results typically measure the extent to which a program is achieving its goals and objectives. Audit objectives that focus on economy and efficiency address the costs and resources used to achieve program results.
- b.** Internal control audit objectives. These relate to an assessment of one or more aspects of an entity's system of internal control that is designed to provide reasonable assurance of achieving effective and efficient operations, reliability of reporting for internal and external use, or compliance with provisions of applicable laws and regulations. Internal control objectives also may be relevant when determining the cause of unsatisfactory program performance. Internal control is a process effected by an entity's oversight body, management, and other personnel that provides reasonable assurance that the objectives of an entity will be achieved. Internal control comprises the plans, methods, policies, and procedures used to fulfill the mission, strategic plan, goals, and objectives of the entity.
- c.** Compliance audit objectives. These relate to an assessment of compliance with criteria established by provisions of laws, regulations, contracts, and grant agreements, or other requirements that could affect the acquisition, protection, use, and disposition of the entity's resources and the quantity, quality, timeliness, and cost of services the entity produces and delivers. Compliance requirements can be either financial or nonfinancial.
- d.** Prospective analysis audit objectives. These provide analysis or conclusions about information that is based on assumptions about events that may occur in the future, along with possible actions that the entity may take in response to the future events.

**1.23** Examples of program effectiveness and results audit objectives include

- a.** assessing the extent to which legislative, regulatory, or organizational goals and objectives are being achieved;

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- b.** assessing the relative ability of alternative approaches to yield better program performance or eliminate factors that inhibit program effectiveness;
- c.** analyzing the relative cost-effectiveness of a program or activity, focusing on combining cost information or other inputs with (1) information about outputs or the benefit provided or (2) outcomes or the results achieved;
- d.** determining whether a program produced intended results or produced results that were not consistent with the program's objectives;
- e.** determining the current status or condition of program operations or progress in implementing legislative requirements;
- f.** determining whether a program provides equitable access to or distribution of public resources within the context of statutory parameters;
- g.** assessing the extent to which programs duplicate, overlap, or conflict with other related programs;
- h.** evaluating whether the entity is following sound procurement practices;
- i.** assessing the reliability, validity, or relevance of performance measures concerning program effectiveness and results or economy and efficiency;
- j.** assessing the reliability, validity, or relevance of financial information related to the performance of a program;
- k.** determining whether government resources (inputs) are obtained at reasonable costs while meeting timeliness and quality considerations;
- l.** determining whether appropriate value was obtained based on the cost or amount paid or based on the amount of revenue received;
- m.** determining whether government services and benefits are accessible to those individuals who have a right to access those services and benefits;

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- n. determining whether fees assessed cover costs;
- o. determining whether and how the program's unit costs can be decreased or its productivity increased; and
- p. assessing the reliability, validity, or relevance of budget proposals or budget requests to assist legislatures in the budget process.

**1.24** Examples of internal control audit objectives include determining whether

- a. organizational missions, goals, and objectives are achieved effectively and efficiently;
- b. resources are used in compliance with laws, regulations, or other requirements;
- c. resources, including sensitive information accessed or stored outside the organization's physical perimeter, are safeguarded against unauthorized acquisition, use, or disposition;
- d. management information, such as performance measures, and public reports are complete, accurate, and consistent to support performance and decision making;
- e. the integrity of information from computerized systems is achieved; and
- f. contingency planning for information systems provides essential backup to prevent unwarranted disruption of the activities and functions that the systems support.

**1.25** Examples of compliance objectives include determining whether

- a. the purpose of the program, the manner in which it is to be conducted, the services delivered, the outcomes, or the population it serves is in compliance with provisions of laws, regulations, contracts, or grant agreements or other requirements;
- b. government services and benefits are distributed or delivered to citizens based on eligibility to obtain those services and benefits;

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- c. incurred or proposed costs are in compliance with applicable laws, regulations, contracts, or grant agreements; and
  - d. revenues received are in compliance with applicable laws, regulations, contracts, or grant agreements.

**1.26** Examples of prospective analysis objectives include providing conclusions based on

- a. current and projected trends and future potential impact on government programs and services and their implications for program or policy alternatives;
- b. program or policy alternatives, including forecasting program outcomes under various assumptions;
- c. policy or legislative proposals, including advantages, disadvantages, and analysis of stakeholder views;
- d. prospective information prepared by management;
- e. budgets and forecasts that are based on (1) assumptions about expected future events and (2) stakeholders' and management's expected reaction to those future events; and
- f. management's assumptions on which prospective information is based.

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## Terms Used in GAGAS

**1.27** This paragraph describes certain terms used in GAGAS. When terminology differs from that used at an organization subject to GAGAS, auditors use professional judgment to determine if there is an equivalent term.<sup>5</sup>

- a. **Attestation engagement:** An examination, review, or agreed-upon procedures engagement conducted under the GAGAS attestation standards related to subject matter or an assertion that is the responsibility of another party.

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<sup>5</sup>See the Glossary for an expanded list of terms used in GAGAS.

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- b.** Audit: Either a financial audit or performance audit conducted in accordance with GAGAS.
- c.** Audit organization: A government audit entity or a public accounting firm or other audit entity that conducts GAGAS engagements.
- d.** Audit report: A report issued as a result of a financial audit, attestation engagement, review of financial statements, or performance audit conducted in accordance with GAGAS.
- e.** Audited entity: The entity that is subject to a GAGAS engagement, whether that engagement is a financial audit, attestation engagement, review of financial statements, or performance audit.
- f.** Auditor: An individual assigned to planning, directing, performing engagement procedures, or reporting on GAGAS engagements (including work on audits, attestation engagements, and reviews of financial statements) regardless of job title. Therefore, individuals who may have the title auditor, information technology auditor, analyst, practitioner, evaluator, inspector, or other similar titles are considered auditors under GAGAS.
- g.** Control objective: The aim or purpose of specified controls; control objectives address the risks related to achieving an entity's objectives.
- h.** Engagement: A financial audit, attestation engagement, review of financial statements, or performance audit conducted in accordance with GAGAS.
- i.** Engagement team (or audit team): Auditors assigned to planning, directing, performing engagement procedures, or reporting on GAGAS engagements.
- j.** Engaging party: The party that engages the auditor to conduct the GAGAS engagement.
- k.** Entity objective: What an entity wants to achieve; entity objectives are intended to meet the entity's mission, strategic plan, and goals and the requirements of applicable laws and regulations.

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- l.** External audit organization: An audit organization that issues reports to third parties external to the audited entity, either exclusively or in addition to issuing reports to senior management and those charged with governance of the audited entity.
- m.** Internal audit organization: An audit organization that is accountable to senior management and those charged with governance of the audited entity and that does not generally issue reports to third parties external to the audited entity.
- n.** Responsible party: The party responsible for a GAGAS engagement's subject matter.
- o.** Review of financial statements: An engagement conducted under GAGAS for review of financial statements.
- p.** Specialist: An individual or organization possessing special skill or knowledge in a particular field other than accounting or auditing that assists auditors in conducting engagements. A specialist may be either an internal specialist or an external specialist.

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## The GAGAS Format

**1.28** GAGAS uses a format designed to allow auditors to quickly identify requirements and application guidance related to those requirements. GAGAS requirements are differentiated from application guidance by borders surrounding the text. The requirements are followed immediately by application guidance that relates directly to the preceding requirements. The auditors' responsibilities related to requirements and application guidance are discussed in paragraphs 2.02 through 2.10.

# Chapter 2: General Requirements for Complying with Government Auditing Standards

**2.01** This chapter establishes general requirements for complying with generally accepted government auditing standards (GAGAS) that are applicable to all GAGAS engagements. The information it contains relates to how auditors conducting GAGAS engagements identify and apply the requirements contained in GAGAS. The chapter also contains requirements for using other audit standards in conjunction with GAGAS and for reporting compliance with GAGAS in the audit report.

## Complying with GAGAS

### Requirements: Complying with GAGAS

**2.02** GAGAS uses two categories of requirements, identified by specific terms, to describe the degree of responsibility they impose on auditors and audit organizations:

- a. **Unconditional requirements:** Auditors and audit organizations must comply with an unconditional requirement in all cases where such requirement is relevant. GAGAS uses *must* to indicate an unconditional requirement.
- b. **Presumptively mandatory requirements:** Auditors and audit organizations must comply with a presumptively mandatory requirement in all cases where such a requirement is relevant except in rare circumstances discussed in paragraphs 2.03, 2.04, and 2.08. GAGAS uses *should* to indicate a presumptively mandatory requirement.<sup>6</sup>

**2.03** In rare circumstances, auditors and audit organizations may determine it necessary to depart from a relevant presumptively mandatory requirement. In such rare circumstances, auditors should perform alternative procedures to achieve the intent of that requirement.

**2.04** If, in rare circumstances, auditors judge it necessary to depart from a relevant presumptively mandatory requirement, they must document their justification for the departure and how the alternative

<sup>6</sup>See para. 2.19 for additional documentation requirements for departures from GAGAS requirements.



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procedures performed in the circumstances were sufficient to achieve the intent of that requirement.

**2.05** Auditors should have an understanding of the entire text of applicable chapters of GAGAS, including application guidance, and any amendments that GAO issued, to understand the intent of the requirements and to apply the requirements properly.<sup>7</sup>

**2.06** Auditors should consider applicable GAO-issued GAGAS interpretive guidance in conducting and reporting on GAGAS engagements.<sup>8</sup>

**Application Guidance: Complying with GAGAS**

**2.07** GAGAS contains requirements together with related explanatory material in the form of application guidance. Not every paragraph of GAGAS carries a requirement. Rather, GAGAS identifies the requirements through use of specific language. GAGAS also contains introductory material that provides context relevant to a proper understanding of a GAGAS chapter or section. Having an understanding of the entire text of applicable GAGAS includes an understanding of any financial audit, attestation, and reviews of financial statement standards incorporated by reference.<sup>9</sup>

**2.08** The need for auditors to depart from a relevant presumptively mandatory requirement is expected to arise only when the requirement is for a specific procedure to be performed and, in the specific circumstances of the engagement, that procedure would be ineffective in achieving the intent of the requirement.

**2.09** The application guidance provides further explanation of the requirements and guidance for applying them. In particular, it may explain more precisely what a requirement means or is intended to address or include examples of procedures that may be appropriate in the circumstances. Although such guidance does not in itself impose a

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<sup>7</sup>See <https://www.gao.gov/yellowbook> for GAGAS amendments.

<sup>8</sup>See <https://www.gao.gov/yellowbook> for GAGAS interpretive guidance.

<sup>9</sup>See paras. 2.13, 6.01, and 7.01 for discussion of standards incorporated by reference.

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requirement, it is relevant to the proper application of the requirements. “May,” “might,” and “could” are used to describe these actions and procedures. The application guidance may also provide background information on matters addressed in GAGAS.

**2.10** Interpretive guidance is not auditing standards. Interpretive guidance provides guidance on the application of GAGAS and recommendations on the application of GAGAS in specific circumstances.

## Relationship between GAGAS and Other Professional Standards

### **Requirement: Relationship between GAGAS and Other Professional Standards**

**2.11** When auditors cite compliance with both GAGAS and another set of standards, such as those listed in paragraphs 2.13, 2.15, 6.01, and 7.01, auditors should refer to paragraph 2.17 for the requirements for citing compliance with GAGAS. In addition to citing GAGAS, auditors may also cite the use of other standards in their reports when they have also met the requirements for citing compliance with the other standards. Auditors should refer to the other set of standards for the basis for citing compliance with those standards.

### **Application Guidance: Relationship between GAGAS and Other Professional Standards**

**2.12** Auditors may use GAGAS in conjunction with professional standards issued by other authoritative bodies.

**2.13** The relationship between GAGAS and other professional standards for financial audits, attestation engagements, and reviews of financial statements is as follows:

- a. The American Institute of Certified Public Accountants (AICPA) has established professional standards that apply to financial audits, attestation engagements, and reviews of financial statements for nonissuers (entities other than issuers under the Sarbanes-Oxley Act of 2002,<sup>10</sup> such as privately held companies,

<sup>10</sup>See the Sarbanes-Oxley Act of 2002 (Public Law 107-204) for a discussion of issuers (generally, publicly traded companies with a reporting obligation under the Securities Exchange Act of 1934).

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nonprofit entities, and government entities) conducted by certified public accountants (CPA). For financial audits and attestation engagements, GAGAS incorporates by reference AICPA Statements on Auditing Standards and Statements on Standards for Attestation Engagements.<sup>11</sup> For reviews of financial statements, GAGAS incorporates by reference AR-C, section 90, *Review of Financial Statements*.<sup>12</sup>

- b.** The International Auditing and Assurance Standards Board (IAASB) has established professional standards that apply to financial audits and assurance engagements. Auditors may elect to use the IAASB standards and the related International Standards on Auditing and International Standards on Assurance Engagements in conjunction with GAGAS.
- c.** The Public Company Accounting Oversight Board (PCAOB) has established professional standards that apply to financial audits and attestation engagements for issuers. Auditors may elect to use the PCAOB standards in conjunction with GAGAS.

**2.14** For financial audits, attestation engagements, and reviews of financial statements, GAGAS does not incorporate the AICPA Code of Professional Conduct by reference, but recognizes that certain CPAs may use or may be required to use the code in conjunction with GAGAS.

**2.15** For performance audits, GAGAS does not incorporate other standards by reference, but recognizes that auditors may use or may be required to use other professional standards in conjunction with GAGAS, such as the following:

- a.** *International Standards for the Professional Practice of Internal Auditing*, Institute of Internal Auditors, Inc.;
- b.** *International Standards of Supreme Audit Institutions*, International Organization of Supreme Audit Institutions;
- c.** *Guiding Principles for Evaluators*, American Evaluation Association;

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<sup>11</sup>AICPA, *Professional Standards*.

<sup>12</sup>AICPA, *Professional Standards*.

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- d. *The Program Evaluation Standards*, Joint Committee on Standards for Education Evaluation;
- e. *Standards for Educational and Psychological Testing*, American Psychological Association; and
- f. *IT Standards, Guidelines, and Tools and Techniques for Audit and Assurance and Control Professionals*, Information Systems Audit and Control Association.

## Stating Compliance with GAGAS in the Audit Report

### **Requirements: Stating Compliance with GAGAS in the Audit Report**

**2.16** When auditors are required to conduct an engagement in accordance with GAGAS or are representing to others that they did so, they should cite compliance with GAGAS in the audit report as set forth in paragraphs 2.17 through 2.19.

**2.17** Auditors should include one of the following types of GAGAS compliance statements in reports on GAGAS engagements, as appropriate.

- a. Unmodified GAGAS compliance statement: Stating that the auditors conducted the engagement in accordance with GAGAS. Auditors should include an unmodified GAGAS compliance statement in the audit report when they have (1) followed unconditional and applicable presumptively mandatory GAGAS requirements or (2) followed unconditional requirements, documented justification for any departures from applicable presumptively mandatory requirements, and achieved the objectives of those requirements through other means.
- b. Modified GAGAS compliance statement: Stating either that
  - (1) the auditors conducted the engagement in accordance with GAGAS, except for specific applicable requirements that were not followed, or
  - (2) because of the significance of the departure(s) from the

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requirements, the auditors were unable to and did not conduct the engagement in accordance with GAGAS.

**2.18** When auditors use a modified GAGAS statement, they should disclose in the report the applicable requirement(s) not followed, the reasons for not following the requirement(s), and how not following the requirement(s) affected or could have affected the engagement and the assurance provided.

**2.19** When auditors do not comply with applicable requirement(s), they should (1) assess the significance of the noncompliance to the engagement objectives; (2) document the assessment, along with their reasons for not following the requirement(s); and (3) determine the type of GAGAS compliance statement.

**Application Guidance: Stating Compliance with GAGAS in the Audit Report**

**2.20** Situations for using modified compliance statements include scope limitations, such as restrictions on access to records, government officials, or other individuals needed to conduct the engagement.

**2.21** The auditors' determination of noncompliance with applicable requirements is a matter of professional judgment, which is affected by the significance of the requirement(s) not followed in relation to the engagement objectives.

**2.22** Determining whether an unmodified or modified GAGAS compliance statement is appropriate is based on the consideration of the individual and aggregate effect of the instances of noncompliance with GAGAS requirements. Factors that the auditor may consider include

- a. the pervasiveness of the instance(s) of noncompliance;
- b. the potential effect of the instance(s) of noncompliance on the sufficiency and appropriateness of evidence supporting the findings, conclusions, and recommendations; and
- c. whether report users might misunderstand the implications of a modified or unmodified GAGAS compliance statement.

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**2.23** If an audit report is issued in situations described in paragraph 3.60 (except in circumstances discussed in paragraphs 3.25 or 3.84), a modified GAGAS compliance statement as discussed in paragraph 2.17b(2) is used.

# Chapter 3: Ethics, Independence, and Professional Judgment

**3.01** The first section of this chapter sets forth fundamental ethical principles for auditors in the government environment. The second section establishes independence standards and provides guidance on this topic for auditors conducting financial audits, attestation engagements, reviews of financial statements, and performance audits under generally accepted government auditing standards (GAGAS). This section emphasizes the importance of independence of the auditor and the audit organization. The third section establishes the standard for the auditor's use of professional judgment and provides related application guidance. The requirements of this chapter are intended to be followed in conjunction with all other applicable GAGAS requirements.

## Ethical Principles

**3.02** The ethical principles presented in this section provide the foundation, discipline, and structure, as well as the environment, that influence the application of GAGAS.<sup>13</sup>

**3.03** Because auditing is essential to government accountability to the public, the public expects audit organizations and auditors who perform their work in accordance with GAGAS to follow ethical principles. Management of the audit organization sets the tone for ethical behavior throughout the organization by maintaining an ethical culture, clearly communicating acceptable behavior and expectations to each employee, and creating an environment that reinforces and encourages ethical behavior throughout all levels of the organization. The ethical tone maintained and demonstrated by management and personnel is an essential element of a positive ethical environment for the audit organization.

**3.04** Performing audit work in accordance with ethical principles is a matter of personal and organizational responsibility. Ethical principles apply in preserving auditor independence,<sup>14</sup> taking on only work that the audit organization is competent to perform,<sup>15</sup> performing high-quality work, and following the applicable standards cited in the audit report. Integrity and objectivity are maintained when auditors perform their work

<sup>13</sup>See paras. 5.47 and 5.48 for a discussion of independence, legal, and ethical requirements in an audit organization's system of quality management.

<sup>14</sup>See paras. 3.18 through 3.108 for independence requirements and guidance.

<sup>15</sup>See paras. 4.02 through 4.15 for additional information on competence.

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and make decisions that are consistent with the broader interest of those relying on the audit report, including the public.

**3.05** Other ethical requirements or codes of professional conduct may also be applicable to auditors who conduct engagements in accordance with GAGAS. For example, individual auditors who are members of professional organizations or are licensed or certified professionals may also be subject to ethical requirements of those professional organizations or licensing bodies. Auditors employed by government entities may also be subject to government ethics laws and regulations.

**3.06** The ethical principles that guide the work of auditors who conduct engagements in accordance with GAGAS are

- a. the public interest;
- b. integrity;
- c. objectivity;
- d. proper use of government information, resources, and positions;  
and
- e. professional behavior.

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## The Public Interest

**3.07** The public interest is defined as the collective well-being of the community of people and entities that the auditors serve. Observing integrity, objectivity, and independence in discharging their professional responsibilities helps auditors serve the public interest and honor the public trust. The principle of the public interest is fundamental to the responsibilities of auditors and critical in the government environment.

**3.08** A distinguishing mark of an auditor is acceptance of responsibility to serve the public interest. This responsibility is critical when auditing in the government environment. GAGAS embodies the concept of accountability for public resources, which is fundamental to serving the public interest.

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## Integrity

**3.09** Public confidence in government is maintained and strengthened by auditors performing their professional responsibilities with integrity. Integrity includes auditors performing their work with an attitude that is objective, fact-based, nonpartisan, and nonideological with regard to



**Chapter 3: Ethics, Independence, and Professional Judgment**

audited entities and users of the audit reports. Within the constraints of applicable confidentiality laws, regulations, or policies, communications with the audited entity, those charged with governance, and the individuals contracting for or requesting the engagement are expected to be honest, candid, and constructive.

**3.10** Making decisions consistent with the public interest of the program or activity under audit is an important part of the principle of integrity. In discharging their professional responsibilities, auditors may encounter conflicting pressures from management of the audited entity, various levels of government, and other likely users. Auditors may also encounter pressures to inappropriately achieve personal or organizational gain. In resolving those conflicts and pressures, acting with integrity means that auditors place priority on their responsibilities to the public interest.

**Objectivity**

**3.11** Auditors' objectivity in discharging their professional responsibilities is the basis for the credibility of auditing in the government sector. Objectivity includes independence of mind and appearance when conducting engagements, maintaining an attitude of impartiality, having intellectual honesty, and being free of conflicts of interest. Maintaining objectivity includes a continuing assessment of relationships with audited entities and other stakeholders in the context of the auditors' responsibility to the public. The concepts of objectivity and independence are closely related. Independence impairments affect auditors' objectivity.<sup>16</sup>

**Proper Use of Government Information, Resources, and Positions**

**3.12** Government information, resources, and positions are to be used for official purposes and not inappropriately for the auditors' personal gain or in a manner contrary to law or detrimental to the legitimate interests of the audited entity or the audit organization. This concept includes the proper handling of sensitive or classified information or resources.

**3.13** In the government environment, the public's right to the transparency of government information has to be balanced with the proper use of that information. In addition, many government programs are subject to laws and regulations dealing with the disclosure of information. Exercising discretion in using information acquired in the course of auditors' duties is

<sup>16</sup>See paras. 3.18 through 3.108 for independence requirements and guidance.

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an important part in achieving this balance. Improperly disclosing any such information to third parties is not an acceptable practice.

**3.14** Accountability to the public for the proper use and prudent management of government resources is an essential part of auditors' responsibilities. Protecting and conserving government resources and using them appropriately for authorized activities are important elements of the public's expectations for auditors.

**3.15** Misusing the auditor position for financial gain or other benefits violates an auditor's fundamental responsibilities. An auditor's credibility can be damaged by actions that could be perceived by an objective third party with knowledge of the relevant information as improperly benefiting an auditor's personal financial interests or those of an immediate or close family member; a general partner; an entity for which the auditor serves as an officer, director, trustee, or employee; or an entity with which the auditor is negotiating concerning future employment.

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## Professional Behavior

**3.16** High expectations for the auditing profession include complying with all relevant legal, regulatory, and professional obligations and avoiding any conduct that could bring discredit to auditors' work, including actions that would cause an objective third party with knowledge of the relevant information to conclude that the auditors' work was professionally deficient. Professional behavior includes auditors putting forth an honest effort in performing their duties in accordance with the relevant technical and professional standards.

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## Independence

**3.17** GAGAS's practical consideration of independence consists of four interrelated sections, providing

- a. general requirements and application guidance;
- b. requirements for and guidance on a conceptual framework for making independence determinations based on facts and circumstances that are often unique to specific environments;
- c. requirements for and guidance on independence for auditors providing nonaudit services, including identification of specific nonaudit services that always impair independence and others that would not normally impair independence; and

- d. requirements for and guidance on documentation necessary to support adequate consideration of auditor independence.

**Requirements: General**

**3.18** In all matters relating to the GAGAS engagement, auditors and audit organizations must be independent from an audited entity.

**3.19** Auditors and audit organizations should avoid situations that could lead reasonable and informed third parties to conclude that the auditors and audit organizations are not independent and thus are not capable of exercising objective and impartial judgment on all issues associated with conducting the engagement and reporting on the work.

**3.20** Except under the limited circumstances discussed in paragraphs 3.66 and 3.67, auditors and audit organizations should be independent from an audited entity during

- a. any period of time that falls within the period covered by the financial statements or subject matter of the engagement and
- b. the period of professional engagement.

**Application Guidance: General**

**3.21** Independence comprises the following:

- a. Independence of mind: The state of mind that permits the conduct of an engagement without being affected by influences that compromise professional judgment, thereby allowing an individual to act with integrity and exercise objectivity and professional skepticism.
- b. Independence in appearance: The absence of circumstances that would cause a reasonable and informed third party to reasonably conclude that the integrity, objectivity, or professional skepticism of an audit organization or member of the engagement team had been compromised.

**3.22** Auditors and audit organizations maintain their independence so that their opinions, findings, conclusions, judgments, and recommendations

will be impartial and will be viewed as impartial by reasonable and informed third parties.

**3.23** The period of professional engagement begins when the auditors either sign an initial engagement letter or other agreement to conduct an engagement or begin to conduct an engagement, whichever is earlier. The period lasts for the duration of the professional relationship—which, for recurring engagements, could cover many periods—and ends with the formal or informal notification, either by the auditors or the audited entity, of the termination of the professional relationship or with the issuance of a report, whichever is later. Accordingly, the period of professional engagement does not necessarily end with the issuance of a report and recommence with the beginning of the following year’s engagement or a subsequent engagement with a similar objective.

**3.24** Under some conditions, the party requesting or requiring an engagement, referred to as the engaging party, will differ from the party responsible for the engagement’s subject matter, referred to as the responsible party. Under such conditions, the GAGAS independence requirements apply to the relationship between the auditors and the responsible party, not the relationship between the auditors and the engaging party. The following are examples of conditions under which the party requesting an engagement may differ from the party responsible for the engagement’s subject matter.

- a. A legislative body requires that auditors conduct, on the legislative body’s behalf, a performance audit of program operations that are the responsibility of an executive agency. GAGAS requires that the auditors be independent of the executive agency.
- b. A state agency engages an independent public accountant to conduct an examination-level attestation engagement to assess the validity of certain information that a local government provided to the state agency. GAGAS requires that the independent public accountant be independent of the local government.
- c. A government department works with a government agency that conducts examination-level attestation engagements of contractor compliance with the terms and conditions of agreements between the department and the contractor. GAGAS requires that the auditors be independent of the contractors.

**3.25** Auditors in government sometimes work under conditions that impair independence in accordance with this section. An example of such a circumstance is a threat created by a statutory requirement for auditors to serve in official roles that conflict with the independence requirements of this section, such as a law that requires an auditor to serve as a voting member of an entity's management committee or board of directors, for which there are no safeguards to eliminate or reduce the threats to an acceptable level. Paragraph 2.17b provides standard language for modified GAGAS compliance statements for auditors who experience such impairments. Determining how to modify the GAGAS compliance statement in these circumstances is a matter of professional judgment.

## GAGAS Conceptual Framework Approach to Independence

**3.26** Many different circumstances, or combinations of circumstances, are relevant in evaluating threats to independence. Therefore, GAGAS establishes a conceptual framework that auditors use to identify, evaluate, and apply safeguards to address threats to independence. The conceptual framework assists auditors in maintaining both independence of mind and independence in appearance. It can be applied to many variations in circumstances that create threats to independence and allows auditors to address threats to independence that result from activities that are not specifically prohibited by GAGAS.

### Requirements: GAGAS Conceptual Framework Approach to Independence

**3.27** Auditors should apply the conceptual framework<sup>17</sup> at the audit organization, engagement team, and individual auditor levels to

- a. identify threats to independence;
- b. evaluate the significance of the threats identified, both individually and in the aggregate; and
- c. apply safeguards as necessary to eliminate the threats or reduce them to an acceptable level.

**3.28** Auditors should reevaluate threats to independence, including any safeguards applied, whenever the audit organization or the

<sup>17</sup>See fig. 1 at the end of ch. 3 for a flowchart on applying the conceptual framework in accordance with GAGAS.

auditors become aware of new information or changes in facts and circumstances that could affect whether a threat has been eliminated or reduced to an acceptable level.

**3.29** Auditors should use professional judgment when applying the conceptual framework.

**3.30** Auditors should evaluate the following broad categories of threats to independence when applying the GAGAS conceptual framework:

- a. Self-interest threat: The threat that a financial or other interest will inappropriately influence an auditor's judgment or behavior.
- b. Self-review threat: The threat that an auditor or audit organization that has provided nonaudit services will not appropriately evaluate the results of previous judgments made or services provided as part of the nonaudit services when forming a judgment significant to a GAGAS engagement.
- c. Bias threat: The threat that an auditor will, as a result of political, ideological, social, or other convictions, take a position that is not objective.
- d. Familiarity threat: The threat that aspects of a relationship with management or personnel of an audited entity, such as a close or long relationship, or that of an immediate or close family member, will lead an auditor to take a position that is not objective.
- e. Undue influence threat: The threat that influences or pressures from sources external to the audit organization will affect an auditor's ability to make objective judgments.
- f. Management participation threat: The threat that results from an auditor's taking on the role of management or otherwise performing management functions on behalf of the audited entity, which will lead an auditor to take a position that is not objective.
- g. Structural threat: The threat that an audit organization's placement within a government entity, in combination with the structure of the government entity being audited, will affect the

audit organization's ability to perform work and report results objectively.

**3.31** Auditors should determine whether identified threats to independence are at an acceptable level or have been eliminated or reduced to an acceptable level, considering both qualitative and quantitative factors to determine the significance of a threat.

**3.32** When auditors determine that threats to independence are not at an acceptable level, the auditors should determine whether appropriate safeguards can be applied to eliminate the threats or reduce them to an acceptable level.

**3.33** In cases where auditors determine that threats to independence require the application of safeguards, auditors should document the threats identified and the safeguards applied to eliminate or reduce the threats to an acceptable level.

**3.34** If auditors initially identify a threat to independence after the audit report is issued, auditors should evaluate the threat's effect on the engagement and on GAGAS compliance. If the auditors determine that the newly identified threat's effect on the engagement would have resulted in the audit report being different from the report issued had the auditors been aware of it, they should communicate in the same manner as that used to originally distribute the report to those charged with governance, the appropriate officials of the audited entity, the appropriate officials of the audit organization requiring or arranging for the engagements, and other known users, so that they do not continue to rely on findings or conclusions that were affected by the threat to independence. If auditors previously posted the report to their publicly accessible website, they should remove the report and post a public notification that the report was removed. The auditors should then determine whether to perform the additional engagement work necessary to reissue the report, including any revised findings or conclusions, or to repost the original report if the additional engagement work does not result in a change in findings or conclusions.

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**Application Guidance: GAGAS Conceptual Framework Approach to Independence**

**3.35** For consideration of auditor independence, offices or units of an audit organization, or related or affiliated entities under common control, are not differentiated from one another. Consequently, for the purposes of evaluating independence using the conceptual framework, an audit organization that includes multiple offices or units, or includes multiple entities related or affiliated through common control, is considered to be one audit organization. Common ownership may also affect independence in appearance regardless of the level of control.

*Identifying Threats*

**3.36** Facts and circumstances that create threats to independence can result from events such as the start of a new engagement, assignment of new personnel to an ongoing engagement, and acceptance of a nonaudit service for an audited entity.

**3.37** Threats to independence may be created by a wide range of relationships and circumstances. Circumstances that result in a threat to independence in one of the categories may result in other threats as well.

**3.38** Examples of circumstances that create self-interest threats for an auditor follow:

- a. An audit organization having undue dependence on income from a particular audited entity.
- b. A member of the audit team entering into employment negotiations with an audited entity.
- c. An audit organization discovering a significant error when evaluating the results of a previous professional service provided by the audit organization.
- d. A member of the audit team having a direct financial interest in the audited entity. However, this would not preclude auditors from auditing pension plans that they participate in if (1) the auditors have no control over the investment strategy, benefits, or other management issues associated with the pension plan and (2) the auditors belong to such pension plan as part of their employment with the audit organization or prior employment with the audited



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entity, provided that the plan is normally offered to all employees in equivalent employment positions.

**3.39** Examples of circumstances that create self-review threats for an auditor follow:

- a. An audit organization issuing a report on the effectiveness of the operation of financial or performance management systems after designing or implementing the systems.
- b. An audit organization having prepared the original data used to generate records that are the subject matter of the engagement.
- c. An audit organization providing a service for an audited entity that directly affects the subject matter information of the engagement.
- d. A member of the engagement team being, or having recently been, employed by the audited entity in a position to exert significant influence over the subject matter of the engagement.

**3.40** Examples of circumstances that create bias threats for an auditor follow:

- a. A member of the engagement team having preconceptions about the objectives of a program under audit that are strong enough to affect the auditor's objectivity.
- b. A member of the engagement team having biases associated with political, ideological, or social convictions that result from membership or employment in, or loyalty to, a particular type of policy, group, entity, or level of government that could affect the auditor's objectivity.

**3.41** Examples of circumstances that create familiarity threats for an auditor follow:

- a. A member of the engagement team having a close or immediate family member who is a principal or senior manager of the audited entity.
- b. A member of the engagement team having a close or immediate family member who is an employee of the audited entity and is in

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a position to exert significant influence over the subject matter of the engagement.

- c. A principal or employee of the audited entity having recently served on the engagement team in a position to exert significant influence over the subject matter of the engagement.
- d. An auditor accepting gifts or preferential treatment from an audited entity, unless the value is trivial or inconsequential.
- e. Senior engagement personnel having a long association with the audited entity.

**3.42** Examples of circumstances that create undue influence threats for an auditor or audit organization include existence of the following:

- a. External interference or influence that could improperly limit or modify the scope of an engagement or threaten to do so, including exerting pressure to inappropriately reduce the extent of work performed in order to reduce costs or fees.
- b. External interference with the selection or application of engagement procedures or in the selection of transactions to be examined.
- c. Unreasonable restrictions on the time allowed to complete an engagement or issue the report.
- d. External interference over assignment, appointment, compensation, and promotion.
- e. Restrictions on funds or other resources provided to the audit organization that adversely affect the audit organization's ability to carry out its responsibilities.
- f. Authority to overrule or to inappropriately influence the auditors' judgment as to the appropriate content of the report.
- g. Threat of replacing the auditor or the audit organization based on a disagreement with the contents of an audit report, the auditors' conclusions, or the application of an accounting principle or other criteria.

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- h.** Influences that jeopardize the auditors' continued employment for reasons other than incompetence, misconduct, or the audited entity's need for GAGAS engagements.

**3.43** Examples of circumstances that create management participation threats for an auditor follow:

- a.** A member of the engagement team being, or having recently been, a principal or senior manager of the audited entity.
- b.** An auditor serving as a voting member of an entity's management committee or board of directors, making policy decisions that affect future direction and operation of an entity's programs, supervising entity employees, developing or approving programmatic policy, authorizing an entity's transactions, or maintaining custody of an entity's assets.
- c.** An auditor or audit organization recommending a single individual for a specific position that is key to the audited entity or program under audit, or otherwise ranking or influencing management's selection of the candidate.
- d.** An auditor preparing management's corrective action plan to deal with deficiencies detected in the engagement.

**3.44** Examples of circumstances that create structural threats for an auditor follow:

- a.** For both external and internal audit organizations, structural placement of the audit function within the reporting line of the areas under audit.
- b.** For internal audit organizations, administrative direction from the audited entity's management.

### *Evaluating Threats*

**3.45** Threats to independence are evaluated both individually and in the aggregate, as threats can have a cumulative effect on auditors' independence.

**3.46** When evaluating threats to independence, an acceptable level is a level at which a reasonable and informed third party would likely conclude

that the audit organization or auditor is independent. The concept of a reasonable and informed third party is a test that involves an evaluation by a hypothetical person. Such a person possesses skills, knowledge, and experience to objectively evaluate the appropriateness of the auditor's judgments and conclusions. This evaluation entails weighing all the relevant facts and circumstances, including any safeguards applied, that the auditor knows, or could reasonably be expected to know, at the time that the evaluation is made.

**3.47** A threat to independence is not at an acceptable level if it either

- a. could affect the auditors' ability to conduct an engagement without being affected by influences that compromise professional judgment or
- b. could expose the auditors or audit organization to circumstances that would cause a reasonable and informed third party to conclude that the integrity, objectivity, or professional skepticism of the audit organization, or an auditor, had been compromised.

**3.48** The GAGAS section on nonaudit services in paragraphs 3.64 through 3.106 provides requirements and guidance on evaluating threats to independence related to nonaudit services that auditors provide to audited entities. That section also enumerates specific nonaudit services that always impair auditor independence with respect to audited entities and that auditors are prohibited from providing to audited entities.

#### *Applying Safeguards*

**3.49** Safeguards are actions or other measures, individually or in combination, that auditors and audit organizations take that effectively eliminate threats to independence or reduce them to an acceptable level. Safeguards vary depending on the facts and circumstances.

**3.50** Examples of safeguards include

- a. consulting an independent third party, such as a professional organization, a professional regulatory body, or another auditor to discuss engagement issues or assess issues that are highly technical or that require significant judgment;
- b. involving another audit organization to perform or re-perform part of the engagement;

- c. having an auditor who was not a member of the engagement team review the work performed; and
- d. removing an auditor from an engagement team when that auditor's financial or other interests or relationships pose a threat to independence.

**3.51** The lists of safeguards in 3.50 and 3.69 cannot provide safeguards for all circumstances. They may, however, provide a starting point for auditors who have identified threats to independence and are considering what safeguards could eliminate those threats or reduce them to an acceptable level. In some cases, multiple safeguards may be necessary to address a threat.

#### *Audit Organizations in Government Entities*

**3.52** The ability of an audit organization structurally located in a government entity to perform work and report the results objectively can be affected by its placement within the government entity and the structure of the government entity being audited. The independence standard applies to auditors in both external audit organizations (reporting to third parties externally or to both internal and external parties) and internal audit organizations (reporting only to senior management within the audited entity). Such audit organizations are often subject to constitutional or statutory safeguards that mitigate the effects of structural threats to independence.

**3.53** For external audit organizations, constitutional or statutory safeguards that mitigate the effects of structural threats to independence may include governmental structures under which a government audit organization is

- a. at a level of government other than the one of which the audited entity is part (federal, state, or local)—for example, federal auditors auditing a state government program—or
- b. placed within a different branch of government from that of the audited entity—for example, legislative auditors auditing an executive branch program.

**3.54** Safeguards other than those described in paragraph 3.53 may mitigate threats resulting from governmental structures. For external audit organizations, structural threats may be mitigated if the head of the audit

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organization meets any of the following criteria in accordance with constitutional or statutory requirements:

- a. directly elected by voters of the jurisdiction being audited;
- b. elected or appointed by a legislative body, subject to removal by a legislative body, and reporting the results of engagements to and accountable to a legislative body;
- c. appointed by someone other than a legislative body, so long as the appointment is confirmed by a legislative body and removal from the position is subject to oversight or approval by a legislative body, and reports the results of engagements to and is accountable to a legislative body; or
- d. appointed by, accountable to, reports to, and can only be removed by a statutorily created governing body, the majority of whose members are independently elected or appointed and are outside the organization being audited.

**3.55** In addition to the criteria in paragraphs 3.53 and 3.54, GAGAS recognizes that there may be other organizational structures under which external audit organizations in government entities could be considered independent. If appropriately designed and implemented, these structures provide safeguards that prevent the audited entity from interfering with the audit organization's ability to perform the work and report the results impartially. An external audit organization may be structurally independent under a structure different from the ones listed in paragraphs 3.53 and 3.54 if the government audit organization is subject to all of the following constitutional or statutory provisions. The following constitutional or statutory provisions may also be used as safeguards to augment those listed in paragraphs 3.53 and 3.54:

- a. protections that prevent the audited entity from abolishing the audit organization;
- b. protections requiring that if the head of the audit organization is removed from office, the head of the agency reports this fact and the reasons for the removal to the legislative body;
- c. protections that prevent the audited entity from interfering with the initiation, scope, timing, and completion of any engagement;

- d. protections that prevent the audited entity from interfering with audit reporting, including the findings and conclusions or the manner, means, or timing of the audit organization's reports;
- e. protections that require the audit organization to report to a legislative body or other independent governing body on a recurring basis;
- f. protections that give the audit organization sole authority over the selection, retention, advancement, and dismissal of its personnel; and
- g. access to records and documents related to the agency, program, or function being audited and access to government officials or other individuals as needed to conduct the engagement.

**3.56** Government internal auditors who work under the direction of the audited entity's management are considered structurally independent for the purposes of reporting internally, if the head of the audit organization meets all of the following criteria:

- a. is accountable to the head or deputy head of the government entity or to those charged with governance;
- b. reports the engagement results both to the head or deputy head of the government entity and to those charged with governance;
- c. is located organizationally outside the staff or line management function of the unit under audit;
- d. has access to those charged with governance; and
- e. is sufficiently removed from pressures to conduct engagements and report findings, opinions, and conclusions objectively without fear of reprisal.

#### *Internal Auditors*

**3.57** Certain entities employ auditors to work for entity management. These auditors may be subject to administrative direction from persons involved in the entity management process. Such audit organizations are internal audit functions and are encouraged to use the Institute of Internal

Auditors' *International Standards for the Professional Practice of Internal Auditing*, in conjunction with GAGAS.

**3.58** When an internal audit organization conducts engagements pertaining to external parties, such as contractors or entities subject to other outside agreements, and no impairments to independence exist, the audit organization can be considered independent as an external audit organization of those external parties.

**Requirements: Independence Impairments**

**3.59** Auditors should conclude that independence is impaired if no safeguards have been effectively applied to eliminate an unacceptable threat or reduce it to an acceptable level.

**3.60** When auditors conclude that independence of the engagement team or the audit organization is impaired under paragraph 3.59, auditors should decline to accept an engagement or should terminate an engagement in progress (except in circumstances discussed in paragraphs 3.25 or 3.84).

**Application Guidance: Independence Impairments**

**3.61** Whether independence is impaired depends on the nature of the threat, whether the threat is of such significance that it would compromise an auditor's professional judgment or create the appearance that the auditor's integrity, objectivity, or professional skepticism may be compromised, and the specific safeguards applied to eliminate the threat or reduce it to an acceptable level.

**3.62** If auditors conclude that an individual auditor's independence is impaired under paragraph 3.59, it may be necessary to terminate the engagement or it may be possible to take action that satisfactorily addresses the effect of the individual auditor's independence impairment.

**3.63** Factors that are relevant in evaluating whether the independence of the engagement team or the audit organization is impaired by an individual auditor's independence impairment include

- a. the nature and duration of the individual auditor's impairment;



- b. the number and nature of any previous impairments with respect to the current engagement;
- c. whether a member of the engagement team had knowledge of the interest or relationship that caused the individual auditor's impairment;
- d. whether the individual auditor whose independence is impaired is (1) a member of the engagement team or (2) another individual for whom there are independence requirements;
- e. the role of the individual auditor on the engagement team whose independence is impaired;
- f. the effect of the service, if any, on the accounting records or audited entity's financial statements if the individual auditor's impairment was caused by the provision of a nonaudit service;
- g. whether a partner or director of the audit organization had knowledge of the individual auditor's impairment and failed to ensure that the individual auditor's impairment was promptly communicated to an appropriate individual within the audit organization; and
- h. the extent of the self-interest, undue influence, or other threats created by the individual auditor's impairment.

### Provision of Nonaudit Services to Audited Entities

#### **Requirement: Nonaudit Services**

**3.64** Before auditors agree to provide a nonaudit service to an audited entity, they should determine whether providing such a service would create a threat to independence, either by itself or in aggregate with other nonaudit services provided, with respect to any GAGAS engagement they conduct.

#### **Application Guidance: Nonaudit Services**

**3.65** Auditors have traditionally provided a range of nonaudit services that are consistent with their skills and expertise. Providing nonaudit services

to audited entities may create threats to the independence of auditors or audit organizations.

**3.66** For performance audits and agreed-upon procedures engagements, nonaudit services that are otherwise prohibited by GAGAS may be provided when such services do not relate to the specific subject matter of the engagement.

**3.67** For financial audits, examination or review engagements, and reviews of financial statements, a nonaudit service otherwise prohibited by GAGAS and provided during the period covered by the financial statements may not threaten independence with respect to those financial statements provided that the following conditions exist:

- a. the nonaudit service was provided prior to the period of professional engagement;
- b. the nonaudit service related only to periods prior to the period covered by the financial statements; and
- c. the financial statements for the period to which the nonaudit service did relate were audited by other auditors (or in the case of an examination, review, or review of financial statements, examined, reviewed, or audited by other auditors as appropriate).

**3.68** Nonaudit services that auditors provide can affect independence of mind and in appearance in periods after the nonaudit services were provided. For example, if auditors have designed and implemented an accounting and financial reporting system that is expected to be in place for many years, a threat to independence in appearance may exist in subsequent periods for future engagements that those auditors conduct. For recurring engagements, having another independent audit organization conduct an engagement over the areas affected by the nonaudit service may provide a safeguard that allows the audit organization that provided the nonaudit service to mitigate the threat to its independence.

**3.69** The following are examples of actions that in certain circumstances could be safeguards in addressing threats to independence related to nonaudit services:

- a. not including individuals who provided the nonaudit service as engagement team members;

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- b. having another auditor, not associated with the engagement, review the engagement and nonaudit work as appropriate;
  - c. engaging another audit organization to evaluate the results of the nonaudit service; or
  - d. having another audit organization re-perform the nonaudit service to the extent necessary to enable that other audit organization to take responsibility for the service.

#### *Routine Activities*

**3.70** Routine activities that auditors perform related directly to conducting an engagement, such as providing advice and responding to questions as part of an engagement, are not considered nonaudit services under GAGAS. Such routine activities generally involve providing advice or assistance to the audited entity on an informal basis as part of an engagement. Routine activities typically are insignificant in terms of time incurred or resources expended and generally do not result in a specific project or engagement or in the auditors producing a formal report or other formal work product. However, activities such as financial statement preparation, cash-to-accrual conversions, and reconciliations are considered nonaudit services under GAGAS, not routine activities related to the performance of an engagement, and are evaluated using the conceptual framework as discussed in paragraphs 3.87 through 3.95.

**3.71** Routine activities directly related to an engagement may include the following:

- a. providing advice to the audited entity on an accounting matter as an ancillary part of the overall financial audit;
- b. providing advice to the audited entity on routine business matters;
- c. educating the audited entity about matters within the technical expertise of the auditors; and
- d. providing information to the audited entity that is readily available to the auditors, such as best practices and benchmarking studies.

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*Other Services Provided by Government Audit Organizations*

**3.72** Audit organizations in government entities frequently provide services that differ from the traditional professional services that an accounting or consulting firm provides to or for an audited entity. These types of services are often provided in response to a statutory requirement, at the discretion of the authority of the audit organization, or to an engaging party (such as a legislative oversight body or an independent external organization) rather than a responsible party, and would generally not create a threat to independence. 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;
- f. assisting legislative bodies by developing questions for use at hearings;
- g. providing training, speeches, and technical presentations;
- h. providing 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; and
- j. providing audit, investigative, and oversight-related services that do not involve a GAGAS engagement, such as

- (1) investigations of alleged fraud, violation of contract provisions or grant agreements, or abuse;
- (2) periodic audit recommendation follow-up engagements and reports; and
- (3) identifying best practices or leading practices for use in advancing the practices of government organizations.

**Requirements: Management Responsibilities**

**3.73** Before auditors agree to provide nonaudit services to an audited entity that the audited entity's management requested and that could create a threat to independence, either by themselves or in aggregate with other nonaudit services provided, with respect to any GAGAS engagement they conduct, auditors should determine that the audited entity has designated an individual who possesses suitable skill, knowledge, or experience and that the individual understands the services to be provided sufficiently to oversee them.

**3.74** Auditors should document consideration of management's ability to effectively oversee nonaudit services to be provided.

**3.75** In cases where the audited entity is unable or unwilling to assume these responsibilities (for example, the audited entity does not have an individual with suitable skill, knowledge, or experience to oversee the nonaudit services provided, or is unwilling to perform such functions because of lack of time or desire), auditors should conclude that the provision of these services is an impairment to independence.

**3.76** Auditors providing nonaudit services to audited entities should obtain agreement from audited entity management that audited entity management performs the following functions in connection with the nonaudit services:

- a. assumes all management responsibilities;
- b. oversees the services, by designating an individual, preferably within senior management, who possesses suitable skill, knowledge, or experience;

- c. evaluates the adequacy and results of the services provided;  
and
- d. accepts responsibility for the results of the services.

**3.77** In connection with nonaudit services, auditors should establish and document their understanding with the audited entity's management or those charged with governance, as appropriate, regarding the following:

- a. objectives of the nonaudit service,
- b. services to be provided,
- c. audited entity's acceptance of its responsibilities as discussed in paragraph 3.76,
- d. the auditors' responsibilities, and
- e. any limitations on the provision of nonaudit services.

**3.78** Auditors should conclude that management responsibilities that the auditors perform for an audited entity are impairments to independence. If the auditors were to assume management responsibilities for an audited entity, the management participation threats created would be so significant that no safeguards could reduce them to an acceptable level.

### **Application Guidance: Management Responsibilities**

**3.79** A critical component of determining whether a threat to independence exists is consideration of management's ability to effectively oversee the nonaudit service to be provided. Although the responsible individual in management is required to have sufficient expertise to oversee the nonaudit services, management is not required to possess the expertise to perform or re-perform the services. However, indicators of management's ability to effectively oversee the nonaudit service include management's ability to determine the reasonableness of the results of the nonaudit services provided and to recognize a material

error, omission, or misstatement in the results of the nonaudit services provided.

**3.80** Management responsibilities involve leading and directing an entity, including making decisions regarding the acquisition, deployment, and control of human, financial, physical, and intangible resources.

**3.81** The following are considered management responsibilities:

- a. setting policies and strategic direction for the audited entity;
- b. directing and accepting responsibility for the actions of the audited entity's employees in the performance of their routine, recurring activities;
- c. having custody of an audited entity's assets;
- d. reporting to those charged with governance on behalf of management;
- e. deciding which of the audit organization's or outside third party's recommendations to implement;
- f. accepting responsibility for the management of an audited entity's project;
- g. accepting responsibility for designing, implementing, or maintaining internal control;
- h. providing services that are intended to be used as management's primary basis for making decisions that are significant to the subject matter of the engagement;
- i. developing an audited entity's performance measurement system when that system is material or significant to the subject matter of the engagement; and
- j. serving as a voting member of an audited entity's management committee or board of directors.

**3.82** Whether a specific activity is a management responsibility as identified in paragraph 3.81 or otherwise depends on the facts and circumstances.

**Requirements: Providing Nonaudit Services**

**3.83** Auditors who previously provided nonaudit services for an entity that is a prospective subject of an engagement should evaluate the effect of those nonaudit services on independence before agreeing to conduct a GAGAS engagement. If auditors provided a nonaudit service in the period to be covered by the engagement, they should (1) determine if GAGAS expressly prohibits the nonaudit service; (2) if audited entity management requested the nonaudit service, determine whether the skill, knowledge, or experience of the individual responsible for overseeing the nonaudit service was sufficient; and (3) determine whether a threat to independence exists and address any threats noted in accordance with the conceptual framework.

**3.84** Auditors in a government entity may be required to provide a nonaudit service that impairs the auditors' independence with respect to a required engagement. If, because of constitutional or statutory requirements over which they have no control, the auditors can neither implement safeguards to reduce the resulting threat to an acceptable level nor decline to provide or terminate a nonaudit service that is incompatible with engagement responsibilities, auditors should disclose the nature of the threat that could not be eliminated or reduced to an acceptable level and modify the GAGAS compliance statement as discussed in paragraph 2.17b accordingly. Determining how to modify the GAGAS compliance statement in these circumstances is a matter of professional judgment.

**Consideration of Specific  
Nonaudit Services**

**3.85** By their nature, certain nonaudit services directly support an entity's operations and, if provided to an audited entity, create a threat to the auditors' ability to maintain independence in mind and appearance. Some aspects of these services will impair auditors' ability to conduct GAGAS engagements for the entities to which the services are provided.

**3.86** Auditors may be able to provide nonaudit services in the broad areas indicated in paragraphs 3.87 through 3.106 without impairing independence if (1) the nonaudit services are not expressly prohibited by GAGAS requirements, (2) the auditors have determined that the requirements for providing nonaudit services in paragraphs 3.73 through 3.78 and paragraph 3.83 have been met, and (3) any significant threats to



independence have been eliminated or reduced to an acceptable level through the application of safeguards. The conceptual framework enables auditors to evaluate independence given the facts and circumstances of individual services that are not specifically prohibited.

### **Requirements: Preparing Accounting Records and Financial Statements**

**3.87** Auditors should conclude that the following services involving preparation of accounting records impair independence with respect to an audited entity:

- a. determining or changing journal entries, account codes or classifications for transactions, or other accounting records for the entity without obtaining management's approval;
- b. authorizing or approving the entity's transactions; and
- c. preparing or making changes to source documents without management approval.

**3.88** Auditors should conclude that preparing financial statements in their entirety from a client-provided trial balance or underlying accounting records creates significant threats to auditors' independence, and should document the threats and safeguards applied to eliminate and reduce threats to an acceptable level in accordance with paragraph 3.33 or decline to provide the services.<sup>18</sup>

**3.89** Auditors should identify as threats to independence any services related to preparing accounting records and financial statements, other than those defined as impairments to independence in paragraph 3.87 and significant threats in paragraph 3.88. These services include

- a. recording transactions for which management has determined or approved the appropriate account classification, or posting coded transactions to an audited entity's general ledger;

<sup>18</sup>See fig. 2 at the end of ch. 3 for a flowchart on independence considerations for preparing accounting records and financial statements.

- b. preparing certain line items or sections of the financial statements based on information in the trial balance;
- c. posting entries that an audited entity's management has approved to the entity's trial balance; and
- d. preparing account reconciliations that identify reconciling items for the audited entity management's evaluation.

**3.90** Auditors should evaluate the significance of threats to independence created by providing any services discussed in paragraph 3.89 and should document the evaluation of the significance of such threats.<sup>19</sup>

### **Application Guidance: Preparing Accounting Records and Financial Statements**

**3.91** Management is responsible for the preparation and fair presentation of the financial statements in accordance with the applicable financial reporting framework, even if the auditor assisted in drafting those financial statements. Consequently, an auditor accepting responsibility for the preparation and fair presentation of financial statements that the auditor will subsequently audit or that will otherwise be the subject matter of an engagement would impair the auditor's independence.

**3.92** Source documents include those providing evidence that transactions have occurred (for example, purchase orders, payroll time records, customer orders, and contracts). Such records also include an audited entity's general ledger and subsidiary records or equivalent.

**3.93** Determining whether services, as discussed in paragraph 3.89, are significant threats and require safeguards is a matter of professional judgment.

**3.94** Factors that are relevant in evaluating the significance of any threats created by providing services as discussed in paragraph 3.89 include

<sup>19</sup>See para. 3.33 for additional requirements related to documenting threats identified and safeguards applied to eliminate or reduce threats to an acceptable level.

- a. the extent to which the outcome of the service could have a material effect on the financial statements,
- b. the degree of subjectivity involved in determining the appropriate amounts or treatment for those matters reflected in the financial statements, and
- c. the extent of the audited entity's involvement in determining significant matters of judgment.

**3.95** Providing clerical assistance, such as typing, formatting, printing, and binding financial statements, is unlikely to be a significant threat.

**Requirement: Internal Audit Assistance Services Provided by External Auditors**

**3.96** Internal audit assistance services involve assisting an entity in performing its internal audit activities. Auditors should conclude that the following internal audit assistance activities impair an external auditor's independence with respect to an audited entity:

- a. setting internal audit policies or the strategic direction of internal audit activities;
- b. performing procedures that form part of the internal control, such as reviewing and approving changes to employee data access privileges; and
- c. determining the scope of the internal audit function and resulting work.

**Requirements: Internal Control Evaluation as a Nonaudit Service**

**3.97** Auditors should conclude that providing or supervising ongoing monitoring procedures over an entity's system of internal control impairs independence because the management participation threat created is so significant that no safeguards could reduce the threat to an acceptable level.

**3.98** Separate evaluations are sometimes provided as a nonaudit service. When providing separate evaluations as nonaudit services, auditors should evaluate the significance of the threat created by performing separate evaluations and apply safeguards when necessary to eliminate the threat or reduce it to an acceptable level.

### **Application Guidance: Internal Control Evaluation as a Nonaudit Service**

**3.99** Accepting responsibility for designing, implementing, or maintaining internal control includes accepting responsibility for designing, implementing, or maintaining monitoring procedures. Monitoring involves the use of either ongoing monitoring procedures or separate evaluations to gather and analyze persuasive information supporting conclusions about the effectiveness of the internal control system. Ongoing monitoring procedures performed on behalf of management are built into the routine, recurring operating activities of an entity.

**3.100** Factors relevant to evaluating the significance of any threats created by providing separate evaluations as a nonaudit service include

- a. the frequency of the separate evaluations and
- b. the scope or extent of the controls (in relation to the scope of the engagement conducted) being evaluated.

**3.101** A separate evaluation provided as a nonaudit service is not a substitute for engagement procedures in a GAGAS engagement.

### **Requirement: Information Technology Services**

**3.102** Auditors should conclude that providing information technology (IT) services to an audited entity that relate to the period under audit impairs independence if those services include

- a. designing or developing an audited entity's financial information system or other IT system that will play a significant role in the management of an area of operations that is or will be the subject matter of an engagement;

- b.** making other than insignificant modifications to source code underlying an audited entity's existing financial information system or other IT system that will play a significant role in the management of an area of operations that is or will be the subject matter of an engagement;
- c.** supervising audited entity personnel in the daily operation of an audited entity's information system; or
- d.** operating an audited entity's network, financial information system, or other IT system that will play a significant role in the management of an area of operations that is or will be the subject matter of an engagement.

**Application Guidance: Information Technology Services**

**3.103** Services related to IT systems include the design or implementation of hardware or software systems. The systems may aggregate source data, form part of the internal control over the subject matter of the engagement, or generate information that affects the subject matter of the engagement.

**Requirement: Appraisal, Valuation, and Actuarial Services**

**3.104** Auditors should conclude that independence is impaired if an audit organization provides appraisal, valuation, or actuarial services to an audited entity when (1) the services involve a significant degree of subjectivity and (2) the results of the service, individually or when combined with other valuation, appraisal, or actuarial services, are material to the audited entity's financial statements or other information on which the audit organization is reporting.

**Application Guidance: Appraisal, Valuation, and Actuarial Services**

**3.105** A valuation comprises the making of assumptions with regard to future developments; the application of appropriate methodologies and

techniques; and the combination of both to compute a certain value, or range of values, for an asset, a liability, or an entity as a whole.

**Requirement: Other Nonaudit Services**

**3.106** Auditors should conclude that providing certain other nonaudit services impairs an external auditor's independence with respect to an audited entity. These activities include the following:

- a. Advisory service
  - (1) Assuming any management responsibilities
- b. Benefit plan administration
  - (1) Making policy decisions on behalf of management
  - (2) Interpreting the provisions in a plan document for a plan participant on behalf of management without first obtaining management's concurrence
  - (3) Making disbursements on behalf of the plan
  - (4) Having custody of the plan's assets
  - (5) Serving in a fiduciary capacity, as defined under the Employee Retirement Income Security Act of 1974<sup>20</sup>
- c. Business risk consulting
  - (1) Making or approving business risk decisions
  - (2) Presenting business risk considerations to those charged with governance on behalf of management
- d. Executive or employee recruiting
  - (1) Committing the audited entity to employee compensation or benefit arrangements

<sup>20</sup>See Section 2510.3-21 of Title 29, *Code of Federal Regulations*.

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(2) Hiring or terminating the audited entity's employees

e. Investment advisory or management

(1) Making investment decisions on behalf of management or otherwise having discretionary authority over an audited entity's investments

(2) Executing a transaction to buy or sell an audited entity's investments

(3) Having custody of an audited entity's assets, such as taking temporary possession of securities

**Documentation**

**Requirement: Documentation**

**3.107** While insufficient documentation of an auditor's compliance with the independence standard does not impair independence, auditors should prepare appropriate documentation under the GAGAS quality management requirements.<sup>21</sup> The independence standard includes the following documentation requirements, where applicable:

- a. document threats to independence that require the application of safeguards, along with safeguards applied, in accordance with the conceptual framework for independence as required by paragraph 3.33;
- b. document the safeguards in paragraphs 3.52 through 3.56 if an audit organization is structurally located within a government entity and is considered structurally independent based on those safeguards;

<sup>21</sup>See paras. 5.132 through 5.138 for additional discussion pertaining to documentation of the system of quality management and paras. 5.47 through 5.50 for additional discussion of policies and procedures on independence, legal, and ethical requirements.

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- c. document consideration of audited entity management’s ability to effectively oversee a nonaudit service to be provided by the auditor as indicated in paragraph 3.74;
- d. document the auditor’s understanding with an audited entity for which the auditor will provide a nonaudit service as indicated in paragraph 3.77; and
- e. document the evaluation of the significance of the threats created by providing any of the services discussed in paragraph 3.89.

**Application Guidance: Documentation**

**3.108** Documentation of independence considerations provides evidence of the auditor’s judgments in forming conclusions regarding compliance with independence requirements.

## Professional Judgment

**Requirement: Professional Judgment**

**3.109** Auditors must use professional judgment in planning and conducting the engagement and in reporting the results.

**Application Guidance: Professional Judgment**

**3.110** Professional judgment includes exercising reasonable care and professional skepticism. Reasonable care includes acting diligently in accordance with applicable professional standards and ethical principles. Attributes of professional skepticism include a questioning mind, awareness of conditions that may indicate possible misstatement owing to error or fraud, and a critical assessment of evidence. Professional skepticism includes being alert to, for example, evidence that contradicts other evidence obtained or information that brings into question the reliability of documents or responses to inquiries to be used as evidence. Further, it includes a mindset in which auditors assume that management is neither dishonest nor of unquestioned honesty. Auditors may accept records and documents as genuine unless they have reason to believe the contrary. Auditors may consider documenting procedures undertaken



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to support their application of professional skepticism in highly judgmental or subjective areas under audit.

**3.111** Using the auditor's professional knowledge, skills, and abilities, in good faith and with integrity, to diligently gather information and objectively evaluate the sufficiency and appropriateness of evidence is a critical component of GAGAS engagements. Professional judgment and competence are interrelated because judgments made depend upon the auditor's competence, as discussed in chapter 4.

**3.112** Professional judgment represents the application of the collective knowledge, skills, and abilities of all the personnel involved with an engagement, as well as the professional judgment of individual auditors. In addition, professional judgment may involve consultation with other stakeholders, specialists, and management in the audit organization.

**3.113** Using professional judgment is important to auditors in carrying out all aspects of their professional responsibilities, including following the independence standards and related conceptual framework; maintaining objectivity and credibility; assigning competent personnel to the engagement; defining the scope of work; evaluating, documenting, and reporting the results of the work; and maintaining appropriate quality for the engagement process.

**3.114** Using professional judgment is important to auditors in applying the conceptual framework to determine independence in a given situation. This includes identifying and evaluating any threats to independence, including threats to the appearance of independence, and related safeguards that may mitigate the identified threats.<sup>22</sup>

**3.115** Using professional judgment is important to auditors in determining the necessary level of understanding of the engagement subject matter and related circumstances. This includes considering whether the audit team's collective experience, training, knowledge, skills, abilities, and overall understanding are sufficient to assess the risks that the subject matter of the engagement may contain a significant inaccuracy or could be misinterpreted.<sup>23</sup>

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<sup>22</sup>See para. 3.21b for a description of independence in appearance.

<sup>23</sup>See paras. 4.02 through 4.15 for a discussion of competence.

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**Chapter 3: Ethics, Independence, and Professional Judgment**

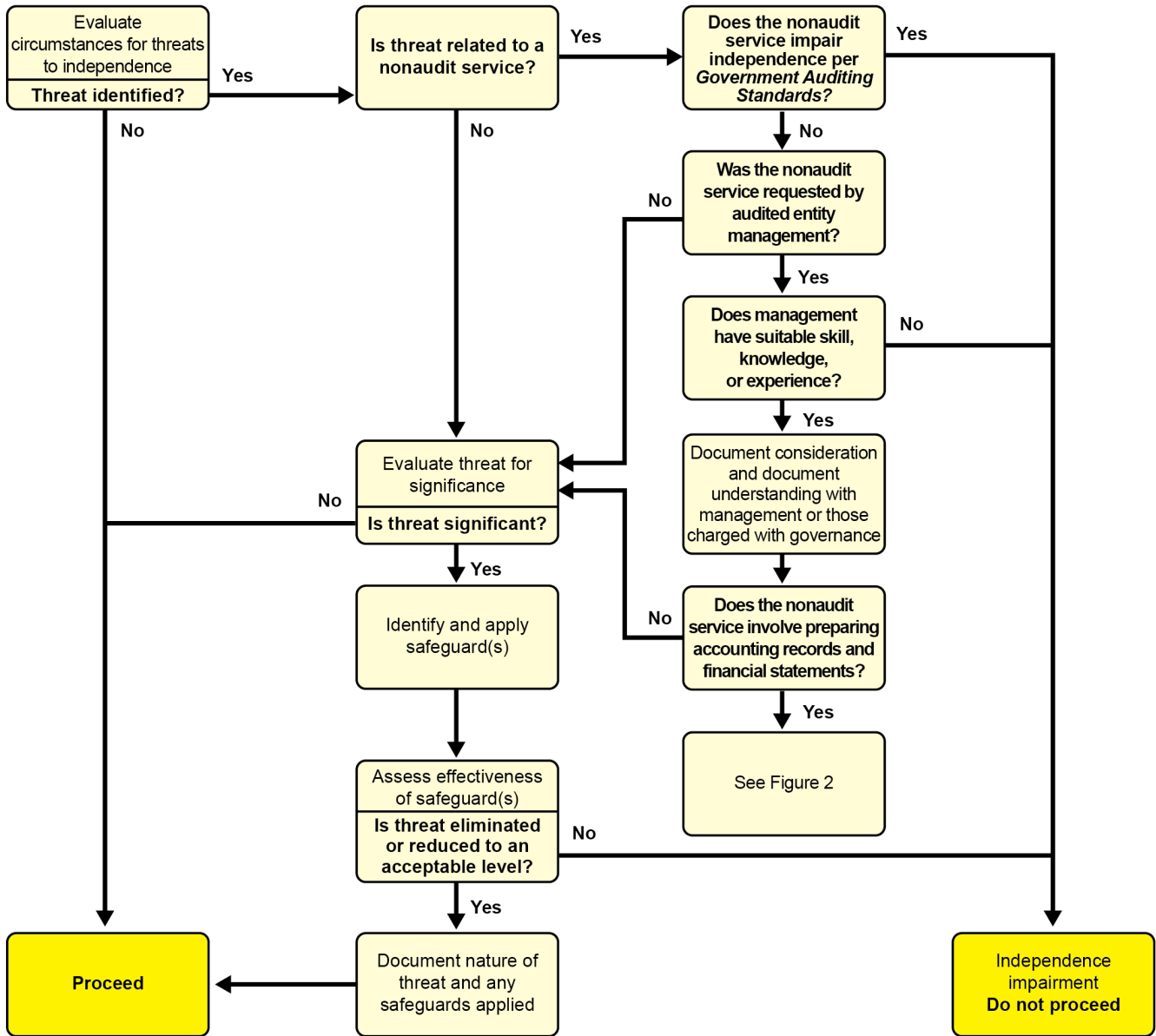
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**3.116** An auditor's consideration of the risk level of each engagement, including the risk of arriving at improper conclusions, is also important. Within the context of audit risk, exercising professional judgment in determining the sufficiency and appropriateness of evidence to be used to support the findings and conclusions based on the engagement objectives and any recommendations reported is integral to the engagement process.

**3.117** While this requirement places responsibility on each auditor and audit organization to exercise professional judgment in planning and conducting an engagement, it does not imply unlimited responsibility nor does it imply infallibility on the part of either the individual auditor or the audit organization. Absolute assurance is not attainable because of factors such as the nature of evidence and characteristics of fraud. Professional judgment does not mean eliminating all possible limitations or weaknesses associated with a specific engagement, but rather identifying, assessing, mitigating, and concluding on them.

Chapter 3: Ethics, Independence, and Professional Judgment

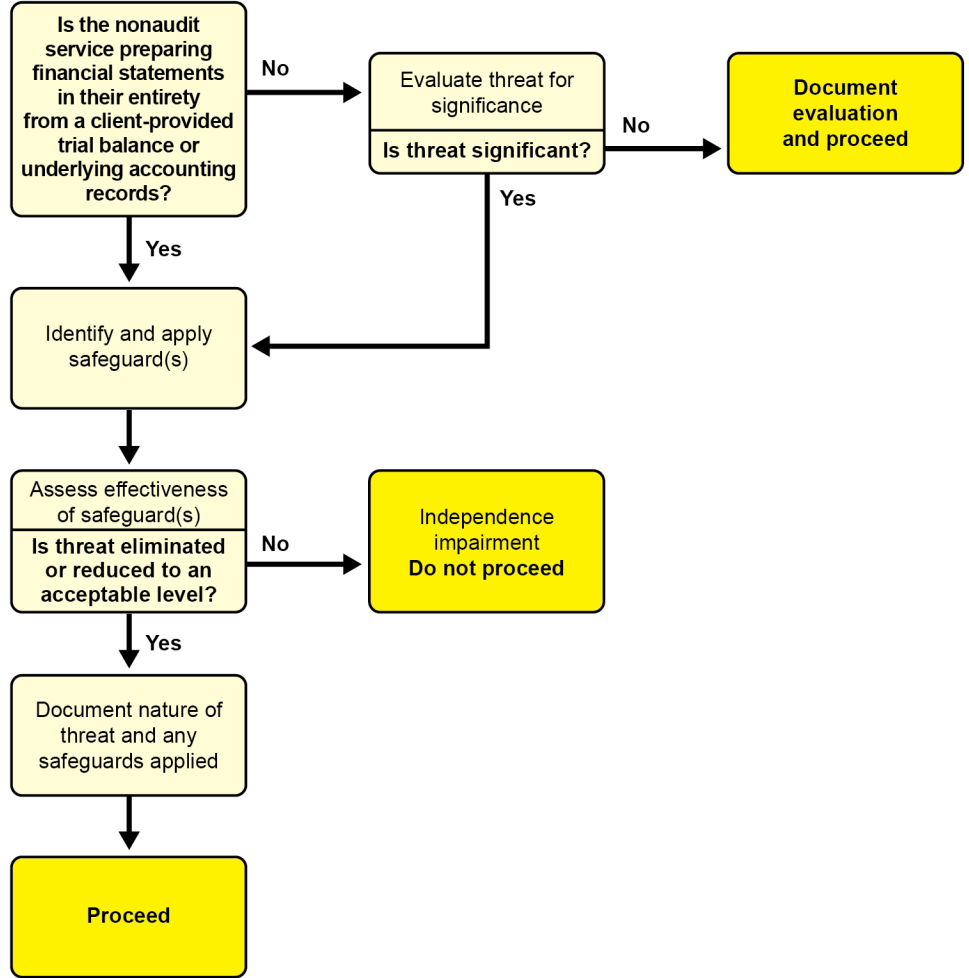
Figure 1: Generally Accepted Government Auditing Standards Conceptual Framework for Independence



Source: GAO. | GAO-24-106786

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Figure 2: Independence Considerations for Preparing Accounting Records and Financial Statements



Source: GAO. | GAO-24-106786

# Chapter 4: Competence and Continuing Professional Education

**4.01** This chapter establishes the generally accepted government auditing standards (GAGAS) requirements for competence and continuing professional education (CPE). Competence includes being knowledgeable about the specific GAGAS requirements and having the skills and abilities to proficiently apply that knowledge on GAGAS engagements. CPE contributes to auditors' competence. The requirements of this chapter are intended to be followed in conjunction with all other applicable GAGAS requirements.

## Competence

### Requirements: General

**4.02** The audit organization's management must assign auditors to conduct the engagement who before beginning work on the engagement collectively possess the competence needed to address the engagement objectives and perform their work in accordance with GAGAS.

**4.03** The audit organization's management must assign auditors who before beginning work on the engagement possess the competence needed for their assigned roles.

**4.04** The audit organization should have a process for recruitment, hiring, continuous development, assignment, and evaluation of personnel so that the workforce has the essential knowledge, skills, and abilities necessary to conduct the engagement. The nature, extent, and formality of the process will depend on various factors, such as the size of the audit organization, its structure, and its work.

### Application Guidance: General

**4.05** Competence is the knowledge, skills, and abilities, obtained from education and experience, necessary to conduct the GAGAS engagement. Competence enables auditors to make sound professional judgments. Competence includes possessing the technical knowledge and skills necessary for the assigned role and the type of work being done. This includes possessing specific knowledge about GAGAS.

**4.06** Competence is derived from a combination of education and experience. Education is a structured and systematic process aimed at developing knowledge, skills, and other abilities; it is a process that is

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typically but not exclusively conducted in academic or learning environments. Experience refers to workplace activities that are relevant to developing professional proficiency. Competence is not necessarily measured by years of auditing experience because such a quantitative measurement may not accurately reflect the kinds of experiences gained by auditors in any given time period. Maintaining competence through a commitment to learning and development throughout auditors' professional lives is an important element for auditors.

### **Application Guidance: Indicators of Competence**

#### *Technical Knowledge and Skills*

**4.07** The knowledge, skills, and abilities needed when conducting an engagement in accordance with GAGAS include the understanding necessary to proficiently apply

- a. GAGAS;
- b. standards, statutory requirements, regulations, criteria, and guidance applicable to auditing or the objectives for the engagement(s) being conducted; and
- c. techniques, tools, and guidance related to professional expertise applicable to the work being performed.

Auditor proficiency in these areas helps ensure that engagements are conducted in accordance with GAGAS.

**4.08** Achieving the knowledge, skills, and abilities needed to conduct a GAGAS engagement may include

- a. having prior experience in the subject matter or type of engagement;
- b. completing CPE related to the subject matter or type of engagement; and
- c. obtaining degrees or certifications relevant to the subject matter or type of engagement.

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### *Competence for Assigned Roles*

**4.09** The audit organization and engagement teams may consider the levels of proficiency needed for each role on the engagement when assigning auditors to the engagement.

**4.10** Roles on the engagement generally include the following:

- a.** Nonsupervisory auditors: Auditors in these roles plan or perform engagement procedures. Work situations for these auditors are characterized by low levels of ambiguity, complexity, and uncertainty. The nonsupervisory auditor role necessitates at least a basic level of proficiency.
- b.** Supervisory auditors: Auditors in these roles plan engagements, perform engagement procedures, or direct engagements. Work situations for these auditors are characterized by moderate levels of ambiguity, complexity, and uncertainty. The supervisory auditor role necessitates at least an intermediate level of proficiency.
- c.** Partners and directors: Auditors in these roles plan engagements, perform engagement procedures, or direct or report on engagements. Partners and directors may also be responsible for reviewing engagement quality prior to issuing the report, for signing the report, or both. Work situations for these auditors are characterized by high levels of ambiguity, complexity, and uncertainty. The partner and director role necessitates an advanced level of proficiency.

**4.11** Definitions of key terms follow:

- a.** Planning: Determining engagement objectives, scope, and methodology; establishing criteria to evaluate matters subject to audit; or coordinating the work of the other audit organizations. This definition excludes auditors whose role is limited to gathering information used in planning the engagement.
- b.** Directing: Supervising the efforts of others who are involved in accomplishing the objectives of the engagement or reviewing engagement work to determine whether those objectives have been accomplished.

- c. Performing engagement procedures: Performing tests and procedures necessary to accomplish the engagement objectives in accordance with GAGAS.
- d. Reporting: Determining the report content and substance or reviewing reports to determine whether the engagement objectives have been accomplished and the evidence supports the report's technical content and substance prior to issuance. This includes signing the report.

**Requirement: Specialists**

**4.12** The engagement team should determine that specialists assisting the engagement team on a GAGAS engagement are qualified and competent in their areas of specialization.

**Application Guidance: Specialists**

**4.13** Some engagements may necessitate the use of specialized techniques or methods that call for the skills of specialists. Specialists do not include individuals with special skill or knowledge related to specialized areas within the field of accounting or auditing, such as income taxation and information technology. Such individuals are considered auditors.

**4.14** The competence and qualifications of specialists significantly affect whether their work will be adequate for the engagement team's purposes and will meet GAGAS requirements. Competence of specialists relates to the nature and level of expertise. Qualifications of specialists relate to their professional certifications, reputations, and previous work in the subject matter. Other relevant factors include the ability of specialists to exercise competence in the circumstances of the engagement and the effects that bias, conflict of interest, or the influence of others may have on the specialists' professional judgment.

**4.15** Sources that may inform the auditors' assessment of the competence and professional qualifications of a specialist include the following:

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



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- 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;
- d. the auditors’ assessment of the specialist’s knowledge and qualification based on prior experience in using the specialist’s work;
- e. the specialist’s knowledge of any technical performance standards or other professional or industry requirements in the specialist’s field (for example, ethical standards and other membership requirements of a professional body or industry association, accreditation standards of a licensing body, or requirements imposed by law or regulation);
- f. the knowledge of the specialist with respect to relevant auditing standards; and
- g. the assessment of unexpected events, changes in conditions, or the evidence obtained from the results of engagement procedures that indicate it may be necessary to reconsider the initial evaluation of the competence and qualifications of a specialist as the engagement progresses.

**Continuing Professional Education**

**Requirements: General**

**4.16** Auditors who plan, direct, perform engagement procedures for, or report on an engagement conducted in accordance with GAGAS should develop and maintain their professional competence by completing at least 80 hours of CPE in every 2-year period as follows.

<b>CPE hours</b>	<b>Subject matter categories of CPE</b>
24 hours	Subject matter directly related to the government environment, government auditing, or the specific or unique environment in which the audited entity operates
56 hours	Subject matter that directly enhance auditors’ professional expertise to conduct engagements

**4.17** Auditors should complete at least 20 hours of CPE in each year of the 2-year periods.

**4.18** The audit organization should maintain documentation of each auditor's CPE.<sup>24</sup>

#### **Application Guidance: General**

**4.19** The continuing competence of the audit organization's personnel depends, in part, on an appropriate level of CPE so that auditors maintain the knowledge, skills, and abilities necessary to conduct the GAGAS engagement. Obtaining CPE specifically on GAGAS, particularly during years in which there are revisions to the standards, may assist auditors in maintaining the competence necessary to conduct GAGAS engagements.

**4.20** CPE used to fulfill the 24-hour requirement may be taken at any time during the 2-year measurement period.

#### **Application Guidance: Subject Matter Categories of CPE**

**4.21** Determining what subjects are appropriate for individual auditors to satisfy the CPE requirements is a matter of professional judgment to be exercised by auditors in consultation with appropriate officials in their audit organization. When determining what specific subjects qualify for the CPE requirement, the auditors may consider the types of knowledge, skills, and abilities, and the level of proficiency necessary, in order to be competent for their assigned roles. Auditors may consider probable future engagements to which they may be assigned when selecting specific CPE subjects to satisfy the 24-hour and the 56-hour CPE requirements. The audit organization is ultimately responsible for determining whether a subject or topic qualifies as acceptable for its auditors.

**4.22** The subject matter categories for the 24-hour requirement may be used to satisfy the 56-hour CPE requirement. If CPE in any of the subject matter and topics that would satisfy the 56-hour requirement, as discussed in paragraph 4.24, is tailored specifically to the government environment, such CPE may qualify toward satisfying the 24-hour

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<sup>24</sup>See para. 4.51 for a discussion of CPE documentation.

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requirement. Examples of CPE subjects that may qualify for each of the categories are listed below.

*Subject Matter Directly Related to the Government Environment, Government Auditing, or the Specific or Unique Environment in Which the Audited Entity Operates (24-Hour Requirement)*

**4.23** Subject matter directly related to the government environment, government auditing, or the specific or unique environment in which the audited entity operates may include, but is not limited to, the following:

- a. generally accepted government auditing standards (GAGAS) and related topics, such as internal control as addressed in GAGAS;
- b. the applicable American Institute of Certified Public Accountants' (AICPA) Statements on Auditing Standards;<sup>25</sup>
- c. the applicable AICPA Statements on Standards for Attestation Engagements and Statements on Standards for Accounting and Review Services;<sup>26</sup>
- d. the applicable auditing standards issued by the Institute of Internal Auditors, the Public Company Accounting and Oversight Board, the International Auditing and Assurance Standards Board, or other auditing standard-setting body;
- e. U.S. generally accepted accounting principles, or the applicable financial reporting framework being used, such as those issued by the Federal Accounting Standards Advisory Board, the Governmental Accounting Standards Board, or the Financial Accounting Standards Board;
- f. *Standards for Internal Control in the Federal Government*;<sup>27</sup>

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<sup>25</sup>See para. 6.01 for a discussion of the AICPA standards incorporated into GAGAS for financial audits.

<sup>26</sup>See para. 7.01 for a discussion of the AICPA standards incorporated into GAGAS for attestation engagements and reviews of financial statements.

<sup>27</sup>GAO, *Standards for Internal Control in the Federal Government*, [GAO-14-704G](#) (Washington, D.C.: September 2014).

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- g.** *Internal Control—Integrated Framework*,<sup>28</sup> as applicable;
  - h.** requirements for recipients of federal contracts or grants, such as Single Audits under the *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards*;<sup>29</sup>
  - i.** requirements for federal, state, or local program audits;
  - j.** relevant or applicable audit standards or guides, including those for information technology auditing and forensic auditing;
  - k.** information technology auditing topics applicable to the government environment;
  - l.** fraud topics applicable to a government environment;
  - m.** statutory requirements, regulations, criteria, guidance, trends, risks, or topics relevant to the specific and unique environment in which the audited entity operates;
  - n.** statutory requirements, regulations, criteria, guidance, trends, risks, or topics relevant to the subject matter of the engagement, such as scientific, medical, environmental, educational, or any other specialized subject matter;
  - o.** topics directly related to the government environment, such as the nature of government (structures, financing, and operations), economic or other conditions and pressures facing governments, common government financial management issues, appropriations, measurement or evaluation of government financial or program performance, and application of general audit methodologies or techniques to a government environment or program;

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<sup>28</sup>Committee of Sponsoring Organizations of the Treadway Commission, *Internal Control—Integrated Framework* (New York: American Institute of Certified Public Accountants, 2013).

<sup>29</sup>See Part 200, Subpart F, of Title 2, *Code of Federal Regulations*.

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- p. specialized audit methodologies or analytical techniques, such as the use of complex survey instruments, actuarial estimates, statistical analysis tests, or statistical or nonstatistical sampling;
- q. performance auditing topics, such as obtaining evidence, professional skepticism, and other applicable audit skills;<sup>30</sup>
- r. government ethics and independence;
- s. partnerships between governments, businesses, and citizens;
- t. legislative policies and procedures;
- u. topics related to fraud, waste, abuse, or improper payments affecting government entities; and
- v. compliance with laws and regulations.

*Subject Matter That Directly Enhances Auditors' Professional Expertise to Conduct Engagements (56-Hour Requirement)*

**4.24** Subject matter that directly enhances auditors' professional expertise to conduct engagements may include, but is not limited to, the following:

- a. subject matter categories for the 24-hour requirement listed in paragraph 4.23;
- b. general ethics and independence;
- c. topics related to accounting, acquisitions management, asset management, budgeting, cash management, contracting, data analysis, program performance, or procurement;
- d. communicating clearly and effectively, both orally and in writing;
- e. managing time and resources;
- f. leadership;

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<sup>30</sup>See chs. 8 and 9 for performance audit topics that may be included.

- g. software applications used in conducting engagements;
- h. information technology; and
- i. economics, human capital management, social and political sciences, and other academic disciplines that may be applied in engagements, as applicable.

#### **Application Guidance: Exemptions and Exceptions**

**4.25** Auditors may be exempted from the 56-hour CPE requirement by the audit organization, but not the 24-hour requirement, if they

- a. charge less than 20 percent of their time annually to engagements conducted in accordance with GAGAS and
- b. are only involved in performing engagement procedures, but not involved in planning, directing, or reporting on the engagement.

The 20 percent may be based on historical or estimated charges in a year, provided that the audit organization has a basis for this determination and monitors actual time. For auditors who change status such that they are charging more than 20 percent of their time annually to engagements under GAGAS, the audit organization may prorate the required CPE hours similar to when auditors are assigned to GAGAS engagements after the beginning of a 2-year CPE measurement period, as discussed in paragraph 4.42.

**4.26** Nonsupervisory auditors who charge less than 40 hours of their time annually to engagements conducted in accordance with GAGAS may be exempted by the organization from all CPE requirements in paragraph 4.16.

**4.27** The audit organization may exempt from the CPE requirements college and university students employed on a temporary basis for a limited period of time (for example, an internship of limited duration) or enrolled in a formal program sponsored by the college or university for a specific period of employment, such as a term or semester.

**4.28** Employees or contract employees performing support services within the audit organization, such as individuals who are assigned to positions in budgeting, human resources, training, and administrative functions, and who do not conduct engagement activities are not auditors

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subject to the GAGAS CPE requirements. Employees or contract employees who assist in the engagement by performing support services, such as performing background research, data entry, writing and editing assistance, proofreading, or report production and distribution are not auditors subject to the GAGAS CPE requirements.

**4.29** The audit organization, at its discretion, may grant exemptions from a portion of the CPE requirement in the event of extended absences or other extenuating circumstances if situations such as the following prevent auditors from fulfilling those requirements and conducting engagements:

- a. ill health,
- b. maternity or paternity leave,
- c. extended family leave,
- d. sabbaticals,
- e. leave without pay absences,
- f. foreign residency,
- g. military service, and
- h. disasters.

The audit organization may not grant exceptions for reasons such as workload, budget, or travel constraints.

#### **Application Guidance: Specialists**

**4.30** External specialists are not auditors subject to the GAGAS CPE requirements. Also, internal specialists assisting on a GAGAS engagement who are not involved in planning, directing, performing engagement procedures, or reporting on a GAGAS engagement are not auditors subject to the GAGAS CPE requirements.

**4.31** Internal specialists who are performing work in accordance with GAGAS as part of the engagement team—including planning, directing, performing engagement procedures, or reporting on a GAGAS engagement—are considered auditors and are subject to the GAGAS

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CPE requirements. The GAGAS CPE requirements become effective for internal specialists when an audit organization first assigns an internal specialist to an engagement. Because internal specialists apply specialized knowledge in government engagements, CPE in their areas of specialization qualifies under the requirement for 24 hours of CPE that directly relates to government auditing, the government environment, or the specific or unique environment in which the audited entity operates.

**Application Guidance: Programs and Activities That Qualify for CPE**

**4.32** CPE programs are structured educational activities or programs with learning objectives designed to maintain or enhance the auditors' competence to address engagement objectives and perform work in accordance with GAGAS.

**4.33** The following are examples of structured educational programs and activities:

- a. internal training programs (e.g., courses, seminars, and workshops);
- b. education and development programs presented at conferences, conventions, meetings, and seminars and meetings or workshops of professional organizations;
- c. training programs presented by other audit organizations, educational organizations, foundations, and associations;
- d. web-based seminars and individual-study or eLearning programs;
- e. audio conferences;
- f. accredited university and college courses (credit and noncredit);
- g. standard-setting organization, professional organization, or audit organization staff meetings when a structured educational program with learning objectives is presented (e.g., the portion of the meeting that is a structured educational program with learning objectives designed to maintain or enhance auditors' competence);
- h. correspondence courses, individual-study guides, and workbooks;



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- i. serving as a speaker, panelist, instructor, or discussion leader at programs that qualify for CPE hours;
  - j. developing or technical review of courses or the course materials for programs that qualify for CPE hours; and
  - k. publishing articles and books that contribute directly to the author's professional proficiency to conduct engagements.

**4.34** Individual auditors who are members of professional organizations or who are licensed professionals, such as certified public accountants, are cautioned that the GAGAS CPE requirements, while similar in many respects to those of professional organizations and of licensing bodies, may not be identical. Some subjects and topics may be acceptable to state licensing bodies or professional organizations, but may not qualify as CPE under GAGAS. Conversely, some CPE that qualifies for GAGAS may not qualify for state licensing bodies or professional organizations. Careful consideration of auditors' relevant professional organizations or licensing body requirements is encouraged to meet other relevant CPE requirements.

**4.35** Examples of training topics that may qualify as CPE for state licensing bodies or professional organizations but would not generally qualify as CPE for purposes of satisfying requirements under GAGAS include certain training in taxation, personal financial planning and investment, taxation strategies, estate planning, retirement planning, and practice management, unless such training directly enhances the auditors' professional proficiency to perform engagements or relate to the subject matter of an engagement. However, if certain taxation or other topics relate to an objective or the subject matter of an engagement, training in those related topics could qualify as CPE under GAGAS.

**4.36** Examples of programs and activities that do not qualify for CPE hours under GAGAS include, but are not limited to, the following:

- a. on-the-job training;
- b. basic or elementary courses in subjects or topics in which auditors already have the knowledge and skills being taught;
- c. programs that are designed for general personal development, such as résumé writing, improving parent-child relations, personal investments and money management, and retirement planning;

- d. programs that demonstrate office equipment or software that is not used in conducting engagements;
- e. programs that provide training on the audit organization's administrative operations;
- f. business sessions at professional organization conferences, conventions, and meetings that do not have a structured educational program with learning objectives;
- g. conducting external quality reviews; and
- h. sitting for professional certification examinations.

Basic or elementary courses would be acceptable in cases where they are deemed necessary as “refresher” courses to enhance the auditors' proficiency to conduct audits and attestation engagements.

#### **Application Guidance: Measurement of CPE**

**4.37** A CPE hour may be granted for each 50 minutes of participation in programs and activities that qualify.

**4.38** For university or college credit courses, each unit of college credit under a semester system equals 15 CPE hours, and each unit of college credit under a quarter system equals 10 CPE hours. For university or college noncredit courses, CPE hours may be granted only for the actual classroom time.

**4.39** For individual-study programs where successful completion is measured by a summary examination, CPE credit may be granted if auditors complete the examination with a passing grade. Auditors in other individual-study programs may earn CPE hours when they satisfactorily complete the requirements of the self-study program. The number of hours granted may be based on the CPE provider's recommended number of CPE hours for the program.

**4.40** Speakers, instructors, and discussion leaders at programs that qualify for CPE and auditors who develop or write the course materials may receive CPE hours for preparation and presentation time to the extent the subject matter contributes to auditors' competence. One CPE hour may be granted for each 50 minutes of presentation time. Up to 2 CPE hours may be granted for developing, writing, or advance

preparation for each 50 minutes of the presentation. Auditors may not receive CPE hours for either preparation or presentation time for repeated presentations that they make within the 2-year period, unless the subject matter involved was changed significantly for each presentation. The maximum number of CPE hours that may be granted to an auditor as a speaker, instructor, discussion leader, or preparer of course materials may not exceed 40 hours for any 2-year period.

**4.41** Articles, books, or materials written by auditors and published on subjects and topics that contribute directly to professional proficiency to conduct engagements qualify for CPE hours in the year they are published. One CPE hour may be granted for each hour devoted to writing articles, books, or materials that are published. However, CPE hours for published writings may not exceed 20 hours for any 2-year period.

**4.42** Auditors hired or assigned to a GAGAS engagement after the beginning of an audit organization's 2-year CPE period may complete a prorated number of CPE hours. An audit organization may define a prorated number of hours based on the number of full 6-month intervals remaining in the CPE period. For example, an audit organization has a 2-year CPE period running from January 1, 2020, through December 31, 2021. The audit organization assigns a new auditor to a GAGAS engagement in May 2020. The audit organization may calculate the prorated CPE requirement for the auditor as follows:

- a. Number of full 6-month intervals remaining in the CPE period: 3
- b. Number of 6-month intervals in the full 2-year period: 4
- c. Newly assigned auditor's CPE requirement:  $\frac{3}{4} \times 80$  hours = 60 hours

When auditors are newly hired or newly assigned to GAGAS engagements and have had some previous CPE, the audit organization has flexibility and may choose between using a pro rata approach or evaluating whether and to what extent any CPE already taken in that period would satisfy GAGAS CPE requirements.

**4.43** For newly assigned auditors who are subject to the 24-hour requirement, the number of prorated hours may be calculated in a similar manner:  $\frac{3}{4} \times 24$  hours = 18 hours, in this example. The prorated amount of hours would be the total requirement over the partial period. The 20-

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hour minimum for each CPE year would not apply when the prorated number of hours is being used to cover a partial 2-year CPE period.

**4.44** At their discretion, audit organizations may give auditors who have not completed the 80-hour CPE requirement for any 2-year period up to 2 months immediately following the 2-year period to make up the deficiency. Audit organizations may also give auditors who have not completed the 20 hours of CPE in a 1-year period up to 2 months immediately following the 1-year period to make up the deficiency. Any CPE hours completed toward a deficiency in one period may be documented in the CPE records and may not be counted toward the requirements for the next period. Audit organizations that grant the 2-month grace period may not allow auditors who have not satisfied the CPE requirements after the grace period to participate in GAGAS engagements until those requirements are satisfied.

**4.45** Auditors may not carry over CPE hours earned in excess of the 80-hour and 24-hour requirements from one 2-year CPE measurement period to the next.

**4.46** If an audit organization discontinues conducting GAGAS engagements or reassigns auditors to non-GAGAS assignments before auditors complete the CPE requirements, the auditors are not required to complete the number of hours to satisfy the CPE requirements. However, the audit organization may wish to have its auditors complete those requirements if it is foreseeable that the auditors will conduct GAGAS engagements in the future.

**4.47** Auditors who complete a professional certification review course may receive CPE hours only for those segments of the review course that are relevant to the standards, statutory requirements, regulations, criteria, and guidance applicable to auditing or to the engagement objectives being performed, or for subject matter that directly enhances auditors' professional expertise to conduct engagements.

**4.48** To simplify administration of the CPE requirements, an audit organization may establish a standard 2-year period for all of its auditors, which can be on either a fixed-year or rolling-year basis. A fixed-year measurement period, for example, would be the 2-year periods 2019 through 2020, 2021 through 2022, and so forth, while a rolling-year measurement period would be 2019 through 2020, 2020 through 2021, 2021 through 2022, and so forth.

**4.49** An audit organization may use a measurement date other than the date it started its first GAGAS engagement, or the audit organization may choose to change its measurement date to coincide with a fiscal year or another reporting requirement, such as one established by a state licensing body or professional organization. For example, if an audit organization changes the end date of the measurement period from December 31 to June 30, during the audit organization's transition period (January 1 to June 30), its auditors may complete at least a prorated number of CPE hours for the 6-month transition period. The number of prorated hours required may be calculated using the method illustrated in paragraphs 4.42 and 4.43.

**Application Guidance: Monitoring CPE**

**4.50** The audit organization's policies and procedures for CPE may address the following:

- a. identifying all auditors required to meet the CPE requirements;
- b. providing auditors with the opportunity to attend internal CPE programs, external CPE programs, or both;
- c. assisting auditors in determining which programs, activities, and subjects qualify for CPE;
- d. documenting the number of CPE hours completed by each auditor; and
- e. monitoring auditor compliance with the CPE requirements to ensure that auditors complete sufficient CPE in qualifying programs and subjects.

**4.51** Policies and procedures for documentation may address maintaining documentation of the CPE hours completed by each auditor subject to the CPE requirements for an appropriate period of time to satisfy any legal and administrative requirements, including peer review. The audit organization may maintain documentation of CPE or may delegate the responsibility to the auditor and put in place adequate procedures to ensure that its records of CPE hours earned by auditors are supported by the documentation maintained by auditors. Documentation may include the following information:

- a. the name of the organization providing the CPE;

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- b. the title of the training program, including the subject matter or field of study;
- c. the dates attended for group programs or dates completed for individual study programs;
- d. the number of CPE hours earned toward the 56-hour and 24-hour requirements;
- e. any reasons for specific exceptions granted to the CPE requirement; and
- f. evidence of completion of CPE, such as a certificate or other evidence of completion from the CPE provider for group and individual-study programs, if provided; documentation of CPE courses presented or copies of course materials developed by or for speakers, instructors, or discussion leaders, along with a written statement supporting the number of CPE hours claimed; or a copy of the published book, article, or other material that name the writer as author or contributor, or a written statement from the writer supporting the number of CPE hours claimed.

**4.52** The audit organization may monitor CPE compliance through its internal inspections or other quality management monitoring activities.

**4.53** The audit organization is not required to prepare reports on CPE. However, the audit organization may consider preparing a periodic CPE report for distribution to the auditors or maintaining or accessing training data online to monitor its auditors' progress toward meeting the CPE requirements.

# Chapter 5: Quality Management, Engagement Quality Reviews, and Peer Review

**5.01** This chapter addresses the audit organization's responsibilities for designing, implementing, and operating a system of quality management for engagements conducted in accordance with generally accepted government auditing standards (GAGAS).<sup>31</sup> It includes requirements and application guidance for engagement quality reviews that the audit organization may use as a response to one or more quality risks relating to quality management. Finally, the chapter addresses the audit organization's responsibilities for administering, planning, performing, and reporting on peer reviews of audit organizations that conduct engagements in accordance with GAGAS. The requirements of this chapter are intended to be followed in conjunction with all other applicable GAGAS requirements.

## System of Quality Management

**5.02** The objective of a system of quality management for engagements performed in accordance with GAGAS is to provide the audit organization with reasonable assurance that the audit organization and its personnel

- a. fulfill their responsibilities in accordance with professional standards and applicable laws and regulations and
- b. perform and report on engagements in accordance with such standards and requirements.

**5.03** In GAGAS, a system of quality management consists of the following components: governance and leadership; independence, legal, and ethical requirements; acceptance, initiation, and continuance of engagements; engagement performance; resources; and information and communication. It also includes two components that are processes. The risk assessment process includes assessing and responding to risks to achieving the quality objectives. The monitoring and remediation process includes (1) providing relevant, reliable, and timely information about the design, implementation, and operation of the system of quality management; (2) taking appropriate actions to respond to and remediate identified deficiencies in the system of quality management; and (3) enabling the audit organization to assess compliance with professional standards and with policies and procedures it has established to address quality risks.

<sup>31</sup>The system of quality management applies to financial audits, attestation engagements, reviews of financial statements, and performance audits conducted in accordance with GAGAS (see para. 1.27h).

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Quality Reviews, and Peer Review**

**5.04** GAGAS establishes a risk-based approach to designing, implementing, and operating the system of quality management in an interconnected and coordinated manner. This risk-based approach involves the following:

- a. establishing the desired outcomes relative to the components of the system of quality management (referred to as quality objectives);
- b. identifying and assessing risks to achieving the quality objectives (referred to as quality risks); and
- c. designing and implementing responses to address quality risks.

**Requirements: System of Quality Management**

**5.05** An audit organization conducting engagements in accordance with GAGAS must design, implement, and operate a system of quality management that provides it with reasonable assurance that the audit organization and its personnel

- a. fulfill their responsibilities in accordance with professional standards and applicable laws and regulations and
- b. perform and report on engagements in accordance with such standards and requirements.

**5.06** Government audit organizations should comply with the GAGAS quality management requirements in paragraphs 5.05 through 5.138 and, if applicable, engagement quality review requirements in paragraphs 5.139 through 5.154. Nongovernment audit organizations not subject to the quality management standards of one of the recognized organizations in paragraph 5.07 should comply with the GAGAS quality management requirements in paragraphs 5.05 through 5.138 and, if applicable, engagement quality review requirements in paragraphs 5.139 through 5.154.

**5.07** A nongovernment audit organization subject to the quality management standards of one of the following recognized organizations should comply with the respective organization's quality management requirements and the requirements of paragraphs 5.55c, 5.55d, and 5.74c:



- a. American Institute of Certified Public Accountants (AICPA)
- b. International Auditing and Assurance Standards Board
- c. Public Company Accounting Oversight Board

**5.08** The audit organization should exercise professional judgment in designing, implementing, and operating a system of quality management, taking into account the nature and circumstances of the audit organization and its engagements.

### **Application Guidance: System of Quality Management**

**5.09** The public interest is served by the consistent performance of quality engagements.<sup>32</sup> The design, implementation, and operation of the system of quality management enable the consistent performance of quality engagements by providing the audit organization with reasonable assurance that the objective of the system of quality management, stated in paragraph 5.02, is achieved. An audit organization obtains reasonable assurance when the system of quality management reduces to an acceptably low level the risk that the objective stated in paragraph 5.02 is not achieved.

**5.10** Quality management is not a separate function of the audit organization; it is the integration of a culture that demonstrates a commitment to quality with the audit organization's strategy, operational activities, and business processes. Designing the system of quality management and the audit organization's operational activities and business processes in an integrated manner promotes a harmonious approach to managing the audit organization and enhances the effectiveness of quality management.

**5.11** Audit organizations may be required or may elect to use GAGAS quality management standards. Nongovernment audit organizations, such as certified public accounting firms, may be subject to or required to follow the quality management standards of one of the recognized organizations in paragraph 5.07. Those audit organizations follow the standards of the recognized organizations and the specific additional

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<sup>32</sup>See paras. 3.07 and 3.08 for additional guidance on the public interest.

GAGAS requirements in paragraph 5.07 to avoid maintaining separate systems of quality management.

### *Scalability Considerations*

**5.12** The design of the audit organization's system of quality management, particularly the complexity and formality of the system, will vary based on the nature and circumstances of the audit organization (such as size, number of offices and geographic dispersion, knowledge and experience of its personnel, and cost-benefit considerations), and the nature and circumstances of its engagements. For example, an audit organization that conducts various types of GAGAS engagements for federal, state, and local governments may need a more complex and formalized system of quality management and supporting documentation than one that conducts performance audits of a single small government entity. Similarly, a large audit organization with multiple divisions and offices may need a more complex and formal system of quality management than a small audit organization with a few auditors at a single location.

## Responsibility for the System of Quality Management

### **Requirements: Responsibility for the System of Quality Management**

**5.13** The audit organization should assign

- a. responsibility and accountability for the system of quality management to a senior-level official within the audit organization and
- b. operational responsibility for the system of quality management or specific aspects of the system of quality management to a specific individual or individuals.

**5.14** The audit organization should determine that the individual or individuals in paragraph 5.13

- a. possess the appropriate experience, knowledge, influence, and authority within the audit organization;
- b. have sufficient time and resources to fulfill the assigned responsibility;
- c. have a sufficient understanding of this chapter and other applicable GAGAS requirements, as well as application guidance

and other explanatory material, to understand the objectives of the system of quality management and to apply the related requirements properly; and

- d. understand the assigned roles and are held accountable for fulfilling them.

**5.15** The audit organization should determine that those assigned operational responsibility for the system of quality management or aspects of the system of quality management are in direct communication with the senior-level official assigned responsibility and accountability for the system of quality management.

#### **Application Guidance: Responsibility for the System of Quality Management**

**5.16** Notwithstanding the assignment of responsibilities related to the system of quality management in accordance with paragraph 5.13, the audit organization remains ultimately responsible for the system of quality management and for holding individuals responsible and accountable for their assigned roles. Further, the audit organization is responsible for its system of quality management even when it uses resources from a service provider.<sup>33</sup>

**5.17** The manner in which an audit organization assigns and describes roles, responsibilities, and authority may vary. Laws and regulations may impose requirements for an audit organization that may affect the structure of leadership and management and their assigned responsibilities. As such, professional judgment assists an audit organization in identifying the appropriate individual or individuals to whom to assign the responsibilities described in paragraph 5.13.

**5.18** Delegating operational responsibility for the system of quality management or aspects of the system of quality management may depend on the size and complexity of the audit organization. For small or less complex audit organizations, the senior-level official responsible and accountable for the system of quality management may also be assigned operational responsibility for the system of quality management. For large or more complex audit organizations, more than one person may be

<sup>33</sup>See para. 5.79 for the definition of a service provider.

assigned operational responsibility for the system of quality management or aspects of the system of quality management. For example, operational responsibility for aspects of a system of quality management that could be delegated include

- a. compliance with independence requirements,
- b. compliance with continuing professional education requirements,
- c. compliance with professional standards, and
- d. the monitoring and remediation process.

## Quality Management Risk Assessment Process

### Requirements: Quality Management Risk Assessment Process

**5.19** The audit organization should design and implement a risk assessment process that establishes quality objectives, identifies and assesses quality risks, and designs and implements responses to address the quality risks.

**5.20** The audit organization should establish the quality objectives specified by this chapter. The audit organization should also establish any additional quality objectives that the audit organization considers necessary to achieve the objective of the system of quality management.

**5.21** The audit organization should identify and assess quality risks. To identify and assess quality risks, the audit organization should

- a. obtain an understanding of the conditions, events, circumstances, actions, or inactions that may adversely affect the achievement of the quality objectives and
- b. consider how, and the degree to which, the conditions, events, circumstances, actions, or inactions may adversely affect the achievement of the quality objectives.

**5.22** The audit organization should design and implement responses to address the quality risks.

**5.23** The audit organization should identify, analyze, and respond to changes in the nature and circumstances of the audit organization or its

engagements that could affect the quality objectives, quality risks, or responses to address quality risks.

### **Application Guidance: Quality Management Risk Assessment Process**

**5.24** Establishing quality objectives, identifying and assessing quality risks, and designing and implementing responses is an iterative process.

**5.25** An audit organization typically performs a quality management risk assessment

- a. at specific periodic intervals, such as annually;
- b. to respond to deficiencies in the system of quality management identified by the monitoring and remediation process; and
- c. as necessary to respond to changes in the nature and circumstances of the audit organization, its engagements, or both.

**5.26** An example of a change in the nature and circumstances of the audit organization includes when the audit organization has a change in its organizational structure or size.

**5.27** Examples of changes in the nature and circumstances of an audit organization's engagements include the following:

- a. When a local government audit organization conducts audits of new state-provided emergency funding that requires additional audit procedures and the issuance of specialized reports.
- b. When a change to an audited entity's operations or programs subject to audit necessitates the use of specialized techniques or methods that require the skills of a specialist.
- c. When an audit organization that solely conducted performance audits begins to conduct both financial and performance audits.

**5.28** Appropriate responses to changes in the nature and circumstances of the audit organization or its engagements could include establishing

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additional quality objectives, quality risks, or responses to address quality risks; updating existing quality risks or responses to address quality risks; or determining that no changes are needed.

### *Quality Objectives*

**5.29** Quality objectives are the desired outcomes to be achieved by the audit organization in relation to the components of the system of quality management.

**5.30** The quality objectives specified by this chapter relate to the following components:

- a. Governance and Leadership (5.45)
- b. Independence, Legal, and Ethical Requirements (5.47)
- c. Acceptance, Initiation, and Continuance of Engagements (5.51)
- d. Engagement Performance (5.54)
- e. Resources (5.74)
- f. Information and Communication (5.81)

**5.31** There are no quality objectives for the quality management risk assessment process and the monitoring and remediation process.

**5.32** The audit organization may identify additional quality objectives beyond those specified by this chapter that it determines are necessary to achieve the objective of the system of quality management. For instance, laws, regulations, contracts, grant agreements, or professional standards may establish requirements that give rise to additional quality objectives. The audit organization may also determine that additional quality objectives previously established are no longer necessary or need to be modified.

**5.33** The need to establish additional quality objectives is not expected to be common. Therefore, not all audit organizations will find it necessary to establish quality objectives beyond those specified in this chapter.

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*Quality Risks*

**5.34** Quality risks are risks that have a reasonable possibility of

- a. occurring and
- b. adversely affecting the achievement of one or more quality objectives individually or in combination with other risks.

**5.35** A risk arises from how, and the degree to which, a condition, event, circumstance, action, or inaction may adversely affect the achievement of a quality objective. Not all risks to achieving a quality objective meet the definition of a quality risk. Professional judgment assists the audit organization in determining whether a risk is a quality risk.

**5.36** Conditions, events, circumstances, actions, or inactions that may adversely affect the achievement of the quality objectives may be related to the nature and circumstances of the audit organization. These may include

- a. the complexity and operating characteristics of the audit organization;
- b. the strategic and operational decisions and actions of the audit organization;
- c. the characteristics and management style of leadership;
- d. the resources of the audit organization, including those provided by service providers; and
- e. law, regulation, professional standards, and the environment in which the audit organization operates.

**5.37** Conditions, events, circumstances, actions, or inactions that may adversely affect the achievement of the quality objectives may relate to the nature and circumstances of the engagements that the audit organization performs. These may include

- a. the types of engagements performed by the audit organization and the reports to be issued and

- b. the types of entities for which and upon which such engagements are undertaken.

**5.38** The degree to which a risk, individually or in combination with other risks, may adversely affect the achievement of one or more quality objectives may vary based on the conditions, events, circumstances, actions, or inactions giving rise to the risk, taking matters such as the following into account:

- a. how the condition, event, circumstance, action, or inaction would affect the achievement of the quality objective(s);
- b. how frequently the condition, event, circumstance, action, or inaction is expected to occur;
- c. how long it would take after the condition, event, circumstance, action, or inaction occurred for it to have an effect, and whether in that time the audit organization would have an opportunity to respond to mitigate its effect; and
- d. how long the condition, event, circumstance, action, or inaction would affect the achievement of the quality objective(s) once it has occurred.

**5.39** The assessment of quality risks may include formal ratings or scores, although audit organizations are not required to use them.

### *Responses*

**5.40** Responses are the policies and procedures that the audit organization designs and implements to address one or more quality risks.

**5.41** The audit organization is not required to design and implement a response to an identified risk for a specific quality objective unless the risk rises to the level of a quality risk.

**5.42** The nature, timing, and extent of the responses to address quality risks are based on the assessments of those risks, that is, the conclusions drawn from considering how, and the degree to which, conditions, events, circumstances, actions, or inactions may adversely affect the achievement of one or more quality objectives.



**5.43** Given the evolving nature of the system of quality management, the responses that the audit organization designs and implements may give rise to conditions, events, circumstances, actions, or inactions that result in further quality risks.

**5.44** The responses that the audit organization designs and implements may operate at various levels within the audit organization. Such levels may include the entity, division or unit, and engagement level or a combination of actions taken at various levels.

## Governance and Leadership

### Requirement: Governance and Leadership

**5.45** The audit organization should establish quality objectives that address its governance and leadership as follows:

- a. The audit organization demonstrates a commitment to quality through a culture that exists throughout the audit organization.
- b. Leadership is responsible and accountable for quality.
- c. Leadership demonstrates a commitment to quality through its actions and behaviors.
- d. The organizational structure and assignment of roles, responsibilities, and authority are appropriate to enable the design, implementation, and operation of the audit organization's system of quality management.
- e. Resource needs are planned for, obtained, allocated, and assigned in a manner consistent with the audit organization's commitment to quality.

### Application Guidance: Governance and Leadership

**5.46** Demonstrating a commitment to quality through a culture that exists throughout the audit organization may include recognizing and reinforcing the following:

- a. the audit organization's role in serving the public interest by consistently performing quality engagements;
- b. the importance of professional ethics, values, and attitudes;

- c. the responsibility of all personnel for quality in performing engagements or activities within the system of quality management and their expected behavior; and
- d. the importance of quality in the audit organization's strategic decisions and actions.

## Independence, Legal, and Ethical Requirements

### Requirements: Independence, Legal, and Ethical Requirements

**5.47** The audit organization should establish the following quality objectives that address fulfilling responsibilities in accordance with independence and legal and ethical requirements relevant to performing GAGAS engagements:

- a. The audit organization and its personnel
  - (1) understand the independence and legal and ethical requirements to which the audit organization and its engagements are subject and
  - (2) fulfill their responsibilities in relation to the independence and legal and ethical requirements to which the audit organization and its engagements are subject.<sup>34</sup>
- b. Service providers who are subject to the independence and legal and ethical requirements to which the audit organization and its engagements are subject
  - (1) understand the independence and legal and ethical requirements that apply to them and
  - (2) fulfill their responsibilities in relation to the independence and legal and ethical requirements that apply to them.

**5.48** The audit organization should

- a. establish policies and procedures for identifying, evaluating, and addressing threats to compliance with independence requirements and applicable legal and ethical requirements and appropriately responding to the causes and consequences of any breaches of these requirements and

<sup>34</sup>See paras. 3.02 through 3.16 for a discussion of ethical principles and paras. 3.18 through 3.108 for independence requirements and guidance.

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| <p><b>b.</b> at least annually, obtain written affirmation of compliance with its policies and procedures on independence from all personnel required to be independent.</p> |
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### **Application Guidance: Independence, Legal, and Ethical Requirements**

**5.49** Policies and procedures pertaining to independence requirements and applicable legal and ethical requirements assist the audit organization in

- a.** communicating its independence requirements to its personnel and
- b.** identifying and evaluating circumstances and relationships that create threats to independence and taking appropriate action to eliminate those threats or reduce them to an acceptable level by applying safeguards or, if considered appropriate, withdrawing from the engagement where withdrawal is not prohibited by law or regulation.

**5.50** Written affirmation of compliance with its policies and procedures on independence from all audit organization personnel required to be independent may be in paper or electronic form. By obtaining affirmation of retrospective compliance with the audit organization's policies and procedures on independence during a specified period and taking appropriate action on information indicating noncompliance, or potential noncompliance, the audit organization demonstrates the importance that it attaches to independence and keeps the issue current for, and visible to, its personnel. An audit organization may obtain affirmation of required personnel's compliance with policies and procedures on independence more frequently than once per year. For example, affirmation may be obtained on a per-engagement basis when such engagements last less than 1 year.

## Acceptance, Initiation, and Continuance of Engagements

### **Requirement: Acceptance, Initiation, and Continuance of Engagements**

**5.51** The audit organization should establish a quality objective that addresses the acceptance, initiation, and continuance of engagements as follows:

The audit organization accepts, initiates, and continues engagements only if it

- a. complies with professional standards, independence requirements, and applicable legal and ethical requirements;
- b. acts within its legal mandate or authority; and
- c. has the capabilities, including time and resources, to do so.

### **Application Guidance: Acceptance, Initiation, and Continuance of Engagements**

**5.52** Government audit organizations may initiate engagements as a result of (1) legal mandates, (2) requests from legislative bodies or oversight bodies, and (3) audit organization discretion. In the case of legal mandates and requests, a government audit organization may be required to conduct the engagement and may not be permitted to make decisions about acceptance or continuance or to resign or withdraw from the engagement.

**5.53** An audit organization may operate with limited resources. An audit organization may consider its workload in determining whether it has the resources to perform quality engagements over the range of work. To achieve this, an audit organization may develop systems to prioritize its work in a way that considers the need to maintain quality.

## Engagement Performance

### **Requirements: Engagement Performance**

**5.54** The audit organization should establish quality objectives that address the performance of engagements as follows:

- a. Engagement teams understand and fulfill their responsibilities in

connection to engagements, including the overall responsibility of an engagement partner or director for

- (1) managing and achieving quality on the engagement and
  - (2) being sufficiently and appropriately involved throughout the engagement.
- b. The nature, timing, and extent of direction and supervision of engagement teams and review of the work performed are appropriate based on the nature and circumstances of the engagements and the resources assigned or made available to the engagement team.
  - c. Engagement teams exercise appropriate professional judgment, which includes exercising reasonable care and professional skepticism.<sup>35</sup>
  - d. Consultation on difficult or contentious matters is undertaken and, as appropriate, documented. Conclusions agreed to from the consultation are implemented and, as appropriate, documented.
  - e. Differences of opinion within the engagement team, or between the engagement team and individuals performing activities within the audit organization's system of quality management, are brought to the attention of officials at the appropriate level of the audit organization; resolved; and, as appropriate, documented.
  - f. Engagement documentation of the work performed, results obtained, and conclusions reached is assembled on a timely basis and is appropriately maintained and retained to meet the needs of the audit organization and comply with professional standards, independence requirements, and applicable legal and ethical requirements.
  - g. Audit procedures and audit reports are appropriate in the context of the engagement objectives.

**5.55** The audit organization should take the following steps:

- a. Assign responsibility to the engagement partner or director for determining that they have taken overall responsibility for managing and achieving quality on the engagement.

<sup>35</sup>See paras. 3.109 through 3.117 for a discussion of professional judgment.

- b. Assign responsibility to the engagement partner or director for determining that independence and ethical requirements have been fulfilled for each engagement prior to issuing the audit report.
- c. If an engagement is terminated before it is completed and an audit report is not issued, document the results of the work to the date of termination and why the engagement was terminated.
- d. If auditors change the engagement objectives during the engagement, document the revised engagement objectives and the reasons for the changes.
- e. Determine if an engagement quality review is an appropriate response to address one or more quality risks.<sup>36</sup>
- f. Design and implement policies and procedures that address the requirements in 5.55a through 5.55e.

### Application Guidance: Engagement Performance

**5.56** Examples of engagement supervision include the following:

- a. tracking the progress of the engagement;
- b. considering the competence of individual members of the engagement team, whether they understand their instructions, and whether the work is being carried out in accordance with the planned approach to the engagement;
- c. addressing significant findings and issues arising during the engagement, considering their significance, and modifying the planned approach appropriately; and
- d. identifying matters for consultation or consideration by engagement team members with appropriate levels of skill and proficiency in auditing, specialists, or both during the engagement.

**5.57** A review of the work performed may include determining whether

<sup>36</sup>See paras. 5.139 through 5.154 for requirements and application guidance on performing engagement quality reviews.

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- a. the work has been performed in accordance with professional standards and applicable laws and regulations;
- b. significant findings and issues have been raised for further consideration;
- c. appropriate consultations have taken place and the resulting conclusions have been documented and implemented;
- d. the nature, timing, and extent of the work performed are appropriate and without need for revision;
- e. the work performed supports the conclusions reached and is appropriately documented;
- f. the evidence obtained is sufficient and appropriate to support the report; and
- g. the objectives of the engagement procedures have been achieved.

**5.58** When an audit organization consists of a single auditor, the requirement for an engagement team member to review work performed by other team members may be achieved through alternative procedures.

**5.59** Consultation involves a discussion at the appropriate professional level with individuals within or outside the audit organization who have specialized expertise.

**5.60** Consultation uses appropriate research, as well as the collective experience and technical expertise of the audit organization. Consultation helps promote quality and improves the application of professional judgment.

**5.61** Effective consultation on technical, ethical, and other matters within the audit organization or, when applicable, outside the audit organization can be achieved when

- a. those consulted are given all the relevant facts that will enable them to provide informed advice;
- b. those consulted have appropriate knowledge, authority, and experience; and

- 
- c. conclusions resulting from consultations are appropriately documented and implemented.

**5.62** Difficult or contentious matters on which consultation is needed may be specified by the audit organization, or the engagement team may identify matters that require consultation. The audit organization may also specify how conclusions should be agreed upon and implemented.

**5.63** The audit organization may encourage identifying differences of opinion at an early stage and may specify the steps to be taken in raising and dealing with them, including how the matter is to be resolved and how the related conclusions should be implemented and documented.

**5.64** The appropriate level of official to whom differences of opinion are raised may vary. For example, a partner or director may be an appropriate level of official to resolve differences of opinion in the engagement team. The senior-level official assigned accountability and responsibility for the system of quality management may be an appropriate level of official to resolve differences of opinion between the engagement team and individuals performing activities within the audit organization's system of quality management.

**5.65** Law, regulation, or professional standards may prescribe the time frames in which the assembly of final engagement files for specific types of engagements is to be completed.

**5.66** Whether engagement documentation is in paper, electronic, or other form, 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.

**5.67** Law, regulation, or professional standards may prescribe the retention periods for engagement documentation. If the retention periods are not prescribed, the audit organization may consider the nature of the engagements that it performs and its circumstances.

**5.68** The engagement partner or director takes overall responsibility for managing and achieving quality by being sufficiently and appropriately involved throughout the engagement. This enables the engagement partner or director to have a basis for determining that the significant judgments made and conclusions reached are appropriate given the nature and circumstances of the engagement.



**5.69** Determining whether and how to communicate the reason for terminating an engagement or changing the engagement objectives to those charged with governance, appropriate officials of the audited 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.

**5.70** An engagement quality review is an objective evaluation of the engagement team's significant judgments and the conclusions reached thereon that the engagement quality reviewer performs and completes before the audit report is released.

**5.71** The audit organization may determine that an engagement quality review is appropriate for all GAGAS engagements, specific types of GAGAS engagements, or specifically identified GAGAS engagements. The audit organization may determine that engagement quality reviews are not necessary to address quality risks.

**5.72** Criteria that an audit organization establishes to determine if an engagement quality review is appropriate may relate to the types of engagements that the audit organization performs and the types of entities for which it undertakes engagements. Examples of conditions, events, circumstances, actions, or inactions that could create quality risks for which an engagement quality review may be an appropriate response include

- a. engagements that involve a high level of complexity or judgment, such as performance audits that are highly technical in nature and financial audits for entities with significant accounting estimates with a high degree of estimation uncertainty;
- b. engagements on which issues have been encountered, such as recurring inspection findings;
- c. entities that hold a significant amount of assets in a fiduciary capacity for a large number of stakeholders;
- d. audited entities with deficiencies in internal control that are significant within the context of the engagement objectives;
- e. for financial audits, audited entities with material restatements in their financial statements; and

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- f. performance audits involving controversial or contentious subject matters or high-risk engagements.

**5.73** The audit organization's responses to address quality risks may include other forms of review that are not engagement quality reviews.

## Resources

### **Requirement: Resources**

**5.74** The audit organization should establish quality objectives that address appropriately obtaining, developing, using, maintaining, allocating, and assigning resources in a timely manner to enable the design, implementation, and operation of a system of quality management as follows:

- a. Personnel are hired, developed, and retained who have the competence and capabilities to consistently perform quality engagements and carry out responsibilities related to the operation of the audit organization's system of quality management.
- b. Personnel develop and maintain the appropriate competence to perform their roles and are held accountable or recognized for doing so through timely evaluation, compensation, promotion, and/or other incentives.
- c. Auditors who are performing work in accordance with GAGAS meet the continuing professional education (CPE) requirements.
- d. The audit organization has sufficient resources to consistently perform quality engagements and enable the operation of the audit organization's system of quality management.
- e. Individuals assigned to engagements or to perform activities within the system of quality management have appropriate competence and capabilities, including sufficient time, to perform their duties.
- f. Appropriate technological and intellectual resources are obtained or developed, implemented, maintained, and used to enable the operation of the audit organization's system of quality management and the performance of engagements.
- g. Human, technological, or intellectual resources from service providers are appropriate for use in the audit organization's system of quality management and in performing engagements.

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### Application Guidance: Resources

**5.75** The policies and procedures designed and implemented relating to hiring, developing, and retaining personnel may address issues such as the following:

- a. recruiting individuals who have, or are able to develop, appropriate competence;
- b. training programs focused on developing personnel's competence and continuing professional development;
- c. evaluation mechanisms that are undertaken at appropriate intervals and include competency areas and other performance measures; and
- d. compensation, promotion, and other incentives for all personnel, including engagement partners or directors and those assigned roles and responsibilities related to the audit organization's system of quality management.

**5.76** Effective performance evaluation, compensation, and advancement procedures are conducive to developing and maintaining competent personnel. Steps that an audit organization may take in developing and maintaining competent personnel include the following:

- a. making personnel aware of the audit organization's expectations regarding performance and ethical principles;
- b. providing personnel with an evaluation of, and counseling on, performance, progress, and career development; and
- c. helping personnel understand that compensation and advancement to positions of greater responsibility depend on, among other things, performance quality, and that failure to comply with the audit organization's policies and procedures may result in disciplinary action.

**5.77** The size and circumstances of the audit organization are important considerations in determining the structure of the audit organization's performance evaluation process. A smaller audit organization, in particular, may employ less formal methods of evaluating the performance of its personnel.

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**5.78** The audit organization may use a suitably qualified external individual or group of individuals or service provider to conduct engagement work or perform activities within the system of quality management when internal resources, for example, personnel with particular areas of technical expertise, are unavailable.

**5.79** A service provider is an individual or organization external to the audit organization that provides a human, technological or intellectual resource that the audit organization uses in its system of quality management or in performing its engagements.

**5.80** Intellectual resources include the information that the audit organization uses to enable the operation of the system of quality management and promote consistency in performing engagements. Examples of intellectual resources include written policies and procedures, methodologies, guides, standardized documentation, and access to information sources such as subscription-based databases.

**Information and  
Communication**

**Requirement: Information and Communication**

**5.81** The audit organization should establish quality objectives that address obtaining, generating, or using information regarding the system of quality management and communicating information to enable the design, implementation, and operation of the system of quality management as follows:

- a.** The audit organization's information system identifies, captures, processes, and maintains relevant and reliable information that supports the system of quality management.
- b.** Relevant and reliable information is communicated to personnel and engagement teams to enable them to understand and carry out their responsibilities within the system of quality management or engagements.
- c.** Personnel and engagement teams communicate relevant and reliable information to the audit organization when performing activities within the system of quality management or engagements.
- d.** Relevant and reliable information is communicated to external parties.

### Application Guidance: Information and Communication

**5.82** Obtaining, generating, or communicating information is generally an ongoing process that involves all personnel and encompasses disseminating information within the audit organization and externally. Information and communication are part of all components of the system of quality management.

**5.83** Relevant and reliable information includes information that is accurate, complete, timely, and valid to enable the proper functioning of the system of quality management and to support decisions regarding the system of quality management.

**5.84** The audit organization may recognize and reinforce the responsibility of personnel and engagement teams to exchange information with the audit organization and one another by establishing communication channels to facilitate communication across the audit organization.

**5.85** Laws, regulations, and professional standards may require information to be communicated externally, particularly to support external parties' understanding of the system of quality management.

#### *Scalability Considerations*

**5.86** The complexity and formality of an audit organization's mechanisms for communicating with personnel or engagement teams information relevant to the system of quality management will vary. For example, a smaller or less complex audit organization may find informal staff meetings effective for communicating with personnel or engagement teams. A larger or more complex audit organization may need formal mechanisms, such as written reports, intranet portals, or periodic official meetings, for communicating such information.

### Monitoring and Remediation Process

#### **Requirement: Monitoring and Remediation Process**

**5.87** The audit organization should establish a process to monitor the design, implementation, and operation of the system of quality management to provide a basis for identifying deficiencies and remediating them on a timely basis.

**Application Guidance: Monitoring and Remediation Process**

**5.88** Monitoring of quality is a process comprising ongoing consideration and evaluation of the audit organization's system of quality management. The purpose of monitoring is to provide management of the audit organization with reasonable assurance that (1) the policies and procedures related to the system of quality management are suitably designed and operating effectively in practice, (2) auditors have fulfilled their responsibilities in accordance with professional standards and applicable laws and regulations, and (3) auditors have performed and reported on engagements in accordance with such standards and requirements.

**5.89** In addition to enabling the evaluation of the system of quality management, the monitoring and remediation process facilitates the proactive and continual improvement of engagement quality and the system of quality management.

**Requirements: Designing and Performing Monitoring and Remediation Activities**

**5.90** The audit organization should design and perform monitoring and remediation activities to

- a. provide relevant, reliable, and timely information about the design, implementation, and operation of the system of quality management;
- b. take appropriate actions to respond to identified deficiencies so that they are remediated on a timely basis; and
- c. enable it to assess compliance with professional standards and with policies and procedures it has established to address quality risks.

**5.91** The audit organization should establish policies and procedures that address the objectivity of the individuals performing the monitoring and remediation activities and require those individuals to have sufficient competence, authority, and time to perform these activities.<sup>37</sup>

<sup>37</sup>See para. 5.106 for guidance concerning threats to objectivity and para. 5.107 for guidance relating to individuals performing self-monitoring activities.

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### **Application Guidance: Designing and Performing Monitoring and Remediation Activities**

**5.92** Monitoring is most effective when performed by persons who do not have responsibility for the specific activity being monitored.

**5.93** Monitoring activities will vary based on the audit organization's facts and circumstances.

**5.94** Monitoring activities may include the following:

- a. assessing the appropriateness of the audit organization's policies and procedures, guidance materials, and any practice aids;
- b. evaluating new developments in professional standards and applicable legal and regulatory requirements and how they are reflected in the audit organization's policies and procedures, when appropriate;
- c. reviewing written affirmation of compliance with policies and procedures on independence;
- d. inspecting engagement documentation and reports for a selection of engagements;
- e. assessing the effectiveness of staff training;
- f. evaluating decisions related to acceptance and continuance of relationships with audited entities and specific engagements; and
- g. assessing audit organization personnel's understanding of the audit organization's quality management policies and procedures and implementation thereof.

**5.95** In determining the nature, timing, and extent of the monitoring activities, the audit organization may consider the following:

- a. Quality management risk assessments
- b. The design of the responses to address quality risks

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- c. The design of the audit organization's quality management risk assessment process and monitoring and remediation process
- d. Changes to the audit organization's operating environment or in the system of quality management
- e. The results of previous monitoring activities, including whether
  - (1) previous monitoring activities continue to be relevant in evaluating the audit organization's system of quality management and
  - (2) remedial actions to address previously identified deficiencies were effective
- f. Other relevant information, including
  - (1) complaints and allegations about
    - i. failures to perform work in accordance with professional standards and applicable laws and regulations or
    - ii. noncompliance with the audit organization's policies and procedures related to the system of quality management and
  - (2) information from inspections

**5.96** The audit organization's monitoring activities may comprise a combination of ongoing monitoring activities and periodic monitoring activities. Ongoing monitoring activities are generally routine activities built into the audit organization's processes and performed on a real-time basis. Periodic monitoring activities are conducted at certain intervals by the audit organization.

**5.97** When performing monitoring activities, the audit organization may determine that changes to the nature, timing, and extent of the monitoring activities are needed, such as when findings concerning the system of quality management indicate the need for more extensive monitoring activities.

**5.98** How the audit organization's quality management risk assessment process is designed (for example, whether it is a centralized or



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decentralized process or the frequency of review) may affect the nature, timing, and extent of the monitoring activities, including those over the audit organization's quality management risk assessment process.

**5.99** Changes in the system of quality management may include

- a. changes to address an identified deficiency in the system of quality management and
- b. changes to the quality objectives, quality risks, or responses to address the quality risks resulting from changes in the nature and circumstances of the audit organization and its engagements.

**5.100** When changes in the system of quality management occur, the audit organization's previous monitoring activities may no longer provide it with information to support the evaluation of the system of quality management. Therefore, the audit organization's monitoring activities may include monitoring of those changes.

**5.101** Inspection is a retrospective evaluation of the adequacy of the audit organization's quality management policies and procedures, its personnel's understanding of those policies and procedures, and the extent of its compliance with them. The extent and nature of inspection procedures vary based on the audit organization's quality management policies and procedures and on the existence, effectiveness, and results of other monitoring activities.

**5.102** The manner in which the inspection is organized depends on many factors, such as the following:

- a. the size of the audit organization;
- b. the number and geographical location of offices;
- c. the results of previous monitoring activities;
- d. the degree of authority of both personnel and offices (for example, whether individual offices are authorized to conduct their own inspections or whether only the head office may conduct them);
- e. the nature and complexity of the audit organization's practice and structure; and

- 
- f. the risks associated with entities that the audit organization audits and specific engagements.

**5.103** Inspection procedures may include the review of engagements to determine if responses to address quality risks at the engagement level have been implemented as designed and are operating effectively. The matters considered during an inspection of an individual engagement depend on how the inspection will be used to monitor the system of quality management.

**5.104** The results of inspection procedures or other relevant information may indicate that previous monitoring activities that the audit organization undertook failed to identify a deficiency in the system of quality management. This information may affect the audit organization's consideration of the nature, timing, and extent of the monitoring activities.

**5.105** A peer review is not a substitute for monitoring activities. However, audit organizations may use the results of a peer review to consider improvements to the system of quality management.

**5.106** The audit organization may consider threats to objectivity when designing the policies and procedures addressing the objectivity of the individuals performing the monitoring activities. Examples of threats to objectivity include when

- a. an individual who performs an inspection of an engagement was an engagement team member or the engagement quality reviewer for that engagement and
- b. an individual who performs another type of monitoring activity participated in designing, executing, or operating the response being monitored.

**5.107** Individuals are not precluded from performing monitoring activities, including inspections, of their own compliance with a system of quality management. However, such self-inspections may be less effective than compliance inspections by another qualified individual. When individuals inspect their own compliance with an audit organization's policies and procedures, the audit organization has a higher risk that noncompliance will not be detected or reported through monitoring activities. To effectively self-monitor for compliance, it is necessary that individuals be able to critically review their own performance, assess their own strengths and weaknesses, and maintain attitudes of continual improvement.

**5.108** An audit organization may use a service provider, including another audit organization, to monitor or assist in the monitoring of the system of quality management.

**Requirements: Evaluating Quality Management Findings and Quality Management Deficiencies**

**5.109** The audit organization should evaluate findings concerning the system of quality management to determine whether deficiencies exist, including in the monitoring and remediation process.

**5.110** The audit organization should evaluate the severity and pervasiveness of identified deficiencies in the system of quality management by investigating their underlying causes and evaluating their effect, both individually and in the aggregate, on the system of quality management.

**Application Guidance: Evaluating Quality Management Findings and Quality Management Deficiencies**

**5.111** A finding in relation to a system of quality management is information about the design, implementation, and operation of the system of quality management that the audit organization has accumulated through the performance of monitoring activities and from other relevant sources, which indicates that one or more deficiencies may exist.

**5.112** The audit organization accumulates findings from monitoring activities, including inspections, and other relevant sources. Information that the audit organization accumulates from the monitoring activities, including inspections, and other relevant sources may lead to observations about the audit organization's system of quality management, such as

- a. actions, behaviors, or conditions that have given rise to positive outcomes in the context of quality or the effectiveness of the system of quality management or
- b. similar circumstances in which no findings were noted (for example, engagements in which no findings were noted but the

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engagements have a similar nature to the engagements in which findings were noted).

**5.113** The information that the audit organization accumulates from the monitoring activities and other relevant sources may also lead to other observations that may be useful to the audit organization. Such information may assist the audit organization in investigating the underlying causes of identified deficiencies, indicate practices that it can support or apply more extensively (for example, across all engagements), or highlight opportunities for it to enhance its system of quality management. The results of the monitoring and remediation process provide information about the operation of the system of quality management that is relevant to the audit organization's quality management risk assessment process.

**5.114** A deficiency in the audit organization's system of quality management exists when

- a. a quality objective required to achieve the objective of the system of quality management is not established;
- b. a quality risk, or combination of quality risks, is not identified or properly assessed;
- c. a response, or combination of responses, does not reduce to an acceptably low level the likelihood of a related quality risk occurring because the responses are not properly designed, implemented, or operating effectively; or
- d. another aspect of the system of quality management is absent, or not properly designed, implemented, or operating effectively, such that a requirement of this chapter has not been addressed.

**5.115** The audit organization exercises professional judgment in determining whether findings, individually or in combination with other findings, give rise to a deficiency in the system of quality management. In making the judgment, the audit organization may consider the relative importance of the findings in the context of the quality objectives, quality risks, responses, or other aspects of the system of quality management to which they relate. The audit organization's judgments may be affected by quantitative and qualitative factors relevant to the findings. In some circumstances, the audit organization may deem it appropriate to obtain more information about the findings to determine whether a deficiency

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exists. Not all findings, including findings about specific engagements, will be a deficiency.

**5.116** Factors the audit organization may consider in evaluating the severity and pervasiveness of an identified deficiency include the following:

- a. The nature of the identified deficiency, including the aspect of the audit organization's system of quality management to which the deficiency relates, and whether the deficiency is in the design, implementation, or operation of the system of quality management
- b. In the case of an identified deficiency related to a response, whether there are compensating responses to address the quality risk to which the response relates
- c. The underlying causes of the identified deficiency
- d. The frequency with which the matter giving rise to the identified deficiency occurred
- e. The magnitude of the identified deficiency, how quickly it occurred, and its duration and effect on the system of quality management.

**5.117** The nature, timing, and extent of the procedures undertaken to understand the underlying causes of an identified deficiency may also be affected by the nature and circumstances of the audit organization, such as the following:

- a. The complexity and operating characteristics of the audit organization
- b. The size of the audit organization
- c. The geographical dispersion of the audit organization
- d. How the audit organization is structured or the extent to which the audit organization concentrates or centralizes its processes or activities

**5.118** Evaluating findings and identifying deficiencies and evaluating the severity and pervasiveness of identified deficiencies, including

investigating the underlying causes of identified deficiencies, is an iterative process.

**Requirements: Responding to Identified Quality Management Deficiencies**

**5.119** The audit organization should design and implement remedial actions that respond to the results of the analysis of underlying causes to address identified deficiencies in the system of quality management.

**5.120** The audit organization should evaluate the remedial actions to determine whether they are effective in addressing the identified quality management deficiencies and their related underlying causes.

**5.121** If the audit organization's evaluation indicates that the remedial actions are not effective in addressing the quality management deficiencies, the audit organization should modify the remedial actions such that identified deficiencies and their related underlying causes are addressed.

*Quality Management Findings About a Particular Engagement*

**5.122** The audit organization should respond to circumstances when quality management findings indicate that there is an engagement for which

- a. required procedures were omitted during the performance of the engagement or
- b. the report issued may not comply with professional standards or applicable laws or regulations.<sup>38</sup>

**Application Guidance: Responding to Identified Quality Management Deficiencies**

**5.123** The nature, timing, and extent of remedial actions may depend on a variety of factors, including

- a. the underlying causes;

<sup>38</sup>See para. 9.68 and AU-C section 560, *Subsequent Events and Subsequently Discovered Facts* (AICPA, *Professional Standards*) for requirements relating to the discovery of insufficient audit evidence after report release.

- b. the severity and pervasiveness of the identified deficiency and therefore the urgency with which it needs to be addressed; and
- c. the effectiveness of the remedial actions in addressing the underlying causes, such as whether the audit organization needs to implement more than one remedial action to effectively address the underlying causes, or it needs to implement remedial actions as interim measures until it is able to implement more effective remedial actions.

**5.124** In some circumstances, the remedial action may include establishing additional quality objectives, or adding or modifying quality risks or responses, to address identified deficiencies.

**Requirements: Ongoing Communication Related to Monitoring and Remediation**

**5.125** The audit organization should communicate to appropriate personnel, including the senior-level official assigned responsibility and accountability for the system of quality management, and relevant engagement partner(s) or director(s) the following:

- a. a description of the monitoring activities performed;
- b. the identified deficiencies, along with information about their severity and pervasiveness; and
- c. the remedial actions to address identified deficiencies.

**5.126** The audit organization should communicate the matters described in paragraph 5.125 to engagement teams and others within the system of quality management to enable the audit organization and appropriate personnel to take prompt remedial action related to deficiencies in accordance with their responsibilities.

**Application Guidance: Ongoing Communication Related to Monitoring and Remediation**

**5.127** Communications about the monitoring and remediation to the senior-level official assigned responsibility and accountability for the system of quality management may be ongoing or periodic.

## Evaluating the System of Quality Management

### Requirements: Evaluating and Concluding on the System of Quality Management

**5.128** The senior-level official assigned responsibility and accountability for the audit organization's system of quality management should evaluate the system of quality management. The evaluation should be undertaken as of a point in time and performed at least annually. Based on this evaluation, the senior-level official should conclude and document one of the following:

- a. The system of quality management provides the audit organization with reasonable assurance that the objective of the system of quality management is being achieved.
- b. Except for matters related to identified deficiencies that have a severe but not pervasive effect on its design, implementation, and operation, the system of quality management provides the audit organization with reasonable assurance that the objective of the system of quality management is being achieved.
- c. The system of quality management does not provide the audit organization with reasonable assurance that the objective of the system of quality management is being achieved.

**5.129** When evaluating and concluding on the system of quality management, the senior-level official assigned responsibility and accountability for the system of quality management should consider

- a. the audit organization's quality management risk assessment process, including its quality objectives, quality risks, and responses and the extent to which the audit organization's responses address the quality risks, and
- b. the results of the monitoring and remediation process.

### Application Guidance: Evaluating and Concluding on the System of Quality Management

**5.130** To evaluate and conclude on the system of quality management, the senior-level official assigned responsibility and accountability for the system of quality management may consider



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- a. the severity and pervasiveness of identified deficiencies and the effect on the achievement of the objective of the system of quality management;
- b. whether remedial actions have been designed and implemented by the audit organization and whether the remedial actions taken up to the time of the evaluation are effective; and
- c. whether the effect of identified deficiencies on the system of quality management has been appropriately addressed, such as whether further actions have been taken in accordance with paragraph 5.121.

**5.131** There may be circumstances when identified deficiencies that are severe (including those that are severe and pervasive) have been appropriately remediated and their effect corrected at the point in time of the evaluation. In such cases, the senior-level official assigned responsibility and accountability for the system of quality management may conclude that the system of quality management provides the audit organization with reasonable assurance that the objective of the system of quality management is being achieved.

## Documentation

### Requirements: Documentation

**5.132** The audit organization should document its system of quality management in a manner sufficient to

- a. support personnel's consistent understanding of the system of quality management, including an understanding of their roles and responsibilities with respect to the system of quality management and performing engagements;
- b. support the consistent implementation and operation of the responses to address quality risks; and
- c. provide evidence of the design, implementation, and operation of the responses to address quality risks to support the evaluation of the system of quality management by the senior-level official assigned responsibility and accountability for it.

**5.133** The audit organization should include the following in its documentation of its system of quality management:

- a. Identification of the
  - (1) senior-level official assigned responsibility and accountability for the system of quality management, as discussed in paragraph 5.13a, and
  - (2) individual or individuals assigned operational responsibility for the system of quality management, as discussed in paragraph 5.13b.
- b. The audit organization's quality management risk assessment, including its quality objectives, quality risks, and a description of the responses and how the audit organization's responses address the quality risks, as discussed in paragraphs 5.19 through 5.23.
- c. Regarding the monitoring and remediation process,
  - (1) evidence of the monitoring activities performed, as discussed in paragraph 5.90;
  - (2) the evaluation of findings, and identified deficiencies and their related underlying causes, as discussed in paragraphs 5.109 and 5.110;
  - (3) remedial actions to address identified deficiencies and the evaluation of the design and implementation of such remedial actions, as discussed in paragraphs 5.119 and 5.120; and
  - (4) communications about monitoring and remediation, as discussed in paragraphs 5.125 and 5.126.
- d. The conclusion and the basis for the conclusion reached pursuant to paragraph 5.128.

**5.134** The audit organization should establish a period of time for document retention for the system of quality management that is sufficient to enable the audit organization and its peer reviewer to monitor the design, implementation, and operation of the system of quality management or for a longer period if required by law or regulation.

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### Application Guidance: Documentation

**5.135** An audit organization's judgments about the form, content, and extent of documentation may be affected by factors related to the nature and complexity of the audit organization itself and the engagements it performs. Areas of greater quality risk, matters involving more complex judgments, and changes to aspects of the system of quality management may have a greater effect on the form, content, and extent of documentation.

**5.136** In some instances, an external oversight authority may establish additional documentation requirements, either formally or informally, due to inspection findings or external peer review results or for reasons that the external oversight authority deems necessary.

**5.137** The audit organization is not required to document the consideration of every condition, event, circumstance, action, or inaction for each quality objective or each risk that may give rise to a quality risk.

**5.138** In documenting the quality risks and how its responses address the quality risks, the audit organization may document the assessments given to each quality risk (that is, the considered occurrence and effect achieving one or more quality objectives) to support the consistent implementation and operation of the responses.

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## Engagement Quality Reviews

**5.139** This section establishes requirements for performing engagement quality reviews for an audit organization that determines that an engagement quality review is an appropriate response to address quality risks. An engagement quality review is an objective evaluation of the engagement team's significant judgments and the conclusions reached thereon.

**5.140** Engagement quality reviews can contribute to audit quality by serving as a safeguard against erroneous or insufficiently supported audits, thereby mitigating audit risk.

**5.141** The audit organization may determine that an engagement quality review is appropriate for all GAGAS engagements, specific types of

GAGAS engagements, or specifically identified GAGAS engagements.<sup>39</sup> The audit organization may determine that engagement quality reviews are not necessary to address quality risks.

**Requirements: Eligibility to Serve as an Engagement Quality Reviewer**

**5.142** An audit organization using engagement quality reviews should establish policies and procedures that set forth the eligibility criteria to be appointed as an engagement quality reviewer or an assistant to an engagement quality reviewer. The policies and procedures should require that any engagement quality reviewer and any assistants to an engagement quality reviewer not be members of the engagement team and

- a. have the competence and capabilities, including sufficient time, and the appropriate authority to perform the engagement quality review and
- b. comply with applicable legal and ethical requirements, including those addressing threats to the objectivity of the engagement quality reviewer.

**5.143** An audit organization using engagement quality reviews should establish policies and procedures that address circumstances in which the engagement quality reviewer's eligibility to perform the engagement quality review is impaired and the appropriate actions to be taken by the audit organization. The audit organization should include in such policies and procedures notification to appropriate individuals within the audit organization if the engagement quality reviewer becomes aware of circumstances that impair the engagement quality reviewer's eligibility.

**Application Guidance: Eligibility to Serve as an Engagement Quality Reviewer**

**5.144** The audit organization may consider threats to objectivity created by an individual being appointed as the engagement quality reviewer after having been previously assigned to the engagement. In recurring

<sup>39</sup>See para. 5.72 for a discussion of criteria that an audit organization establishes to determine if an engagement quality review is an appropriate response for one or more quality risks.

engagements, the matters on which significant judgments are made often do not vary. Significant judgments made in prior engagements may continue to affect the engagement team's judgments in subsequent engagements. Therefore, the ability of an engagement quality reviewer to perform an objective evaluation of significant judgments may be affected when the individual was previously involved with making those judgments. In such circumstances, it is important that appropriate safeguards are put in place to reduce threats to objectivity to an acceptable level.

**Requirements: Performance of the Engagement Quality Review**

**5.145** An audit organization using engagement quality reviews should establish policies and procedures regarding the performance of the engagement quality review that address the following:

- a. The engagement quality reviewer's responsibilities to perform procedures at appropriate points in time during the engagement to provide an appropriate basis for an objective evaluation of the engagement team's significant judgments and the conclusions reached thereon.
- b. The responsibilities of the engagement partner or director in relation to the engagement quality review, including that
  - (1) the engagement partner or director is precluded from releasing the audit report until after having received notification from the engagement quality reviewer that the engagement quality review is complete and
  - (2) documentation is provided to the engagement quality reviewer to permit completion of the engagement quality review.
- c. Circumstances when the nature and extent of engagement team discussions with the engagement quality reviewer about a significant judgment give rise to a threat to the engagement quality reviewer's objectivity and appropriate actions to take in these circumstances.

**5.146** In performing an engagement quality review, the engagement quality reviewer should do the following:

- a. Read and obtain an understanding about information communicated to the engagement quality reviewer by the

- (1) engagement team regarding the nature and circumstances of the engagement and the entity and
  - (2) audit organization related to its monitoring and remediation process, in particular, identified deficiencies that may relate to, or affect, the areas involving significant judgments made by the engagement team.
- b. Discuss with the engagement partner or director and, if applicable, other members of the engagement team, significant matters and significant judgments made in planning, performing, and reporting on the engagement.
- c. Based on the information obtained in paragraph 5.146 (a) and (b), review selected engagement documentation relating to the engagement team's significant judgments and evaluate the following:
  - (1) The basis for making those significant judgments, including, when applicable to the type of engagement, the engagement team's exercise of professional skepticism.
  - (2) Whether the engagement documentation supports the conclusions reached.
  - (3) Whether the conclusions reached are appropriate.
- d. Evaluate whether appropriate consultation has taken place on difficult or contentious matters or matters involving differences of opinion and the conclusions arising from those consultations.
- e. Evaluate the basis for
  - (1) the engagement partner's or director's determination that the engagement partner's or director's involvement has been sufficient and appropriate throughout the engagement such that the engagement partner or director has the basis for determining that the significant judgments made and the conclusions reached are appropriate given the nature and circumstances of the engagement and
  - (2) the engagement partner's or director's determination that independence and ethical requirements have been fulfilled.
- f. Review
  - (1) for audits of financial statements, the financial statements

and the auditor's report thereon, including, if applicable, the description of the key audit matters;

- (2) for reviews of financial statements or financial information, the financial statements or financial information and the audit report thereon; or
- (3) for other engagements, the audit report, and when applicable, the subject matter information.

**5.147** If an engagement quality reviewer has concerns that the engagement team's significant judgments or conclusions are not appropriate, the engagement quality reviewer should notify the engagement partner or director. If such concerns are not resolved to the engagement quality reviewer's satisfaction, the engagement quality reviewer should notify appropriate individuals in the audit organization that the engagement quality review cannot be completed.

### **Application Guidance: Performance of the Engagement Quality Review**

**5.148** Frequent communication between the engagement team and engagement quality reviewer throughout the engagement may facilitate an effective and timely engagement quality review.

**5.149** The audit organization's policies and procedures may specify the nature, timing, and extent of the procedures that the engagement quality reviewer performs and may emphasize the importance of the engagement quality reviewer exercising professional judgment in performing the review.

**5.150** Examples of significant judgments and conclusions include

- a. matters relating to planning the engagement, including the identification of suitable criteria and the composition of the engagement team;
- b. conclusions on the results of procedures performed by the engagement team on significant areas of the engagement;
- c. the evaluation of work performed by specialists and conclusions drawn thereon; and

- d. the overall assessment of the sufficiency and appropriateness of evidence.

**5.151** The audit organization's policies and procedures may specify the individual or individuals in the audit organization to be notified if the engagement quality reviewer has unresolved concerns that the engagement team's significant judgments or conclusions are not appropriate. With respect to such unresolved concerns, the audit organization's policies and procedures may also require consultation within or outside the audit organization.

**Requirement: Completion of the Engagement Quality Review**

**5.152** When an engagement quality review is performed, the engagement quality reviewer should notify the engagement partner or director when the engagement quality review is complete.

**Requirement: Engagement Quality Review Documentation**

**5.153** When an engagement quality review is performed, the engagement quality reviewer should document

- a. the names of the engagement quality reviewer and individuals who assisted with the engagement quality review;
- b. that the procedures required by the audit organization's policies on engagement quality reviews have been performed;
- c. that the engagement quality reviewer is not aware of any unresolved matters that would cause the engagement quality reviewer to believe that the significant judgments that the engagement team made and the conclusions it reached were not appropriate;
- d. the notifications required in accordance with paragraphs 5.147 and 5.152; and
- e. the date of completion of the engagement quality review.



### Application Guidance: Engagement Quality Review Documentation

**5.154** The form, content, and extent of the documentation of the engagement quality review may vary based on factors such as

- a. the nature and complexity of the engagement,
- b. the nature of the entity,
- c. the nature and complexity of the matters subject to the engagement quality review, or
- d. the extent of the engagement documentation reviewed.

## External Peer Review

### Requirements: General

**5.155** Each audit organization conducting engagements in accordance with GAGAS must obtain an external peer review conducted by reviewers independent of the audit organization being reviewed. The peer review should be sufficient in scope to provide a reasonable basis for determining whether, for the period under review, (1) the reviewed audit organization's system of quality management was suitably designed and (2) the organization is complying with its system of quality management so that it has reasonable assurance that it is fulfilling its responsibilities in accordance with professional standards and performing and reporting in conformity with such standards in all material respects.

**5.156** Audit organizations affiliated with one of the following recognized organizations should comply with the respective organization's peer review requirements and the requirements listed throughout paragraphs 5.161 through 5.175.

- a. American Institute of Certified Public Accountants
- b. Council of the Inspectors General on Integrity and Efficiency
- c. Association of Local Government Auditors
- d. International Organization of Supreme Audit Institutions
- e. National State Auditors Association

**5.157** Any audit organization not affiliated with an organization listed in paragraph 5.156 should meet the minimum GAGAS peer review requirements throughout paragraphs 5.161 through 5.189.

**Application Guidance: General**

**5.158** Each audit organization has discretion in selecting and accepting its peer review teams. Auditors in governments or jurisdictions without access to established peer review programs may engage other auditors, including public accounting firms, to conduct their peer reviews. If access to an established peer review program is not available, auditors may organize regional programs with other auditors.

**5.159** In cases of unusual difficulty or hardship, extensions of the deadlines for submitting peer review reports exceeding 3 months beyond the due date may be granted by the entity that administers the peer review program with the concurrence of GAO.

**5.160** Some audit organizations may be subject to or required to follow a peer review program of a recognized organization. Other audit organizations may follow a specific peer review program voluntarily. In instances where the audit organization follows a recognized organization's peer review program voluntarily, the use of such a peer review program means compliance with the recognized organization's entire peer review process, including, where applicable, standards for administering, performing, and reporting on peer reviews, oversight procedures, training, and related guidance materials.

**Requirements: Assessment of Peer Review Risk**

**5.161** The peer review team should perform an assessment of peer review risk to help determine the number and types of engagements to select for review.

**5.162** Based on the risk assessment, the peer review team should select engagements that provide a reasonable cross section of all types of work subject to the reviewed audit organization's system of quality management, including one or more engagements conducted in accordance with GAGAS.

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## Application Guidance: Assessment of Peer Review Risk

### 5.163 Peer review risk is the risk that the review team

- a. fails to identify significant weaknesses in the reviewed audit organization's system of quality management for its auditing practice, its lack of compliance with that system, or a combination thereof;
- b. issues an inappropriate opinion on the reviewed audit organization's system of quality management for its auditing practice, its compliance with that system, or a combination thereof; or
- c. makes an inappropriate decision about the matters to be included in, or excluded from, the peer review report.

**5.164** A selection approach that provides a cross section of all types of work is generally applicable to audit organizations that conduct a small number of GAGAS engagements in relation to other types of engagements. In these cases, one or more GAGAS engagements may represent more than what would be selected when looking at a cross section of the audit organization's work as a whole. Some audit organizations conduct audit and attestation work in a number of functional areas. For example, an organization may conduct financial audits, attestation engagements, reviews of financial statements, and performance audits. The peer review team may consider reviewing a sample of engagements from each of the major functional areas included within the scope of the review.

**5.165** A peer review is designed to test significant risk areas where it is possible that engagements are not being conducted, reported on, or both in conformity with professional standards in all material respects. A peer review is not designed to test every engagement, compliance with every professional standard, or every detailed component of the audit organization's system of quality management.

**5.166** Examples of the factors that may be considered when performing an assessment of risk for selecting engagements for peer review include

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- a. scope of the engagements, including size of the audited entity or engagements covering multiple locations;
- b. functional area or type of government program;
- c. types of engagements conducted, including the extent of nonaudit services provided to audited entities;
- d. personnel (including use of new personnel or personnel not routinely assigned the types of engagements conducted);
- e. initial engagements;
- f. familiarity resulting from a long-standing relationship with the audited entity;
- g. political sensitivity of the engagements;
- h. budget constraints faced by the audit organization that could negatively affect engagement quality;
- i. results of the peer review team's review of the design of system of quality management;
- j. results of the audit organization's monitoring process; and
- k. overall risk tolerance within the audit organization that could negatively affect engagement quality.

**Requirements: Peer Review Report Ratings**

**5.167** The peer review team should use professional judgment in deciding on the type of peer review rating to issue; the ratings are as follows:

- a. Peer review rating of pass: A conclusion that the audit organization's system of quality management has been suitably designed and complied with to provide the audit organization with reasonable assurance of performing and reporting in conformity with professional standards in all material respects.

- b.** Peer review rating of pass with deficiencies: A conclusion that the audit organization's system of quality management has been suitably designed and complied with to provide the audit organization with reasonable assurance of performing and reporting in conformity with professional standards in all material respects with the exception of a certain deficiency or deficiencies described in the report.
- c.** Peer review rating of fail: A conclusion, based on the significant deficiencies described in the report, that the audit organization's system of quality management is not suitably designed to provide the audit organization with reasonable assurance of performing and reporting in conformity with professional standards in all material respects, or that the audit organization has not complied with its system of quality management to provide the audit organization with reasonable assurance of performing and reporting in conformity with professional standards in all material respects.

**5.168** The peer review team should determine the type of peer review rating to issue based on the observed matters' importance to the audit organization's system of quality management as a whole and the nature, causes, patterns, and pervasiveness of those matters. The matters should be assessed both alone and in aggregate.

**5.169** The peer review team should aggregate and systematically evaluate any observed matters (circumstances that warrant further consideration by the peer review team) and document its evaluation.<sup>40</sup> The peer review team should perform its evaluation and issue report ratings as follows:

- a.** If the peer review team's evaluation of observed matters does not identify any findings (more than a remote possibility that the reviewed audit organization would not perform, report, or both in conformity with professional standards), or identifies findings that are not considered to be deficiencies, the peer review team issues a pass rating.

<sup>40</sup>See fig. 3 at the end of ch. 5 for a flowchart on developing peer review communications for observed matters in accordance with GAGAS.

- b. If the peer review team's evaluation of findings identified deficiencies but did not identify any significant deficiencies, the peer review team issues a pass with deficiencies rating and communicates the deficiencies in its report.
- c. If the peer review team's evaluation of deficiencies identified significant deficiencies, the peer review team issues a fail rating and communicates the deficiencies and significant deficiencies in its report.

### Application Guidance: Peer Review Report Ratings

**5.170** Deficiencies are findings that because of their nature, causes, pattern, or pervasiveness, including their relative importance to the audit organization's system of quality management taken as a whole, could create a situation in which the audit organization would not have reasonable assurance of performing, reporting, or both in conformity with professional standards in one or more important respects.

**5.171** Significant deficiencies are one or more deficiencies that the peer review team concludes result from a condition in the audit organization's system of quality management or compliance with that system such that the system taken as a whole does not provide reasonable assurance of performing, reporting, or both in conformity with professional standards.

#### Requirements: Availability of the Peer Review Report to the Public

**5.172** An external audit organization should make its most recent peer review report publicly available. If a separate communication detailing findings, conclusions, and recommendations is issued, the external audit organization is not required to make that communication publicly available. An internal audit organization that reports internally to management and those charged with governance should provide a copy of its peer review report to those charged with governance.

**5.173** An external audit organization should satisfy the publication requirement for its peer review report by posting the report on a publicly available website or to a publicly available file. Alternatively, if

neither of these options is available, then the audit organization should use the same mechanism it uses to make other reports or documents public.

**5.174** Because information in peer review reports may be relevant to decisions on procuring audit services, an audit organization seeking to enter into a contract to conduct an engagement in accordance with GAGAS should provide the following to the party contracting for such services when requested:

- a. the audit organization's most recent peer review report and
- b. any subsequent peer review reports received during the period of the contract.

**5.175** Auditors who are using another audit organization's work should request a copy of that organization's most recent peer review report, and the organization should provide this document when it is requested.

### **Application Guidance: Availability of the Peer Review Report to the Public**

**5.176** To help the public understand the peer review reports, an audit organization may include a description of the peer review process and how it applies to its organization. Examples of additional information that audit organizations may include to help users understand the meaning of the peer review report follow:

- a. Explanation of the peer review process
- b. Description of the audit organization's system of quality management
- c. Explanation of the relationship of the peer review results to the audited organization's work
- d. If a peer review report is issued with a rating of pass with deficiencies or fail, explanation of the reviewed audit organization's plan for improving its system of quality management and the status of the improvements

## Additional Requirements for Audit Organizations Not Affiliated with Recognized Organizations

### Requirement: Peer Review Scope

**5.177** The peer review team should include the following elements in the scope of the peer review:

- a. review of the audit organization's design of, and compliance with, quality management and related policies and procedures;
- b. consideration of the adequacy and results of the audit organization's internal monitoring procedures;
- c. review of selected audit reports and related documentation and, if applicable, documentation related to selected terminated engagements prepared in accordance with paragraph 5.55c, if any terminated engagements are selected from the universe of engagements used for the peer review sample;
- d. review of prior peer review reports, if applicable;
- e. review of other documents necessary for assessing compliance with standards, for example, independence documentation, CPE records, and relevant human resource management files; and
- f. interviews with selected members of the audit organization's personnel in various roles to assess their understanding of and compliance with relevant quality management policies and procedures.

### Application Guidance: Peer Review Scope

**5.178** Review of documentation related to terminated engagements can provide information on the audit organization's response to threats to independence. For example, the documentation may include information on whether an engagement was terminated as a result of an undue influence from outside the audit organization.



**Requirement: Peer Review Intervals**

**5.179** An audit organization not already subject to a peer review requirement should obtain an external peer review at least once every 3 years. The audit organization should obtain its first peer review covering a review period ending no later than 3 years from the date an audit organization begins its first engagement in accordance with GAGAS.

**Application Guidance: Peer Review Intervals**

**5.180** The period under review in a peer review generally covers 1 year.

**Requirement: Written Agreement for Peer Review**

**5.181** The peer review team and the reviewed audit organization should incorporate their basic agreement on the peer review into a written agreement. The written agreement should be drafted by the peer review team, reviewed by the reviewed audit organization to ensure that it accurately describes the agreement between the parties, and signed by the authorized representatives of both the peer review team and the reviewed audit organization prior to the initiation of work under the agreement. The written agreement should state that the peer review will be conducted in accordance with GAGAS peer review requirements.

**Application Guidance: Written Agreement for Peer Review**

**5.182** The written agreement is meant to ensure mutual consent on the fundamental aspects of the peer review and to avoid any potential misunderstandings. The written agreement may address the following:

- a. scope of the peer review;
- b. staffing and time frame;
- c. compensation for conducting the peer review, if applicable;
- d. preliminary findings, if applicable;
- e. reporting results;

- f. administrative matters; and
- g. access to audit documentation.

**5.183** The peer review team is responsible for ensuring that the peer review is conducted in accordance with GAGAS peer review requirements.

**Requirement: Peer Review Team**

**5.184** The peer review team should meet the following criteria:

- a. The review team collectively has adequate professional competence and knowledge of GAGAS and government auditing.
- b. The organization conducting the peer review and individual review team members are independent (as defined in GAGAS) of the audit organization being reviewed, its personnel, and the engagements selected for the peer review.<sup>41</sup>
- c. The review team collectively has sufficient knowledge to conduct a peer review.

**Application Guidance: Peer Review Team**

**5.185** Peer review knowledge and professional competence may be obtained from on-the-job training, training courses, or a combination of both. Having individuals on the peer review team with prior experience on a peer review or internal inspection team is desirable.

**Requirement: Report Content**

**5.186** The peer review team should prepare one or more written reports communicating the results of the peer review, which collectively include the following elements:

<sup>41</sup>See paras. 3.18 through 3.108 for independence requirements and guidance.

- a. a description of the scope of the peer review, including any limitations;
- b. a rating concluding on whether the system of quality management of the reviewed audit organization was adequately designed and complied with during the period reviewed and would provide the audit organization with reasonable assurance that it conformed to professional standards;
- c. specification of the professional standards to which the reviewed audit organization is being held;
- d. reference to a separate written communication, if issued under the peer review program;
- e. a statement that the peer review was conducted in accordance with GAGAS peer review requirements; and
- f. a detailed description of the findings, conclusions, and recommendations related to any deficiencies or significant deficiencies identified in the review.

### Application Guidance: Report Content

**5.187** When the scope of the peer review is limited by conditions that preclude the application of one or more peer review procedures considered necessary in the circumstances and the peer review team cannot accomplish the objectives of those procedures through alternative procedures, the report can be modified by including a statement in the report's scope paragraph, body, and opinion paragraph. The statement describes the relationship of the excluded engagement(s) or functional area(s) to the reviewed audit organization's full scope of practice as a whole and system of quality management and the effects of the exclusion on the scope and results of the review.

### Requirements: Audit Organization's Response to the Peer Review Report

**5.188** If the reviewed audit organization receives a report with a peer review rating of pass with deficiencies or fail, the reviewed audit

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organization should respond in writing to the deficiencies or significant deficiencies and related recommendations identified in the report.

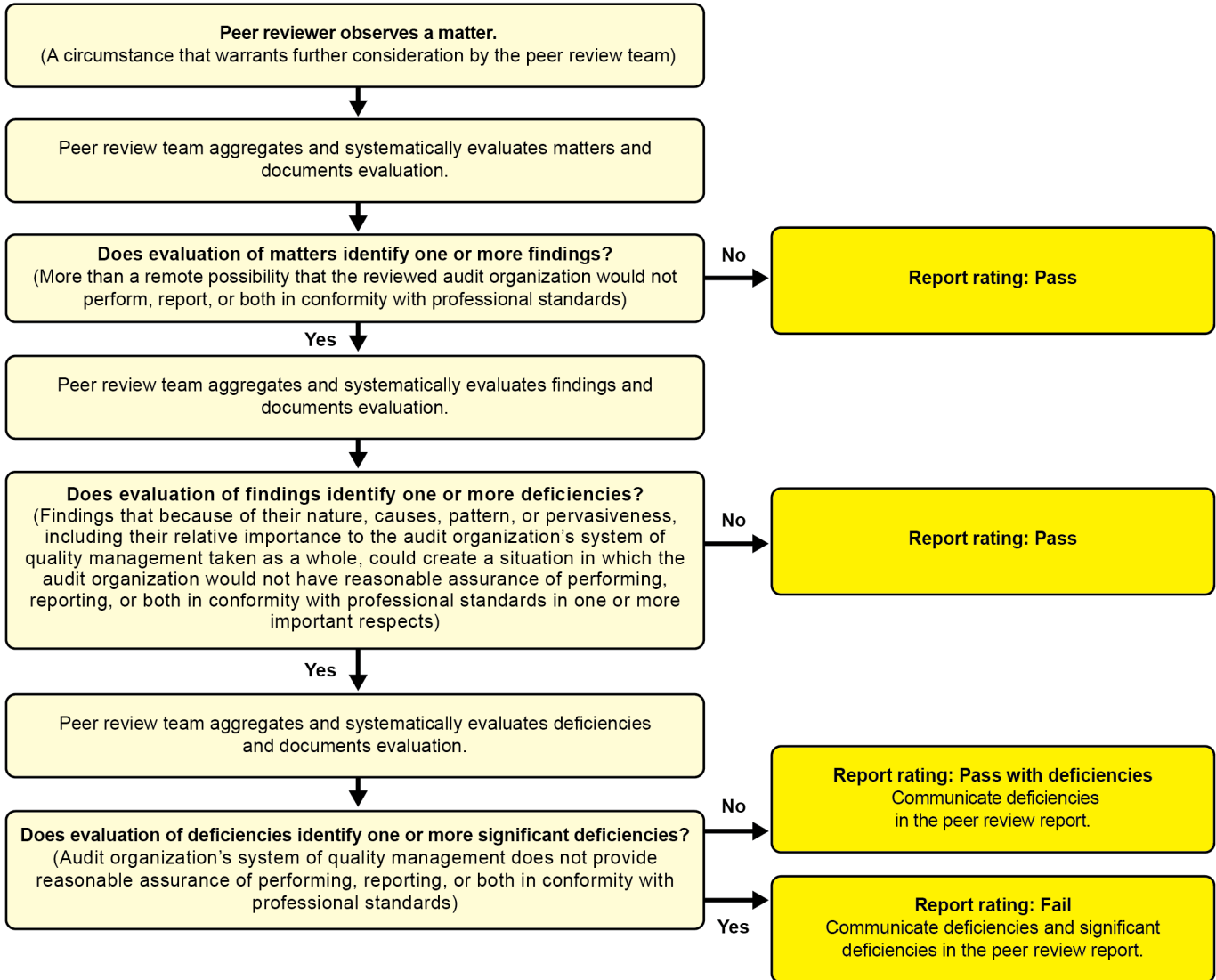
**5.189** With respect to each deficiency or significant deficiency in the report, the reviewed audit organization should describe in its letter of response the corrective actions already taken, target dates for planned corrective actions, or both.

**Application Guidance: Audit Organization's Response to the Peer Review Report**

**5.190** When an audit organization receives a peer review rating of pass with deficiencies or fail that relates to its GAGAS engagements, critical evaluation of the design and implementation of the system of quality management is a factor in determining the audit organization's ability to accept and perform future GAGAS engagements.

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Figure 3: Developing Peer Review Communications for Observed Matters in Accordance with Generally Accepted Government Auditing Standards



Source: GAO. | GAO-24-106786

# Chapter 6: Standards for Financial Audits

**6.01** This chapter contains requirements and guidance for conducting and reporting on financial audits conducted in accordance with generally accepted government auditing standards (GAGAS). GAGAS incorporates by reference the American Institute of Certified Public Accountants' (AICPA) Statements on Auditing Standards (SAS).<sup>42</sup> All sections of the SAS are incorporated, including the introduction, objectives, definitions, requirements, and application material. GAGAS does not incorporate the AICPA Code of Professional Conduct by reference but recognizes that certain certified public accountants (CPA) may use or may be required to use the code in conjunction with GAGAS.<sup>43</sup> For financial audits conducted in accordance with GAGAS, the requirements and guidance in the incorporated SAS and this chapter apply. The requirements and guidance contained in chapters 1 through 5 also apply.

## Additional GAGAS Requirements for Conducting Financial Audits

### Compliance with Standards

#### **Requirement: Compliance with Standards**

**6.02** GAGAS establishes requirements for financial audits in addition to the requirements in the AICPA SAS. Auditors should comply with these additional requirements, along with the AICPA requirements for financial audits, when citing GAGAS in financial audit reports.

#### **Application Guidance: Compliance with Standards**

**6.03** Standards used in conjunction with GAGAS require the auditors to apply the concept of materiality appropriately in planning and performing the audit.<sup>44</sup> Additional considerations may apply to GAGAS engagements

<sup>42</sup>See para. 2.13 and the AICPA *Codification of Statements on Auditing Standards (AU-C)* for additional discussion of the relationship between GAGAS and other professional standards.

<sup>43</sup>See para. 2.14 for a discussion of the AICPA Code of Professional Conduct.

<sup>44</sup>See AU-C section 320, *Materiality in Planning and Performing an Audit (AICPA, Professional Standards)*.

that concern government entities or entities that receive government awards. For example, for engagements conducted in accordance with GAGAS, auditors may find it appropriate to use lower materiality levels than those used in non-GAGAS audits 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.

## Licensing and Certification

### Requirements: Licensing and Certification

**6.04** Auditors engaged to conduct financial audits in the United States who do not work for a government audit organization should be licensed CPAs, persons working for licensed certified public accounting firms, or licensed accountants in states that have multiclass licensing systems that recognize licensed accountants other than CPAs.

**6.05** Auditors engaged to conduct financial audits of entities operating outside of the United States who do not work for a government audit organization should meet the qualifications indicated in paragraph 6.04, have certifications that meet all applicable national and international standards and serve in their respective countries as the functional equivalent of CPAs in the United States, or work for nongovernment audit organizations that are the functional equivalent of licensed certified public accounting firms in the United States.

## Auditor Communication

### Requirements: Auditor Communication

**6.06** If the law or regulation requiring an audit specifically identifies the entities to be audited, auditors should communicate pertinent information that in the auditors' professional judgment needs to be communicated both to individuals contracting for or requesting the audit and to those legislative committees, if any, that have ongoing oversight responsibilities for the audited entity.

**6.07** If the identity of those charged with governance is not clearly evident, auditors should document the process followed and

conclusions reached in identifying the appropriate individuals to receive the required communications.

### Application Guidance: Auditor Communication

**6.08** One example of a law or regulation requiring an audit that does not specifically identify the entities to be audited is the Single Audit Act Amendments of 1996.

**6.09** For some matters, early communication to management or those charged with governance may be important because of the relative significance and the urgency for corrective follow-up action.<sup>45</sup> Further, early communication is important to allow management to take prompt corrective action to prevent further occurrences when a control deficiency results in identified or suspected noncompliance with provisions of laws, regulations, contracts, and grant agreements or identified or suspected instances of fraud. When a deficiency is communicated early, the reporting requirements and application guidance in paragraphs 6.40 through 6.50 still apply.

**6.10** 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. The process for identifying those charged with governance includes evaluating the organizational structure for directing and controlling operations to achieve the audited entity's objectives and how the audited entity delegates authority and establishes accountability for management.

## Results of Previous Engagements

### Requirement: Results of Previous Engagements

**6.11** When planning the audit, auditors should ask management of the audited entity to identify previous audits, attestation engagements, and other studies that directly relate to the objectives of the audit, including whether related recommendations have been implemented. Auditors should evaluate whether the audited entity has taken appropriate corrective action to address findings and

<sup>45</sup>See AU-C section 265, *Communicating Internal Control Related Matters Identified in an Audit* (AICPA, *Professional Standards*).



recommendations from previous engagements that could have a significant effect on the subject matter. Auditors should use this information in assessing risk and determining the nature, timing, and extent of current audit work and determining the extent to which testing the implementation of the corrective actions is applicable to the current audit objectives.

## Investigations or Legal Proceedings

### **Requirement: Investigations or Legal Proceedings**

**6.12** Auditors should inquire of management of the audited entity whether any investigations or legal proceedings have been initiated or are in process with respect to the period under audit, and should evaluate the effect of initiated or in-process investigations or legal proceedings on the current audit.

### **Application Guidance: Investigations or Legal Proceedings**

**6.13** Laws, regulations, or policies may require auditors to communicate indications of certain types of fraud or noncompliance with provisions of laws, regulations, contracts, and grant agreements to law enforcement or investigatory authorities before performing additional audit procedures.

**6.14** Avoiding interference with investigations or legal proceedings is important in pursuing indications of fraud and noncompliance with provisions of laws, regulations, contracts, and grant agreements. In some cases, it may be appropriate for the auditors to work with investigators or legal authorities or to withdraw from or defer further work on the engagement or a portion of the engagement to avoid interfering with an ongoing investigation or legal proceeding.

## Noncompliance with Provisions of Laws, Regulations, Contracts, and Grant Agreements

### **Requirement: Noncompliance with Provisions of Laws, Regulations, Contracts, and Grant Agreements**

**6.15** Auditors should extend the AICPA requirements concerning consideration of noncompliance with laws and regulations to include

consideration of noncompliance with provisions of contracts and grant agreements.<sup>46</sup>

### **Application Guidance: Noncompliance with Provisions of Laws, Regulations, Contracts, and Grant Agreements**

**6.16** Government programs are subject to provisions of many laws, regulations, contracts, and grant agreements. At the same time, these provisions' significance within the context of the audit objectives varies widely, depending on the objectives of the audit. Auditors may consult with their 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, and (3) evaluate the results of those tests. Auditors also may consult with their 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.

## Findings

### **Requirements: Findings**

**6.17** When auditors identify findings, they should plan and perform procedures to develop the criteria, condition, cause, and effect of the findings to the extent that these elements are relevant and necessary to achieve the audit objectives.

**6.18** Auditors should consider internal control deficiencies in their evaluation of identified findings when developing the cause element of the identified findings.

<sup>46</sup>See AU-C section 250, *Consideration of Laws and Regulations in an Audit of Financial Statements* (AICPA, *Professional Standards*).

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**Application Guidance: Findings**

**6.19** Findings may involve deficiencies in internal control; noncompliance with provisions of laws, regulations, contracts, and grant agreements; or instances of fraud.

**6.20** Given the concept of accountability for use of public resources and government authority, evaluating internal control in a government environment may also include considering internal control deficiencies that result in waste or abuse. Because the determination of waste and abuse is subjective, auditors are not required to perform specific procedures to detect waste or abuse in financial audits. However, auditors may consider whether and how to communicate such matters if they become aware of them. Auditors may also discover that waste or abuse are indicative of fraud or noncompliance with provisions of laws, regulations, contracts, and grant agreements.

**6.21** Waste is the act of using or expending resources carelessly, extravagantly, or to no purpose. Importantly, waste can include activities that do not include abuse and does not necessarily involve a violation of law. Rather, waste relates primarily to mismanagement, inappropriate actions, and inadequate oversight.

**6.22** The following are examples of waste, depending on the facts and circumstances:

- a. Making travel choices that are contrary to existing travel policies or are unnecessarily extravagant or expensive.
- b. Making procurement or vendor selections that are contrary to existing policies or are unnecessarily extravagant or expensive.

**6.23** Abuse is 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, but excludes fraud and noncompliance with provisions of laws, regulations, contracts, and grant agreements. Abuse also includes misuse of authority or position for personal financial interests or those of an immediate or close family member or business associate.

**6.24** The following are examples of abuse, depending on the facts and circumstances:

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- 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).

**6.25** Criteria: For inclusion in findings, criteria may include 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 in the report. In a financial audit, the applicable financial reporting framework, such as generally accepted accounting principles, represents one set of criteria.

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

**6.27** Cause: The cause is the factor or factors responsible for the difference between the condition and the criteria, and 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 contributing to the difference between the condition and the criteria.

**6.28** Effect or potential effect: The effect or potential effect is the outcome or consequence resulting from the difference between the condition and the criteria. 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.

**6.29** Regardless of the type of finding identified, the cause of a finding may relate to one or more underlying internal control deficiencies. Depending on the magnitude of impact, likelihood of occurrence, and nature of the deficiency, the deficiency could be a significant deficiency or material weakness in a financial audit.<sup>47</sup>

**6.30** Considering internal control in the context of a comprehensive internal control framework, such as *Standards for Internal Control in the Federal Government* or *Internal Control—Integrated Framework*,<sup>48</sup> can help auditors to determine whether underlying internal control deficiencies exist as the root cause of findings. Identifying these deficiencies can help provide the basis for developing meaningful recommendations for corrective actions.

## Audit Documentation

### Requirements: Audit Documentation

**6.31** Auditors should document supervisory review, before the report release date, of the evidence that supports the findings and conclusions contained in the audit report.

**6.32** Auditors should document any departures from the GAGAS requirements and the effect on the audit and on the auditors' conclusions when the audit is not in compliance with applicable GAGAS requirements because of law, regulation, scope limitations, restrictions on access to records, or other issues affecting the audit.

<sup>47</sup>See AU-C section 265, *Communicating Internal Control Related Matters Identified in an Audit* (AICPA, *Professional Standards*).

<sup>48</sup>Para. .A16 of AU-C section 940, *An Audit of Internal Control Over Financial Reporting That Is Integrated With an Audit of Financial Statements* (AICPA, *Professional Standards*) indicates that the Committee of Sponsoring Organizations of the Treadway Commission's *Internal Control—Integrated Framework* and *Standards for Internal Control in the Federal Government* (GAO-14-704G) provide suitable and available criteria against which management may evaluate and report on the effectiveness of the entity's internal control over financial reporting. *Standards for Internal Control in the Federal Government* may be adopted by entities beyond those federal entities for which it is legally required, such as state, local, and quasi-governmental entities, as well as other federal entities and not-for-profit organizations, as a framework for an internal control system.

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**Application Guidance: Audit Documentation**

**6.33** When documenting departures from the GAGAS requirements, the audit documentation requirements apply to departures from unconditional requirements and from presumptively mandatory requirements when alternative procedures performed in the circumstances were not sufficient to achieve the objectives of the requirements.

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**Availability of Individuals and Documentation****Requirement: Availability of Individuals and Documentation**

**6.34** Subject to applicable provisions of laws and regulations, auditors should make appropriate individuals and audit documentation available upon request and in a timely manner to other auditors or reviewers.

**Application Guidance: Availability of Individuals and Documentation**

**6.35** Underlying GAGAS audits is the premise that audit organizations in federal, state, and local governments and public accounting firms engaged to conduct financial audits in accordance with GAGAS cooperate in auditing programs of common interest so that auditors may use others' work and avoid duplication of efforts. 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 and to audit documentation.

## Additional GAGAS Requirements for Reporting on Financial Audits

### Reporting the Auditors' Compliance with GAGAS

#### **Requirement: Reporting the Auditors' Compliance with GAGAS**

**6.36** When auditors comply with all applicable GAGAS requirements, they should include a statement in the audit report that they conducted the audit in accordance with GAGAS.<sup>49</sup>

#### **Application Guidance: Reporting the Auditors' Compliance with GAGAS**

**6.37** Because GAGAS incorporates by reference the AICPA's financial audit standards, GAGAS does not require auditors to cite compliance with the AICPA standards when citing compliance with GAGAS. GAGAS does not prohibit auditors from issuing a separate report conforming only to the requirements of the AICPA or other standards.<sup>50</sup>

**6.38** When disclaiming an opinion on a financial audit, auditors may revise the statement that the auditor was engaged to audit the financial statements.<sup>51</sup> For example, auditors may state that they were engaged to conduct the audit in accordance with GAGAS or that the auditors' work was conducted in accordance with GAGAS, depending on whether the use of GAGAS is required or voluntary. Determining how to revise this statement is a matter of professional judgment.

**6.39** Although there is no requirement in GAGAS to communicate key audit matters in the auditor's report, auditors may be required to communicate in the auditor's report key audit matters for audits of government entities and entities that receive government financial

<sup>49</sup>See paras. 2.16 through 2.19 for information on the GAGAS compliance statement.

<sup>50</sup>See AU-C section 700, *Forming an Opinion and Reporting on Financial Statements* (AICPA, *Professional Standards*).

<sup>51</sup>See AU-C section 705, *Modifications to the Opinion in the Independent Auditor's Report* (AICPA, *Professional Standards*).

assistance if (1) engaged to do so by management or those charged with governance,<sup>52</sup> or (2) required by law or regulation.<sup>53</sup>

## Reporting on Internal Control; Compliance with Provisions of Laws, Regulations, Contracts, and Grant Agreements; and Instances of Fraud

### **Requirements: Reporting on Internal Control; Compliance with Provisions of Laws, Regulations, Contracts, and Grant Agreements; and Instances of Fraud**

**6.40** Auditors should report on internal control and compliance with provisions of laws, regulations, contracts, or grant agreements regardless of whether they identify internal control deficiencies or instances of noncompliance.

**6.41** When providing an opinion or a disclaimer on financial statements, auditors should report as findings any significant deficiencies or material weaknesses in internal control over financial reporting that the auditors identified based on the engagement work performed.

**6.42** Auditors should include in their report on internal control or compliance the relevant information about noncompliance and fraud when auditors, based on sufficient, appropriate evidence, identify or suspect

- a. noncompliance with provisions of laws, regulations, contracts, or grant agreements that has a material effect on the financial statements or other financial data significant to the audit objectives or
- b. fraud that is material, either quantitatively or qualitatively, to the financial statements or other financial data significant to the audit objectives.

**6.43** Auditors should include either in the same or in separate report(s) a description of the scope of the auditors' testing of internal control over financial reporting and of compliance with provisions of

<sup>52</sup>See para. 1.04 for additional information on those charged with governance.

<sup>53</sup>See AU-C section 701, *Communicating Key Audit Matters in the Independent Auditor's Report* (AICPA, *Professional Standards*).



laws, regulations, contracts, and grant agreements. Auditors should also state in the report(s) whether the tests they performed provided sufficient, appropriate evidence to support opinions on the effectiveness of internal control and on compliance with provisions of laws, regulations, contracts, and grant agreements.

**6.44** If auditors report separately (including separate reports bound in the same document) on internal control over financial reporting and on compliance with provisions of laws, regulations, contracts, and grant agreements, they should include a reference in the audit report on the financial statements to those additional reports. They should also state in the audit report that the reports on internal control over financial reporting and on compliance with provisions of laws, regulations, contracts, and grant agreements are an integral part of a GAGAS audit in considering the audited entity's internal control over financial reporting and compliance. If separate reports are used, the auditors should make the report on internal control and compliance available to users in the same manner as the financial audit report to which it relates.

**6.45** Auditors should communicate in writing to audited entity officials when

- a. identified or suspected noncompliance with provisions of laws, regulations, contracts, or grant agreements comes to the auditor's attention during the course of an audit that has an effect on the financial statements or other financial data significant to the audit objectives that is less than material but warrants the attention of those charged with governance or
- b. the auditor has obtained evidence of identified or suspected instances of fraud that have an effect on the financial statements or other financial data significant to the audit objectives that are less than material but warrant the attention of those charged with governance.

**Application Guidance: Reporting on Internal Control; Compliance with Provisions of Laws, Regulations, Contracts, and Grant Agreements; and Instances of Fraud**

**6.46** The GAGAS requirement to report on internal control over financial reporting is based on the AICPA requirements to communicate in writing

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to those charged with governance significant deficiencies and material weaknesses in internal control over financial reporting identified during an audit. The objective of the GAGAS internal control reporting requirement for financial audits is to increase the availability of information on significant deficiencies and material weaknesses to users of financial statements other than those charged with governance.

**6.47** Internal control plays an expanded role in the government sector. Given the government's accountability for public resources, assessing internal control in a government environment may involve considering controls that would not be required in the private sector. In the government sector, evaluating controls that are relevant to the audit involves understanding significant controls that the audited entity designed, implemented, and operated as part of its responsibility for oversight of public resources.

**6.48** The audit report on internal control and compliance with provisions of laws, regulations, contracts, and grant agreements relates only to the most recent reporting period included, when comparative financial statements are presented.

**6.49** When identified or suspected noncompliance with provisions of laws, regulations, contracts, or grant agreements that does not warrant the attention of those charged with governance comes to the auditor's attention during the course of the audit, the auditors' determination of how to communicate such instances to audited entity officials is a matter of professional judgment. When identified or suspected noncompliance with provisions of laws, regulations, contracts, or grant agreements is clearly inconsequential, the auditors' determination of whether and how to communicate such instances to audited entity officials is a matter of professional judgment.

**6.50** When auditors identify or suspect noncompliance with provisions of laws, regulations, contracts, or grant agreements or instances of fraud, 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.

## Presenting Findings in the Audit Report

### Requirements: Presenting Findings in the Audit Report

**6.51** When presenting findings, auditors should develop the elements of the findings to the extent necessary to assist management or oversight officials of the audited entity in understanding the need for corrective action.

**6.52** 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 appropriate, 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. If the results cannot be projected, auditors should limit their conclusions appropriately.

### Application Guidance: Presenting Findings in the Audit Report

**6.53** Along with assisting management or oversight officials of the audited entity in understanding the need for corrective action, clearly developed findings assist auditors in making recommendations for corrective action. If auditors sufficiently develop the elements of a finding, they may provide recommendations for corrective action.

## Reporting Findings Directly to Parties outside the Audited Entity

### Requirements: Reporting Findings Directly to Parties outside the Audited Entity

**6.54** Auditors should report identified or suspected noncompliance with provisions of laws, regulations, contracts, and grant agreements and instances of fraud directly to parties outside the audited entity in the following two circumstances.

- a. When audited 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 audited entity management fails to take timely and appropriate steps to respond to fraud or noncompliance with provisions of laws, regulations, contracts, and grant agreements 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 audited entity's failure to take timely and appropriate steps directly to the funding agency.

**6.55** Auditors should comply with the requirements in paragraph 6.54 even if they have resigned or been dismissed from the audit prior to its completion.

**6.56** Auditors should obtain sufficient, appropriate evidence, such as confirmation from outside parties, to corroborate representations by management of the audited entity that it has reported audit findings in accordance with provisions of laws, regulations, or funding agreements. When auditors are unable to do so, they should report such information directly as discussed in paragraphs 6.54 and 6.55.

#### **Application Guidance: Reporting Findings Directly to Parties outside the Audited Entity**

**6.57** The reporting in paragraph 6.54 is in addition to any legal requirements to report such information directly to parties outside the audited entity.

#### Obtaining and Reporting the Views of Responsible Officials

##### **Requirements: Obtaining and Reporting the Views of Responsible Officials**

**6.58** Auditors should obtain and report the views of responsible officials of the audited entity concerning the findings, conclusions,

and recommendations in the audit report, as well as any planned corrective actions.

**6.59** 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, provide a copy of the summary to the responsible officials to verify that the comments are accurately represented, and include the summary in their report.

**6.60** When the audited entity's comments are inconsistent or in conflict with the findings, conclusions, or recommendations in the draft report, 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 by sufficient, appropriate evidence.

**6.61** If the audited entity refuses to provide comments or is unable to provide comments within a reasonable period of time, the auditors should 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.

### **Application Guidance: Obtaining and Reporting the Views of Responsible Officials**

**6.62** 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 audited entity's responsible officials and the corrective actions they plan to take. Obtaining the comments in writing is preferred, but oral comments are acceptable. 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. Technical comments address points of fact or are editorial in nature and do not address substantive issues, such as methodology, findings, conclusions, or recommendations.

**6.63** 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 engagement, and the parties are familiar with the findings and issues addressed in the draft report; or the auditors do not expect major disagreements with findings, conclusions, or recommendations in the draft report or major controversies with regard to the issues discussed in the draft report.

## Reporting Confidential or Sensitive Information

### Requirements: Reporting Confidential or Sensitive Information

**6.64** If certain information is prohibited from public disclosure or is excluded from a report because of its confidential or sensitive nature, auditors should disclose in the report that certain information has been omitted and the circumstances that make the omission necessary.

**6.65** When circumstances call for omission of certain information from the report, auditors should evaluate whether this omission could distort the audit results or conceal improper or illegal practices and revise the report language as necessary to avoid report users drawing inappropriate conclusions from the information presented.

**6.66** When the audit organization is subject to public records laws, auditors should determine whether public records laws could affect 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. Auditors use professional judgment to determine the appropriate means to communicate the omitted information to management and those charged with governance considering, among other things, whether public records laws could affect the availability of classified or limited use reports.

### Application Guidance: Reporting Confidential or Sensitive Information

**6.67** If the report refers to the omitted information, the reference may be general and not specific. If the omitted information is not necessary to meet the audit objectives, the report need not refer to its omission.

**6.68** 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 such information and distribute the report only to persons authorized by law or regulation to receive it.

**6.69** Additional circumstances associated with public safety, privacy, or 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 misuse of this information could cause. 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. In some instances, it may be appropriate to issue both a publicly available report with the sensitive information excluded and a limited use report. The auditors may consult with legal counsel regarding any requirements or other circumstances that may necessitate omitting certain information. Considering the broad public interest in the program or activity under audit assists auditors when deciding whether to exclude certain information from publicly available reports.

**6.70** In cases described in paragraph 6.66, the auditors may communicate general information in a written report and communicate detailed information orally. The auditors may consult with legal counsel regarding applicable public records laws.

## Distributing Reports

### Requirement: Distributing Reports

**6.71** Distribution of reports completed in accordance with GAGAS depends on the auditors' relationship with the audited entity and the nature of the information contained in the reports. Auditors should document any limitation on report distribution.

- a. An audit organization in a government entity should distribute audit reports to those charged with governance, to the appropriate audited entity officials, 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.** A public accounting firm contracted to conduct an audit in accordance with GAGAS should clarify report distribution responsibilities with the engaging party. If the contracting firm is responsible for 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.



# Chapter 7: Standards for Attestation Engagements and Reviews of Financial Statements

**7.01** This chapter contains requirements and guidance for conducting and reporting on attestation engagements and reviews of financial statements conducted in accordance with generally accepted government auditing standards (GAGAS). For attestation engagements, GAGAS incorporates by reference the American Institute of Certified Public Accountants' (AICPA) Statements on Standards for Attestation Engagements (SSAE). For reviews of financial statements, GAGAS incorporates by reference AICPA's AR-C section 90, *Review of Financial Statements*.<sup>54</sup> All sections of the cited standards are incorporated, including the introduction, objectives, definitions, requirements, and application and other explanatory material. GAGAS does not incorporate the AICPA Code of Professional Conduct by reference but recognizes that certain certified public accountants (CPA) may use or may be required to use the code in conjunction with GAGAS.<sup>55</sup> For attestation engagements and reviews of financial statements conducted in accordance with GAGAS, the requirements and guidance in the respective incorporated standards and this chapter apply. The requirements and guidance contained in chapters 1 through 5 also apply.

**7.02** An attestation engagement can provide one of three levels of service as defined by the AICPA: an examination engagement, a review engagement, or an agreed-upon procedures engagement.

**7.03** The AICPA standards used in conjunction with GAGAS require auditors to establish an understanding with the audited entity regarding the services to be performed for each attestation engagement or review of financial statements. Such an understanding reduces the risk that either the auditors or the audited entity may misinterpret the needs or expectations of the other party. The understanding includes the objectives of the engagement, responsibilities of audited entity management, responsibilities of auditors, and limitations of the engagement.<sup>56</sup>

**7.04** Auditors often conduct GAGAS engagements under a contract with a party other than the officials of the audited entity or pursuant to a third-

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<sup>54</sup>AICPA, *Professional Standards*.

<sup>55</sup>See para. 2.14 for a discussion of the AICPA Code of Professional Conduct.

<sup>56</sup>See para. .08 of AT-C section 205, *Assertion-Based Examination Engagements*, para. .09 of AT-C section 206, *Direct Examination Engagements*, para. .09 of AT-C section 210, *Review Engagements*, and para. .15 of AT-C section 215, *Agreed-Upon Procedures Engagements*; and para. .16 of AR-C section 90, *Review of Financial Statements* (AICPA, *Professional Standards*).

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party request. In such cases, auditors may also find it appropriate to communicate information regarding the services to be performed to the individuals contracting for or requesting the engagement. Such an understanding can help auditors avoid any misunderstandings regarding the nature of the review or agreed-upon procedures engagement. For example, a review engagement only provides limited assurance, and as a result, auditors do not perform sufficient work to be able to develop elements of a finding or provide recommendations that are common in other types of GAGAS engagements. An agreed-upon procedures engagement does not provide an opinion or conclusion, and as a result, auditors do not perform sufficient work to be able to develop elements of a finding or provide recommendations that are common in other types of GAGAS engagements. Consequently, requesting parties may find that a different type of attestation engagement or a performance audit may provide the appropriate level of assurance to meet their needs.

## Examination Engagements

### Compliance with Standards

**Requirement: Compliance with Standards**

**7.05** GAGAS establishes requirements for examination engagements in addition to the requirements for examinations contained in the AICPA's SSAEs. Auditors should comply with these additional requirements, along with the AICPA requirements for examination engagements, when citing GAGAS in their examination engagement reports.

**Application Guidance: Compliance with Standards**

**7.06** The AICPA standards applicable to examinations require the auditors to apply the concept of materiality appropriately in planning and performing the examination. Additional considerations may apply to GAGAS engagements that concern government entities or entities that receive government awards. For example, for engagements conducted in accordance with GAGAS, auditors may find it appropriate to use lower materiality levels than those used in non-GAGAS engagements because of the public accountability of government entities and entities receiving

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government funding, various legal and regulatory requirements, and the visibility and sensitivity of government programs.

## Licensing and Certification

### **Requirements: Licensing and Certification**

**7.07** Auditors engaged to conduct examination engagements in the United States who do not work for a government audit organization should be licensed CPAs, persons working for licensed certified public accounting firms, or licensed accountants in states that have multiclass licensing systems that recognize licensed accountants other than CPAs.

**7.08** Auditors engaged to conduct examination engagements of entities operating outside of the United States who do not work for a government audit organization should meet the qualifications indicated in paragraph 7.07, have certifications that meet all applicable national and international standards and serve in their respective countries as the functional equivalent of CPAs in the United States, or work for nongovernment audit organizations that are the functional equivalent of licensed certified public accounting firms in the United States.

## Auditor Communication

### **Requirements: Auditor Communication**

**7.09** If the law or regulation requiring an examination engagement specifically identifies the entities to be examined, auditors should communicate pertinent information that in the auditors' professional judgment needs to be communicated both to individuals contracting for or requesting the examination and to those legislative committees, if any, that have ongoing oversight responsibilities for the audited entity.

**7.10** If the identity of those charged with governance is not clearly evident, auditors should document the process followed and conclusions reached in identifying the appropriate individuals to receive the required communications.

### Application Guidance: Auditor Communication

**7.11** For some matters, early communication to those charged with governance or management may be important because of the relative significance and the urgency for corrective follow-up action. Further, early communication is important to allow management to take prompt corrective action to prevent further occurrences when a control deficiency results in identified or suspected noncompliance with provisions of laws, regulations, contracts, and grant agreements or identified or suspected fraud. When a deficiency is communicated early, the reporting requirements and application guidance in paragraphs 7.39 through 7.47 still apply.

**7.12** 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. The process for identifying those charged with governance includes evaluating the organizational structure for directing and controlling operations to achieve the audited entity's objectives and how the audited entity delegates authority and establishes accountability for management.

### Results of Previous Engagements

#### Requirement: Results of Previous Engagements

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

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**Investigations or Legal  
Proceedings**

**Requirement: Investigations or Legal Proceedings**

**7.14** Auditors should inquire of management of the audited entity whether any investigations or legal proceedings significant to the engagement objectives have been initiated or are in process with respect to the period under examination, and should evaluate the effect of initiated or in-process investigations or legal proceedings on the current examination engagement.

**Application Guidance: Investigations or Legal Proceedings**

**7.15** Laws, regulations, or policies may require auditors to report indications of certain types of fraud or noncompliance with provisions of laws, regulations, contracts, and grant agreements to law enforcement or investigatory authorities before performing additional examination procedures.

**7.16** Avoiding interference with investigations or legal proceedings is important in pursuing indications of fraud and noncompliance with provisions of laws, regulations, contracts, and grant agreements. In some cases, it may be appropriate for the auditors to work with investigators or legal authorities or to withdraw from or defer further work on the attestation engagement or a portion of the engagement to avoid interfering with an ongoing investigation or legal proceeding.

**Noncompliance with  
Provisions of Laws,  
Regulations, Contracts,  
and Grant Agreements**

**Requirement: Noncompliance with Provisions of Laws,  
Regulations, Contracts, and Grant Agreements**

**7.17** Auditors should extend the AICPA requirements concerning consideration of noncompliance with laws and regulations to include consideration of noncompliance with provisions of contracts and grant agreements.<sup>57</sup>

<sup>57</sup>See paras. .33 and .34 of AT-C section 205, *Assertion-Based Examination Engagements* (AICPA, *Professional Standards*).

### Application Guidance: Noncompliance with Provisions of Laws, Regulations, Contracts, and Grant Agreements

**7.18** Government programs are subject to provisions of many laws, regulations, contracts, and grant agreements. At the same time, these provisions' significance within the context of the engagement objectives varies widely, depending on the objectives of the engagement. Auditors may consult with their legal counsel to (1) determine those laws and regulations that are significant to the examination objectives, (2) design tests of compliance with laws and regulations, and (3) evaluate the results of those tests. Auditors also may consult with their legal counsel when engagement objectives require testing compliance with provisions of contracts or grant agreements. Depending on the circumstances of the engagement, 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.

## Findings

### Requirements: Findings

**7.19** When auditors identify findings, they should plan and perform procedures to develop the criteria, condition, cause, and effect of the findings to the extent that these elements are relevant and necessary to achieve the examination objectives.

**7.20** Auditors should consider internal control deficiencies in their evaluation of identified findings when developing the cause element of the identified findings.

### Application Guidance: Findings

**7.21** Findings may involve deficiencies in internal control; noncompliance with provisions of laws, regulations, contracts, and grant agreements; or instances of fraud.

**7.22** Given the concept of accountability for use of public resources and government authority, evaluating internal control in a government environment may also include considering internal control deficiencies that result in waste or abuse. Because the determination of waste and abuse is subjective, auditors are not required to perform specific procedures to detect waste or abuse in examinations. However, auditors

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may consider whether and how to communicate such matters if they become aware of them. Auditors may also discover that waste or abuse are indicative of fraud or noncompliance with provisions of laws, regulations, contracts, and grant agreements.

**7.23** Waste is the act of using or expending resources carelessly, extravagantly, or to no purpose. Importantly, waste can include activities that do not include abuse and does not necessarily involve a violation of law. Rather, waste relates primarily to mismanagement, inappropriate actions, and inadequate oversight.

**7.24** The following are examples of waste, depending on the facts and circumstances:

- a. Making travel choices that are contrary to existing travel policies or are unnecessarily extravagant or expensive.
- b. Making procurement or vendor selections that are contrary to existing policies or are unnecessarily extravagant or expensive.

**7.25** Abuse is 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, but excludes fraud and noncompliance with provisions of laws, regulations, contracts, and grant agreements. Abuse also includes misuse of authority or position for personal financial interests or those of an immediate or close family member or business associate.

**7.26** 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

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organization with which the official is negotiating concerning future employment).

**7.27** Criteria: For inclusion in findings, criteria may include 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 in the report.

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

**7.29** Cause: The cause is the factor or factors responsible for the difference between the condition and the criteria, and 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 contributing to the difference between the condition and the criteria.

**7.30** Effect or potential effect: The effect or potential effect is the outcome or consequence resulting from the difference between the condition and the criteria. 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.

**7.31** Regardless of the type of finding identified, the cause of a finding may relate to an underlying internal control deficiency. Depending on the magnitude of impact, likelihood of occurrence, and nature of the deficiency, this deficiency could be a significant deficiency or a material weakness.

**7.32** Considering internal control in the context of a comprehensive internal control framework, such as *Standards for Internal Control in the*



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*Federal Government or Internal Control—Integrated Framework*,<sup>58</sup> can help auditors to determine whether underlying internal control deficiencies exist as the root cause of findings. Identifying these deficiencies can help provide the basis for developing meaningful recommendations for corrective actions.

**Examination Engagement  
Documentation**

**Requirements: Examination Engagement Documentation**

**7.33** Auditors should comply with the following documentation requirements.

- a. Before the date of the examination report, document supervisory review of the evidence that supports the findings, conclusions, and recommendations contained in the examination report.
- b. Document any departures from the GAGAS requirements and the effect on the examination engagement and on the auditors' conclusions when the examination engagement does not comply with applicable GAGAS requirements because of law, regulation, scope limitations, restrictions on access to records, or other issues affecting the examination engagement.

**7.34** In addition to the requirements of the examination engagement standards used in conjunction with GAGAS, auditors should prepare attest documentation in sufficient detail to enable an experienced auditor, having no previous connection to the examination 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.

<sup>58</sup>The Committee of Sponsoring Organizations of the Treadway Commission's *Internal Control—Integrated Framework* and *Standards for Internal Control in the Federal Government* (GAO-14-704G) provide suitable and available criteria against which management may evaluate and report on the effectiveness of the entity's internal control. *Standards for Internal Control in the Federal Government* may be adopted by entities beyond those federal entities for which it is legally required, such as state, local, and quasi-governmental entities, as well as other federal entities and not-for-profit organizations, as a framework for an internal control system.

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**Application Guidance: Examination Engagement Documentation**

**7.35** When documenting departures from the GAGAS requirements where alternative procedures performed were not sufficient to achieve the objectives of the requirements, the examination engagement documentation requirements apply to departures from unconditional requirements and presumptively mandatory requirements.

**7.36** An experienced auditor is an individual who possesses the competencies and skills to be able to conduct the examination engagement. These competencies and skills include an understanding of (1) examination engagement processes and related examination standards, (2) GAGAS and applicable legal and regulatory requirements, (3) the subject matter on which the auditors are engaged to report, (4) the suitability and availability of criteria, and (5) issues related to the audited entity's environment.

**Availability of Individuals  
and Documentation**

**Requirement: Availability of Individuals and Documentation**

**7.37** Subject to applicable provisions of laws and regulations, auditors should make appropriate individuals and examination engagement documentation available upon request and in a timely manner to other auditors or reviewers.

**Application Guidance: Availability of Individuals and Documentation**

**7.38** Underlying GAGAS examination engagements is the premise that audit organizations in federal, state, and local governments and public accounting firms engaged to conduct examination engagements in accordance with GAGAS cooperate in evaluating programs of common interest so that auditors may use others' work and avoid duplication of efforts. 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 and to engagement documentation.

## Reporting the Auditors' Compliance with GAGAS

### Requirements: Reporting the Auditors' Compliance with GAGAS

**7.39** When auditors comply with all applicable GAGAS requirements, they should include a statement in the report that they conducted the examination in accordance with GAGAS.<sup>59</sup>

**7.40** If auditors report separately (including separate reports bound in the same document) on deficiencies in internal control; noncompliance with provisions of laws, regulations, contracts, and grant agreements; or instances of fraud, they should state in the examination report that they are issuing those additional reports. They should include a reference to the separate reports and also state that the reports are an integral part of a GAGAS examination engagement.

### Application Guidance: Reporting the Auditors' Compliance with GAGAS

**7.41** Because GAGAS incorporates by reference the AICPA's attestation standards, GAGAS does not require auditors to cite compliance with the AICPA standards when citing compliance with GAGAS. GAGAS does not prohibit auditors from issuing a separate report conforming only to the requirements of the AICPA or other standards.

## Reporting Deficiencies in Internal Control

### Requirement: Reporting Deficiencies in Internal Control

**7.42** Auditors should include in the examination report all internal control deficiencies, even those communicated early, that are considered to be significant deficiencies or material weaknesses that the auditors identified based on the engagement work performed.<sup>60</sup>

<sup>59</sup>See paras. 2.16 through 2.19 for information on the GAGAS compliance statement.

<sup>60</sup>GAGAS's use of internal control terminology is consistent with the definitions contained in AU-C section 265, *Communicating Internal Control Related Matters Identified in an Audit* (AICPA, *Professional Standards*).

### Application Guidance: Reporting Deficiencies in Internal Control

**7.43** Determining whether and how to communicate to officials of the audited entity internal control deficiencies that are not considered significant deficiencies or material weaknesses is a matter of professional judgment.

### Reporting on Noncompliance with Provisions of Laws, Regulations, Contracts, and Grant Agreements or Instances of Fraud

#### Requirements: Reporting on Noncompliance with Provisions of Laws, Regulations, Contracts, and Grant Agreements or Instances of Fraud

**7.44** Auditors should include in their examination report the relevant information about noncompliance and fraud when auditors, based on sufficient, appropriate evidence, identify or suspect

- a. noncompliance with provisions of laws, regulations, contracts, or grant agreements that has a material effect on the subject matter or an assertion about the subject matter or
- b. fraud that is material, either quantitatively or qualitatively, to the subject matter or an assertion about the subject matter that is significant to the engagement objectives.

**7.45** When auditors identify or suspect noncompliance with provisions of laws, regulations, contracts, or grant agreements or instances of fraud that have an effect on the subject matter or an assertion about the subject matter that are less than material but warrant the attention of those charged with governance, they should communicate in writing to audited entity officials.

### Application Guidance: Reporting on Noncompliance with Provisions of Laws, Regulations, Contracts, or Grant Agreements or Instances of Fraud

**7.46** When auditors identify or suspect noncompliance with provisions of laws, regulations, contracts, or grant agreements or instances of fraud that do not warrant the attention of those charged with governance, the auditors' determination of whether and how to communicate such instances to audited entity officials is a matter of professional judgment.

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**7.47** When auditors identify or suspect noncompliance with provisions of laws, regulations, contracts, or grant agreements or instances of fraud, 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.

**Presenting Findings in the  
Report**

**Requirements: Presenting Findings in the Report**

**7.48** When presenting findings, auditors should develop the elements of the findings to the extent necessary to assist management or oversight officials of the audited entity in understanding the need for taking corrective action.

**7.49** 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 findings. To give the reader a basis for judging the prevalence and consequences of the findings, auditors should, as appropriate, 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. If the results cannot be projected, auditors should limit their conclusions appropriately.

**Application Guidance: Presenting Findings in the Report**

**7.50** Along with assisting management or oversight officials of the audited entity in understanding the need for taking corrective action, clearly developed findings assist auditors in making recommendations for corrective action. If auditors sufficiently develop the elements of a finding, they may provide recommendations for corrective action.

**Reporting Findings  
Directly to Parties outside  
the Audited Entity**

**Requirements: Reporting Findings Directly to Parties outside the  
Audited Entity**

**7.51** Auditors should report identified or suspected noncompliance with provisions of laws, regulations, contracts, and grant agreements and

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instances of fraud directly to parties outside the audited entity in the following two circumstances.

- a. When audited 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 audited entity management fails to take timely and appropriate steps to respond to fraud or noncompliance with provisions of laws, regulations, contracts, and grant agreements 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 audited entity's failure to take timely and appropriate steps directly to the funding agency.

**7.52** Auditors should comply with the requirements in paragraph 7.51 even if they have resigned or been dismissed from the engagement prior to its completion.

**7.53** Auditors should obtain sufficient, appropriate evidence, such as confirmation from outside parties, to corroborate representations by management of the audited entity that it has reported engagement findings in accordance with laws, regulations, or funding agreements. When auditors are unable to do so, they should report such information directly, as discussed in paragraphs 7.51 and 7.52.

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### Application Guidance: Reporting Findings Directly to Parties outside the Audited Entity

**7.54** The reporting in paragraph 7.51 is in addition to any legal requirements to report such information directly to parties outside the audited entity.

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### Obtaining and Reporting the Views of Responsible Officials

#### Requirements: Obtaining and Reporting the Views of Responsible Officials

**7.55** Auditors should obtain and report the views of responsible officials of the audited entity concerning the findings, conclusions, and recommendations in the examination report, as well as any planned corrective actions.

**7.56** 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, provide a copy of the summary to the responsible officials to verify that the comments are accurately represented, and include the summary in their report.

**7.57** When the audited entity's comments are inconsistent or in conflict with the findings, conclusions, or recommendations in the draft report, 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 by sufficient, appropriate evidence.

**7.58** If the audited entity refuses to provide comments or is unable to provide comments within a reasonable period of time, the auditors should 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.

### Application Guidance: Obtaining and Reporting the Views of Responsible Officials

**7.59** 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 audited entity's responsible officials and the corrective actions they plan to take. Obtaining the comments in writing is preferred, but oral comments are acceptable. When 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. Technical comments address points of fact or are editorial in nature and do not address substantive issues, such as methodology, findings, conclusions, or recommendations.

**7.60** 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 engagement, and the parties are familiar with the findings and issues addressed in the draft report; or the auditors do not expect major disagreements with findings, conclusions, or recommendations in the draft report or major controversies with regard to the issues discussed in the draft report.

### Reporting Confidential or Sensitive Information

#### Requirements: Reporting Confidential or Sensitive Information

**7.61** If certain information is prohibited from public disclosure or is excluded from a report because of its confidential or sensitive nature, auditors should disclose in the report that certain information has been omitted and the circumstances that make the omission necessary.

**7.62** When circumstances call for omission of certain information, auditors should evaluate whether the omission could distort the examination engagement results or conceal improper or illegal practices and revise the report language as necessary to avoid report users drawing inappropriate conclusions from the information presented.

**7.63** When the audit organization is subject to public records laws, auditors should determine whether public records laws could affect 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. Auditors use professional judgment to determine the appropriate means to communicate the omitted information to management and those charged with governance considering, among other things, whether public records laws could affect the availability of classified or limited use reports.

### **Application Guidance: Reporting Confidential or Sensitive Information**

**7.64** If the report refers to the omitted information, the reference may be general and not specific. If the omitted information is not necessary to meet the engagement objectives, the report need not refer to its omission.

**7.65** 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 such information and distribute the report only to persons authorized by law or regulation to receive it.

**7.66** Additional circumstances associated with public safety, privacy, or 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 misuse of this information could cause. 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. In some instances, it may be appropriate to issue both a publicly available report with the sensitive information excluded and a limited use report. The auditors may consult with legal counsel regarding any requirements or other circumstances that may necessitate omitting certain information.

**7.67** Considering the broad public interest in the program or activity under examination assists auditors when deciding whether to exclude certain information from publicly available reports.

**7.68** In cases described in paragraph 7.63, the auditors may communicate general information in a written report and communicate

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detailed information orally. The auditors may consult with legal counsel regarding applicable public records laws.

## Distributing Reports

### **Requirement: Distributing Reports**

**7.69** Distribution of reports completed in accordance with GAGAS depends on the auditors' relationship with the audited organization and the nature of the information contained in the reports. Auditors should document any limitation on report distribution.

- a. An audit organization in a government entity should distribute reports to those charged with governance, to the appropriate audited entity officials, and to the appropriate oversight bodies or organizations requiring or arranging for the examination 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. A public accounting firm contracted to conduct an examination engagement in accordance with GAGAS should clarify report distribution responsibilities with the engaging party. If the contracting firm is responsible for the distribution, it should reach agreement with the party contracting for the examination engagement about which officials or organizations will receive the report and the steps being taken to make the report available to the public.

## Review Engagements

### Compliance with Standards

### **Requirement: Compliance with Standards**

**7.70** GAGAS establishes requirements for review engagements in addition to the requirements for reviews contained in the AICPA's SSAEs. Auditors should comply with the additional GAGAS

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requirements, along with the applicable AICPA requirements, when citing GAGAS in their review engagement reports.

**Licensing and Certification**

**Requirements: Licensing and Certification**

**7.71** Auditors engaged to conduct review engagements in the United States who do not work for a government audit organization should be licensed CPAs, persons working for licensed certified public accounting firms, or licensed accountants in states that have multiclass licensing systems that recognize licensed accountants other than CPAs.

**7.72** Auditors engaged to conduct review engagements of entities operating outside of the United States who do not work for a government audit organization should meet the qualifications indicated in paragraph 7.71, have certifications that meet all applicable national and international standards and serve in their respective countries as the functional equivalent of CPAs in the United States, or work for nongovernment audit organizations that are the functional equivalent of licensed certified public accounting firms in the United States.

**Noncompliance with  
Provisions of Laws,  
Regulations, Contracts,  
and Grant Agreements**

**Requirement: Noncompliance with Provisions of Laws,  
Regulations, Contracts, and Grant Agreements**

**7.73** Auditors should extend the AICPA requirements concerning consideration of noncompliance with laws and regulations to include consideration of noncompliance with provisions of contracts and grant agreements.<sup>61</sup>

<sup>61</sup>See paras. .23 and .24 of AT-C section 210, *Review Engagements* (AICPA, *Professional Standards*).

## Reporting Auditors' Compliance with GAGAS

### Requirement: Reporting Auditors' Compliance with GAGAS

**7.74** When auditors comply with all applicable requirements for a review engagement conducted in accordance with GAGAS, they should include a statement in the review report that they conducted the engagement in accordance with GAGAS.<sup>62</sup>

### Application Guidance: Reporting Auditors' Compliance with GAGAS

**7.75** Because GAGAS incorporates by reference the AICPA's attestation standards, GAGAS does not require auditors to cite compliance with the AICPA standards when they cite compliance with GAGAS. GAGAS does not prohibit auditors from issuing a separate report conforming only to the requirements of the AICPA or other standards setters.

**7.76** Because review engagements are substantially less in scope than audits and examination engagements, it is important to include all required reporting elements contained in the standards used in conjunction with GAGAS. Including only those elements that the reporting standards for review engagements require or permit helps ensure that auditors comply with the standards and that users of GAGAS reports have an understanding of the nature of the work performed and the results of the review engagement.

## Distributing Reports

### Requirement: Distributing Reports

**7.77** Distribution of reports completed in accordance with GAGAS depends on the auditors' relationship with the audited organization and the nature of the information contained in the reports. If the subject matter or the assertion involves material that is classified or contains confidential or sensitive information, auditors should limit report distribution. Auditors should document any limitation on report distribution.

- a. An audit organization in a government entity should distribute reports to those charged with governance, to the appropriate

<sup>62</sup>See paras. 2.16 through 2.19 for information on the GAGAS compliance statement.

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audited 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 and to others authorized to receive such reports.

- b. A public accounting firm contracted to conduct a review engagement in accordance with GAGAS should clarify report distribution responsibilities with the engaging party. If the contracting firm is responsible for 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.

## Agreed-Upon Procedures Engagements

### Compliance with Standards

**Requirement: Compliance with Standards**

**7.78** GAGAS establishes requirements for agreed-upon procedures engagements in addition to the requirements for agreed-upon procedures engagements contained in the AICPA's SSAEs. Auditors should comply with the additional GAGAS requirements, along with the applicable AICPA requirements, when citing GAGAS in their agreed-upon procedures engagement reports.

### Licensing and Certification

**Requirements: Licensing and Certification**

**7.79** Auditors engaged to conduct agreed-upon procedures engagements in the United States who do not work for a government audit organization should be licensed CPAs, persons working for licensed certified public accounting firms, or licensed accountants in

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states that have multiclass licensing systems that recognize licensed accountants other than CPAs.

**7.80** Auditors engaged to conduct agreed-upon procedures engagements of entities operating outside of the United States who do not work for a government audit organization should meet the qualifications indicated in paragraph 7.79, have certifications that meet all applicable national and international standards and serve in their respective countries as the functional equivalent of CPAs in the United States, or work for nongovernment audit organizations that are the functional equivalent of licensed certified public accounting firms in the United States.

**Noncompliance with  
Provisions of Laws,  
Regulations, Contracts,  
and Grant Agreements**

**Requirement: Noncompliance with Provisions of Laws,  
Regulations, Contracts, and Grant Agreements**

**7.81** Auditors should extend the AICPA requirements concerning consideration of noncompliance with laws and regulations to include consideration of noncompliance with provisions of contracts and grant agreements.<sup>63</sup>

**Reporting Auditors'  
Compliance with GAGAS**

**Requirement: Reporting Auditors' Compliance with GAGAS**

**7.82** When auditors comply with all applicable GAGAS requirements for agreed-upon procedures engagements, they should include a statement in the agreed-upon procedures engagement report that they conducted the engagement in accordance with GAGAS.<sup>64</sup>

<sup>63</sup>See para. .41 of AT-C section 215, *Agreed-Upon Procedures Engagements* (AICPA, *Professional Standards*).

<sup>64</sup>See paras. 2.16 through 2.19 for information on the GAGAS compliance statement.

### Application Guidance: Reporting Auditors' Compliance with GAGAS

**7.83** Because GAGAS incorporates by reference the AICPA's attestation standards, GAGAS does not require auditors to cite compliance with the AICPA standards when citing compliance with GAGAS. GAGAS does not prohibit auditors from issuing a separate report conforming only to the requirements of the AICPA or other standards.

**7.84** Because agreed-upon procedures engagements are substantially less in scope than audits and examination engagements, it is important not to deviate from the required reporting elements contained in the attestation standards incorporated by reference in GAGAS, other than including the reference to GAGAS. For example, a required element of the report on agreed-upon procedures is a statement that the auditors were not engaged to and did not conduct an examination or a review of the subject matter, the objective of which would be the expression of an opinion or a conclusion, respectively, and that had the auditors performed additional procedures, other matters may have come to their attention that would have been reported.<sup>65</sup> Including only those elements that the AICPA reporting standards for agreed-upon procedures engagements require or permit helps ensure that auditors comply with the AICPA standards and that users of GAGAS reports understand the nature of the work performed and the results of the agreed-upon procedures engagement.

## Distributing Reports

### Requirement: Distributing Reports

**7.85** Distribution of reports completed in accordance with GAGAS depends on the auditors' relationship with the audited organization and the nature of the information contained in the reports. If the subject matter or the assertion involves material that is classified or contains confidential or sensitive information, auditors should limit the report distribution. Auditors should document any limitation on report distribution.

- a. An audit organization in a government entity should distribute reports to those charged with governance, to the appropriate

<sup>65</sup>See para. .34(o) and .34(q) of AT-C section 215, *Agreed-Upon Procedures Engagements* (AICPA, *Professional Standards*).

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audited 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 and to others authorized to receive such reports.

- b. A public accounting firm contracted to conduct an agreed-upon procedures engagement in accordance with GAGAS should clarify report distribution responsibilities with the engaging party. If the contracting firm is responsible for 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.

Reviews of Financial Statements

Compliance with Standards

Requirement: Compliance with Standards

7.86 GAGAS establishes requirements for reviews of financial statements in addition to the requirements for reviews of financial statements contained in the AICPA's AR-C section 90, Review of Financial Statements.66 Auditors should comply with the additional GAGAS requirements, along with the applicable AICPA requirements, when citing GAGAS in their review engagement reports.

Licensing and Certification

Requirements: Licensing and Certification

7.87 Auditors engaged to conduct reviews of financial statements in the United States who do not work for a government audit organization should be licensed CPAs, persons working for licensed certified public

66AICPA, Professional Standards.



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accounting firms, or licensed accountants in states that have multiclass licensing systems that recognize licensed accountants other than CPAs.

**7.88** Auditors engaged to conduct reviews of financial statements of entities operating outside of the United States who do not work for a government audit organization should meet the qualifications indicated in paragraph 7.87, have certifications that meet all applicable national and international standards and serve in their respective countries as the functional equivalent of CPAs in the United States, or work for nongovernment audit organizations that are the functional equivalent of licensed certified public accounting firms in the United States.

**Noncompliance with  
Provisions of Laws,  
Regulations, Contracts,  
and Grant Agreements**

**Requirement: Noncompliance with Provisions of Laws,  
Regulations, Contracts, and Grant Agreements**

**7.89** Auditors should extend the AICPA requirements concerning consideration of noncompliance with laws and regulations to include consideration of noncompliance with provisions of contracts and grant agreements.<sup>67</sup>

**Reporting Auditors'  
Compliance with GAGAS**

**Requirement: Reporting Auditors' Compliance with GAGAS**

**7.90** When auditors comply with all applicable requirements for a review of financial statements conducted in accordance with GAGAS, they should include a statement in the report that they conducted the engagement in accordance with GAGAS.<sup>68</sup>

<sup>67</sup>See paras. .34 through .36 of AR-C section 90, *Review of Financial Statements* (AICPA, *Professional Standards*).

<sup>68</sup>See paras. 2.16 through 2.19 for information on the GAGAS compliance statement.

### Application Guidance: Reporting Auditors' Compliance with GAGAS

**7.91** Because GAGAS incorporates by reference the AICPA's AR-C section 90, *Review of Financial Statements*,<sup>69</sup> GAGAS does not require auditors to cite compliance with the AICPA standards when they cite compliance with GAGAS. GAGAS does not prohibit auditors from issuing a separate report conforming only to the requirements of the AICPA or other standards setters.

**7.92** Because reviews of financial statements are substantially less in scope than audits and examination engagements, it is important to include all required reporting elements contained in the standards used in conjunction with GAGAS. For example, a required reporting element of the review of financial statements under AR-C section 90, *Review of Financial Statements*,<sup>70</sup> is to include a statement that a review is substantially less in scope than an audit, the objective of which is the expression of an opinion regarding the financial statements as a whole and that accordingly the accountant does not express such an opinion.<sup>71</sup> Including only those elements that the reporting standards for review of financial statements engagements require or permit helps ensure that auditors comply with the standards and that users of GAGAS reports have an understanding of the nature of the work performed and the results of the review engagement.

## Distributing Reports

### Requirement: Distributing Reports

**7.93** Distribution of reports completed in accordance with GAGAS depends on the auditors' relationship with the audited organization and the nature of the information contained in the reports. If the subject matter involves material that is classified or contains confidential or sensitive information, auditors should limit report distribution. Auditors should document any limitation on report distribution.

<sup>69</sup>AICPA, *Professional Standards*.

<sup>70</sup>AICPA, *Professional Standards*.

<sup>71</sup>See para. .76(c)(vi) of AR-C section 90, *Review of Financial Statements* (AICPA, *Professional Standards*).

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**Chapter 7: Standards for Attestation  
Engagements and Reviews of Financial  
Statements**

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- a.** An audit organization in a government entity should distribute reports to those charged with governance, to the appropriate audited 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 and to others authorized to receive such reports.
- b.** A public accounting firm contracted to conduct a review of financial statements engagement in accordance with GAGAS should clarify report distribution responsibilities with the engaging party. If the contracting firm is responsible for 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.

# Chapter 8: Fieldwork Standards for Performance Audits

**8.01** This chapter contains fieldwork requirements and guidance for performance audits conducted in accordance with generally accepted government auditing standards (GAGAS). Fieldwork requirements establish an overall approach for auditors to apply in planning and performing an audit to obtain sufficient, appropriate evidence that provides a reasonable basis for findings and conclusions based on the audit objectives. For performance audits conducted in accordance with GAGAS, the requirements and guidance in chapters 1 through 5 and chapter 9 also apply.

**8.02** The fieldwork requirements for performance audits relate to planning the audit; conducting the engagement; supervising staff; obtaining sufficient, appropriate evidence; and preparing audit documentation. The concepts of evidence, significance, and audit risk form a framework for applying these requirements and are included throughout the discussion of performance audits.

## Planning

### Requirements: General

**8.03** Auditors must adequately plan the work necessary to address the audit objectives. Auditors must document the audit plan.

**8.04** Auditors must plan the audit to reduce audit risk to an acceptably low level.

**8.05** In planning the audit, auditors should assess significance and audit risk. Auditors should apply these assessments to establish the scope and methodology for addressing the audit objectives. Planning is a continuous process throughout the audit.

**8.06** Auditors should design the methodology to obtain sufficient, appropriate evidence that provides a reasonable basis for findings and conclusions based on the audit objectives and to reduce audit risk to an acceptably low level.

**8.07** Auditors should identify and use suitable criteria based on the audit objectives.

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**Application Guidance: General**

**8.08** The audit objectives are what the audit is intended to accomplish. They identify the audit subject matter and performance aspects to be included. Audit objectives can be thought of as questions about the program that the auditors seek to answer based on evidence obtained and assessed against criteria. Audit objectives may also pertain to the current status or condition of a program. The term program as used in GAGAS includes processes, projects, studies, policies, operations, activities, entities, and functions.

**8.09** Auditors may need to refine or adjust the audit objectives, scope, and methodology as work is performed. However, in situations where the audit objectives are established by statute or legislative oversight, auditors may not have latitude to define or adjust the audit objectives or scope.

**8.10** 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.

**8.11** 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 perform to address the audit objectives.

**8.12** Obtaining sufficient, appropriate evidence provides auditors with a reasonable basis for findings and conclusions that are valid, accurate, appropriate, and complete with respect to the audit objectives.

**8.13** The sufficiency and appropriateness of evidence needed and tests of evidence are determined by the auditors 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 and in evaluating whether sufficient, appropriate evidence has been obtained to address the audit objectives.

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**Chapter 8: Fieldwork Standards for  
Performance Audits**

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**8.14** In performance audits conducted in accordance with GAGAS, auditors are the party who measures or evaluates the subject matter of the engagement and who presents the resulting information as part of, or accompanying, the audit report. Therefore, GAGAS does not require auditors to obtain management assertions with respect to the subject matter when conducting a performance audit.

**8.15** The concept of significance 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 matter's effect on the audited program or activity. Professional judgment assists auditors when evaluating the significance of matters within the context of the audit objectives. In the performance audit requirements, the term significant is comparable to the term material as used in the context of financial statement engagements.

**8.16** 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 or appropriate, an inadequate audit process, or intentional omissions or misleading information because of misrepresentation or fraud. The assessment of audit risk involves both qualitative and quantitative considerations. Factors affecting audit risk include 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 for preventing and detecting inconsistencies, significant errors, or fraud; and auditors' access to records. Audit risk includes the risk that 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 specialists, additional reviewers, and other resources to conduct the audit; 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.

**8.17** 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 in the report. Suitable criteria are relevant, reliable, objective, and understandable and do not result in the omission of significant information, as applicable, within the context of the audit objectives. The relative importance of each of these characteristics to a particular engagement is a matter of professional judgment. In instances where laws, regulations, or policies prescribe the criteria to be used for the engagement, such criteria are presumed to be suitable in the absence of indications to the contrary.

**8.18** Examples of criteria include

- a. laws and regulations applicable to the operation of the audited entity;
- b. goals, 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. contracts or grant agreements; and
- h. benchmarks against which performance is compared, including performance of other entities or sectors.

**8.19** For audit objectives that pertain to the current status or condition of a program, sufficient, appropriate evidence is gathered to provide reasonable assurance that the description of the current status or condition of a program is accurate and reliable and does not omit significant information relevant to the audit objectives. Information addressing the audit objectives is to be provided in an objective, understandable manner. The relative importance of each of the characteristics of the information to a particular engagement is a matter of professional judgment.

## Auditor Communication

**Requirements: Auditor Communication**

**8.20** Auditors should communicate an overview of the objectives, scope, and methodology and the timing of the performance audit and planned reporting (including any potential restrictions on the report), unless doing so could significantly impair the auditors' ability to obtain sufficient, appropriate evidence to address the audit objectives. Auditors should communicate such information with the following parties, 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;
- c. the individuals contracting for or requesting audit services, such as contracting officials or grantees; or
- d. the cognizant legislative committee, when auditors conduct the audit pursuant to a law or regulation or when they conduct the work for the legislative committee that has oversight of the audited entity.

**8.21** In situations where the parties required to receive communications, as described in paragraph 8.20, are not clearly evident, auditors should document the process followed and conclusions reached in identifying the appropriate individuals to receive the required communications.

**8.22** Auditors should retain any written communication resulting from paragraph 8.20 as audit documentation.

**Application Guidance: Auditor Communication**

**8.23** Determining the form, content, and frequency of the communication with management or those charged with governance is a matter of professional judgment, although written communication is preferred. Auditors may use an engagement letter to communicate key information early in the engagement.



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**8.24** Examples of communications regarding the objectives, scope, methodology, and timing that could impair the auditors' ability to obtain sufficient, appropriate evidence include situations in which the auditors plan to perform unannounced cash counts or perform procedures related to indications of fraud.

**8.25** Communicating with those charged with governance or management may include communicating deficiencies in internal control; fraud; or noncompliance with provisions of laws, regulations, contracts, and grant agreements. Early communication of these matters may be important because of their relative significance and the urgency for corrective follow-up action. Further, early communication is important to allow management to take prompt corrective action to prevent further occurrences when a control deficiency results in noncompliance with provisions of laws, regulations, contracts, and grant agreements or fraud. When a deficiency is communicated early, the reporting requirements and application guidance in paragraphs 9.29 through 9.44 still apply.

**8.26** 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. The process for identifying those charged with governance includes evaluating the organizational structure for directing and controlling operations to achieve the audited entity's objectives and how the audited entity delegates authority and establishes accountability for management.

**Investigations or Legal  
Proceedings**

**Requirement: Investigations or Legal Proceedings**

**8.27** Auditors should inquire of management of the audited entity whether any investigations or legal proceedings significant to the audit objectives have been initiated or are in process with respect to the period under audit, and should evaluate the effect of initiated or in-process investigations or legal proceedings on the current audit.

**Application Guidance: Investigations or Legal Proceedings**

**8.28** Laws, regulations, or policies may require auditors to report indications of the following to law enforcement or investigatory authorities before performing additional audit procedures: certain types of fraud or

noncompliance with provisions of laws, regulations, contracts, and grant agreements.

**8.29** Avoiding interference with investigations or legal proceedings is important in pursuing indications of fraud and noncompliance with provisions of laws, regulations, contracts, and grant agreements. In some cases, it may be appropriate for the auditors to work with investigators or legal authorities or to withdraw from or defer further work on the engagement or a portion of the engagement to avoid interfering with an ongoing investigation or legal proceeding.

## Results of Previous Engagements

### **Requirement: Results of Previous Engagements**

**8.30** 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 engagements 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.

## Assigning Auditors

### **Requirements: Assigning Auditors**

**8.31** Audit management should assign sufficient auditors with adequate collective professional competence, as described in paragraphs 4.02 through 4.15, to conduct the audit. Staffing an audit includes, among other things,

- a. assigning auditors with the collective knowledge, skills, and abilities appropriate for the audit;

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Performance Audits**

- b. assigning a sufficient number of auditors to the audit;
- c. providing for on-the-job training of auditors; and
- d. engaging specialists when necessary.

**8.32** If planning to use the work of specialists, auditors should document the nature and scope of the work to be performed by the specialists, including

- a. the objectives and scope of the specialists' work,
- b. the intended use of the specialists' work to support the audit objectives,
- c. the specialists' procedures and findings so they can be evaluated and related to other planned audit procedures, and
- d. the assumptions and methods used by the specialists.

**Preparing a Written Audit  
Plan**

**Requirement: Preparing a Written Audit Plan**

**8.33** Auditors must prepare a written audit plan for each audit. Auditors should update the plan, as necessary, to reflect any significant changes to the plan made during the audit.

**Application Guidance: Preparing a Written Audit Plan**

**8.34** 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.

**8.35** A written audit plan provides an opportunity for 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 conduct the audit and to meet expected time frames for completing the work.

## Conducting the Engagement

### Nature and Profile of the Program and User Needs

#### **Requirement: Nature and Profile of the Program and User Needs**

**8.36** 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 condition;
- 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. the program's strategic plan and objectives; and
- f. external factors or conditions that could directly affect the program.

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**Application Guidance: Nature and Profile of the Program and User Needs**

**8.37** One group of users of the audit report is government officials or other parties who authorize or request audits. Other important users of the audit report are the audited entity, those responsible for acting on the auditors' recommendations, oversight organizations, and legislative bodies. Other potential users of the audit report include legislators or government officials (other than those who 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.

**8.38** Obtaining an understanding of the program under audit helps auditors to assess the relevant risks associated with the program and the effect of the risks 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, observations, and reviewing documents while 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. Provisions of laws, regulations, contracts, and 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 contracts or grant agreements. Thus, understanding the laws and legislative history establishing a program and the provisions of contracts or grant agreements is essential to understanding the program itself. Obtaining that understanding is also a necessary step in identifying the provisions of laws, regulations, contracts, and 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 a program's purpose when they provide authority for the program. Audited entity officials may provide more detailed

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information on the program's purpose to supplement the authorizing legislation. Audited 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 is a process effected by an entity's oversight body, management, and other personnel that provides reasonable assurance that the objectives of an entity will be achieved. Internal control comprises the plans, methods, policies, and procedures used to fulfill the mission, strategic plan, goals, and objectives of the entity.
- d. **Inputs:** Inputs are the amount of resources (in terms of, for example, money, material, or personnel) that is put into a program. These resources may come from within or outside the entity operating the program. Measures of inputs can have a number of dimensions, such as cost, timing, and quality. Examples of measures of inputs are dollars spent, employee hours expended, and square feet of building space used.
- e. **Program operations:** Program operations are the strategies, processes, and activities management uses to convert inputs 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 workplace after a specified period. 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 purposes of helping unemployed citizens obtain and retain jobs and improving

the safety of aviation operations, respectively. 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 a program's unexpected or unintentional effects, both positive and negative.

### Determining Significance and Obtaining an Understanding of Internal Control

#### **Requirements: Determining Significance and Obtaining an Understanding of Internal Control**

**8.39** Auditors should determine and document whether internal control is significant to the audit objectives.<sup>72</sup>

**8.40** If it is determined that internal control is significant to the audit objectives, auditors should obtain an understanding of such internal control.

#### **Application Guidance: Determining Significance and Obtaining an Understanding of Internal Control**

**8.41** Consideration of internal control in a performance audit begins with determining the significance of internal control to the audit objectives and documenting that determination. Some factors that may be considered when determining the significance of internal control to the audit objectives include

- a. the subject matter under audit, such as the program or program component under audit, including the audited entity's objectives for the program and associated inherent risks;
- b. the nature of findings and conclusions expected to be reported, based on the needs and interests of audit report users;

<sup>72</sup>See fig.4 at the end of ch. 8 for a flowchart on consideration of internal control in a GAGAS performance audit.

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**Chapter 8: Fieldwork Standards for Performance Audits**

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- c. the three categories of entity objectives (operations, reporting, and compliance);<sup>73</sup> and
  - d. the five components of internal control (control environment, risk assessment, control activities, information and communication, and monitoring) and the integration of the components.

**8.42** If internal control is significant to the audit objectives, auditors determine which of the five components of internal control are significant to the audit objectives, as all components of internal control are generally relevant, but not all components may be significant to the audit objectives. This determination can also identify the underlying principles, control objectives, or specific controls that are significant to the audit objectives. Determining which internal control components, principles, control objectives, and/or specific controls are significant to the audit objectives is a matter of professional judgment.

**8.43** Determining the significance of internal control may be an iterative process. As discussed in paragraph 8.09, the audit objectives can evolve and become more refined throughout the audit. When this occurs, the significance of internal control is determined and documented for the new or revised objectives.

**8.44** Determining the significance of internal control may be documented in formats such as narratives or tables. The documentation includes the conclusions on whether internal control is significant to the audit objectives, and if so, which components of internal control are significant to the audit objectives. The documentation may also include the factors considered and steps taken to perform the determination.

**8.45** Determining the significance of internal control to the audit objectives affects the audit planning required in paragraphs 8.03 through 8.07. Specifically, it enables auditors to determine whether to assess internal control as part of the audit and, if they do, to identify criteria for the assessment and plan the appropriate scope, methodology, and extent of internal control assessments to perform.

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<sup>73</sup>The terminology used in this section is consistent with the definitions and concepts in the Committee of Sponsoring Organizations of the Treadway Commission's *Internal Control—Integrated Framework* (COSO Framework) and *Standards for Internal Control in the Federal Government* (GAO-14-704G) (Green Book).



**8.46** The nature and extent of procedures auditors perform to obtain an understanding of internal control is a matter of professional judgment and may vary among audits based on audit objectives, audit risk, internal control deficiencies, and the auditors' knowledge about internal control gained in prior audits. The understanding of internal control builds on the understanding of the program required in paragraph 8.36. The auditors' understanding of internal control may be obtained through procedures such as inquiries, observations, inspection of documents and records, review of other audit reports, or direct tests.

**8.47** Approaches for obtaining an understanding of internal control may vary and may include consideration of entity-level controls, transaction-level controls, or both. However, even when assessing only transaction-level controls, it may be beneficial to gain an understanding of entity-level controls that may affect transaction-level controls by obtaining a broad understanding of the five components of internal control at the entity level. This involves considering the relationships between the components, which work together in an integrated manner in an effective internal control system, and the principles of internal control that support each component. In addition to obtaining a broad understanding of internal control at the entity level, auditors may also obtain an understanding of internal control at the transaction level for the specific programs and processes under audit.

**8.48** Obtaining an understanding of internal control assists auditors in identifying an audited entity's key controls relevant to the audit objectives. Identifying key controls involves considering the entity's objectives that are relevant to the audit and whether the entity has controls in place to achieve those objectives and address associated risks. Collectively, key controls are those controls necessary to achieve the entity's control objectives and provide reasonable assurance of achieving the entity's objectives. Key controls often have one or both of the following characteristics:

- a. Their failure may significantly affect the achievement of the entity's objectives, yet not reasonably be detected in a timely manner by other controls.
- b. Their operation may prevent or detect other control failures before they have an opportunity to become significant to the achievement of the entity's objectives.

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## Assessing Internal Control

**Requirement: Assessing Internal Control**

**8.49** If internal control is determined to be significant to the audit objectives, auditors should plan and perform audit procedures to assess internal control to the extent necessary to address the audit objectives.

**Application Guidance: Assessing Internal Control**

**8.50** The auditors' understanding of internal control provides a basis for determining the nature, timing, and extent of procedures for assessments of internal control, if such an assessment will be performed. Assessments of internal control in a performance audit are performed to the extent necessary to address the audit objectives. The levels of internal control assessment that may be performed based on the audit objectives are (1) assessing the design; (2) assessing the design and implementation; or (3) assessing the design, implementation, and operating effectiveness of controls that are significant to the audit objectives.

**8.51** Assessments of internal control involve designing and performing procedures to obtain sufficient, appropriate evidence, as required in paragraphs 8.90 through 8.94, to support and document the auditors' findings and conclusions on design, implementation, and/or operating effectiveness of controls that are significant to the audit objectives. The controls being assessed are generally the key controls identified during the planning phase of the engagement, which may include controls at both the entity and transaction levels. Changes may be made to the initial determination of key controls based on additional information gathered during the course of fieldwork.

**8.52** The design of internal control is assessed by determining whether controls individually and in combination are capable of achieving an objective and addressing the related risk. The implementation of internal control is assessed by determining if the control exists and has been placed into operation. The operating effectiveness of internal control is assessed by determining whether controls were applied at relevant times during the period under evaluation, the consistency with which they were applied, and by whom or by what means they were applied. A control cannot be effectively implemented if it was not effectively designed. A control cannot be operating effectively if it was not effectively designed and implemented.

**8.53** During the assessment of each control, deficiencies in internal control may be identified. A deficiency in internal control exists when the design, implementation, or operation of a control does not allow management or personnel to achieve control objectives and address related risks.<sup>74</sup> A deficiency in design exists when a necessary control is missing or is not properly designed so that even if the control operates as designed, the control objective would not be met. A deficiency in implementation exists when a control is properly designed but not implemented correctly in the internal control system. A deficiency in operating effectiveness exists when a properly designed control does not operate as designed or the person performing the control does not have the necessary competence or authority to perform the control effectively.

## Internal Control Deficiencies Considerations

### Requirement: Internal Control Deficiencies Considerations

**8.54** Auditors should evaluate and document the significance of identified internal control deficiencies within the context of the audit objectives.

### Application Guidance: Internal Control Deficiencies Considerations

**8.55** Internal control deficiencies are evaluated for significance within the context of the audit objectives. Deficiencies are evaluated both on an individual basis and in the aggregate. Consideration is given to the correlation among deficiencies. This evaluation and the audit work performed form the basis of the auditors' determination whether, individually or in combination, the deficiencies are significant within the context of the audit objectives.<sup>75</sup>

**8.56** Determining whether deficiencies are significant within the context of the audit objectives involves evaluating the following factors:

- a. **Magnitude of impact:** Magnitude of impact refers to the likely effect that the deficiency could have on the entity achieving its objectives and is affected by factors such as the size, pace, and duration of

<sup>74</sup>See paras. 1.27g and 1.27k for definitions of control objective and entity objective.

<sup>75</sup>See paras. 9.29 through 9.34 for a discussion of reporting on internal control.

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the deficiency's impact. A deficiency may be more significant to one objective than another.

- b. Likelihood of occurrence: Likelihood of occurrence refers to the possibility of a deficiency impacting an entity's ability to achieve its objectives.
- c. Nature of the deficiency: The nature of the deficiency involves factors such as the degree of subjectivity involved with the deficiency and whether the deficiency arises from fraud or misconduct.

**8.57** Internal control deficiencies are a type of finding, and the requirements related to developing the four elements of a finding in paragraph 8.116 apply. When determining the cause of internal control deficiencies, it may be helpful for auditors to perform an analysis to identify the root cause of the deficiencies. Identifying the root causes of internal control deficiencies may strengthen the quality of auditors' recommendations for corrective actions.

**8.58** The following are examples of control deficiencies:

- a. Ineffective oversight by those charged with governance of the entity's financial reporting, performance reporting, or internal control, or an ineffective overall governance structure.
- b. 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 large or complex entity.
- c. Failure by management or those charged with governance to assess the effect of a deficiency previously communicated to them and either to correct it or to conclude that it does not need to be corrected.
- d. Inadequate controls for the safeguarding of assets.
- e. Inadequate design of information systems general, application, and user controls that prevents an information system from providing complete and accurate information consistent with financial, compliance, or performance reporting objectives or other current needs.

- f. Failure of an application control caused by a deficiency in the design or operation of an information system's general controls.
- g. Employees or management who lack the qualifications and training to fulfill their assigned functions.

## Information Systems Controls Considerations

### Requirements: Information Systems Controls Considerations

**8.59** The effectiveness of significant internal controls frequently depends on the effectiveness of information systems controls. 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.

**8.60** When information systems controls are determined to be significant to the audit objectives or when the effectiveness of significant controls depends on the effectiveness of information systems controls, auditors should then evaluate the design, implementation, and/or operating effectiveness of such controls. This evaluation includes other information systems controls that affect 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.

**8.61** 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.

**8.62** When evaluating information systems controls is an audit objective, auditors should test information systems controls to the extent necessary to address the audit objective.

### Application Guidance: Information Systems Controls Considerations

**8.63** 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 depend on information systems

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processing and include general controls, application controls, and user controls.

- a. Information systems general controls (entity-wide, system, and application levels) are the policies and procedures that apply to all or a large segment of an entity's information systems. General controls help 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.
- b. 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 file, interface, and the data management system.
- c. User controls are portions of controls that are performed by people interacting with information systems controls. A user control is an information systems control if its effectiveness depends on information systems processing or the reliability (accuracy, completeness, and validity) of information processed by information systems.

**8.64** An entity'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 these controls in order to obtain sufficient, appropriate evidence. For example, an audit objective may involve evaluating the effectiveness of information systems controls related to certain systems, facilities, or entities.

**8.65** 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, application, and user controls that are critical to providing assurance over the reliability of the information required for the audit.

**8.66** 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 or as a separate audit objective or audit procedure, depending on the audit's objectives. 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 hardware and software used, the configuration of the entity's systems and networks, and the entity's information systems strategy.

**8.67** The following factors may assist auditors in determining the significance of information system controls to the audit objectives:

- 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 depends on information systems controls, there may not be sufficient supporting or corroborating information or documentary evidence 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 auditors conclude that information systems controls are effective, they may reduce the direct testing of data.

## Provisions of Laws, Regulations, Contracts, and Grant Agreements

### **Requirement: Provisions of Laws, Regulations, Contracts, and Grant Agreements**

**8.68** Auditors should identify any provisions of laws, regulations, contracts, and grant agreements that are significant within the context of the audit objectives and assess the risk that noncompliance with provisions of laws, regulations, contracts, and grant agreements could occur. Based on that risk assessment, the auditors should design and perform procedures to obtain reasonable assurance of detecting instances of noncompliance with provisions of laws, regulations, contracts, and grant agreements that are significant within the context of the audit objectives.

### **Application Guidance: Provisions of Laws, Regulations, Contracts, and Grant Agreements**

**8.69** Government programs are subject to many provisions of laws, regulations, contracts, and grant agreements. At the same time, these provisions' significance within the context of the audit objectives varies widely, depending on the objectives of the audit. Auditors may consult with their legal counsel to (1) determine those laws and regulations that are significant to the audit objectives, (2) design tests of compliance with provisions of laws and regulations, and (3) evaluate the results of those tests. Auditors also may consult with their 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 law enforcement authorities, to obtain information on compliance matters.

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



## Fraud

**Requirements: Fraud**

**8.71** Auditors should assess the risk of fraud 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 increase the risk of fraud. Auditors should gather and assess information to identify the risk of fraud that is significant within the scope of the audit objectives or that could affect the findings and conclusions.

**8.72** Assessing the risk of fraud is an ongoing process throughout the audit. When information comes to the auditors' attention indicating that fraud, 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.

**Application Guidance: Fraud**

**8.73** Fraud involves obtaining something of value through willful misrepresentation. Whether an act is, in fact, fraud is determined through the judicial or other adjudicative system and is beyond auditors' professional responsibility.

**8.74** Auditors may obtain information through discussion with officials of the audited entity or through other means to determine the susceptibility of a program to fraud, the extent to which the audited entity has implemented leading practices to manage fraud risks, the status of internal controls the audited entity has established to prevent and detect fraud, or the risk that officials of the audited entity could override internal control. An attitude of professional skepticism in assessing the risk of fraud assists auditors in assessing which factors or risks could significantly affect the audit objectives.

**8.75** In some circumstances, conditions such as the following could indicate a heightened risk of fraud:

- a. economic, programmatic, or entity operating conditions that threaten the entity's financial stability, viability, or budget;

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- b. the nature of the entity's operations provide opportunities to engage in fraud;
  - c. management's monitoring of compliance with laws, regulations, and policies is inadequate;
  - d. the organizational structure is unstable or unnecessarily complex;
  - e. management communication or support for ethical standards is lacking;
  - f. management is willing to accept unusually high levels of risk in making significant decisions;
  - g. the entity has a history of impropriety, such as previous issues with fraud, 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. asset accountability or safeguarding procedures are lacking;
  - k. a history of improper payments;
  - l. evidence of false or misleading information; and
  - m. evidence of unusual patterns and trends in contracting, procurement, acquisition, and other activities of the entity or program.

**8.76** If fraud that may have occurred is not significant within the context of the audit objectives, the auditors may perform additional audit work as a separate engagement or refer the matter to other parties with oversight responsibility or jurisdiction.

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

### Requirements: Identifying Sources of Evidence and the Amount and Type of Evidence Required

**8.77** 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.

**8.78** Auditors should evaluate whether any lack of sufficient, appropriate evidence is caused by internal control deficiencies or other program weaknesses, and whether the lack of sufficient, appropriate evidence could be the basis for audit findings.

### Application Guidance: Identifying Sources of Evidence and the Amount and Type of Evidence Required

**8.79** If auditors believe 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.

## Using the Work of Others

### Requirements: Using the Work of Others

**8.80** Auditors should determine whether other auditors have conducted, or are conducting, audits that could be relevant to the current audit objectives.

**8.81** 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 can be relied on in the context of the current audit objectives.<sup>76</sup>

<sup>76</sup>See para. 5.175 for additional discussion on using the work of other auditors and peer review reports.

**8.82** If the engagement team intends to use the work of a specialist, it should assess the independence of the specialist.<sup>77</sup>

### Application Guidance: Using the Work of Others

**8.83** The results of other auditors' work may be useful sources of information for planning and conducting 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.

**8.84** Internal auditing 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. Auditors may determine that it is appropriate to use the work of the internal auditors in assessing the effectiveness of design or operation of internal controls that are significant within the context of the audit objectives.

**8.85** 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 effort. Procedures that auditors may perform in making this determination include reviewing the other audit report, audit plan, or audit documentation, 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.

**8.86** The engagement team's assessment of the independence of specialists who perform audit work includes identifying threats and applying any necessary safeguards in the same manner as they would for auditors performing work on those audits.<sup>78</sup>

<sup>77</sup>See para. 1.27p for the definition of specialist.

<sup>78</sup>See paras. 3.18 through 3.108 for requirements and guidance related to independence.

## Supervision

### Requirement: Supervision

**8.87** Auditors must properly supervise audit staff.

### Application Guidance: Supervision

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

**8.89** The nature and extent of the auditors' supervision 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 auditors.

## Evidence

### Requirements: Evidence

**8.90** Auditors must obtain sufficient, appropriate evidence to provide a reasonable basis for addressing the audit objectives and supporting their findings and conclusions.

**8.91** In assessing the appropriateness of evidence, auditors should assess whether the evidence is relevant, valid, and reliable.

**8.92** 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 to the extent that would persuade a knowledgeable person that the findings are reasonable.

**8.93** When auditors use information provided 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.

**8.94** Auditors should evaluate the objectivity, credibility, and reliability of testimonial evidence.

### **Application Guidance: Evidence**

**8.95** Audit objectives may vary widely, as may the level of work necessary to assess the sufficiency and appropriateness of evidence to address the objectives. The concepts of audit risk and significance assist auditors in evaluating the audit evidence. 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 determining the sufficiency and appropriateness of evidence and in reporting the results of the audit work.

**8.96** When auditors use information that audited entity officials provided as part of their evidence, auditors may find it necessary to test management's procedures to obtain assurance, perform direct testing of the information, or obtain additional corroborating evidence. The nature, timing, 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. Using a risk-based approach, auditors may consider additional procedures if they become aware of evidence that conflicts with that provided by management. In their overall assessment, auditors may document how they resolved situations involving conflicting evidence.<sup>79</sup>

**8.97** Auditors may request that management provide written representations as to the accuracy and completeness of information provided.

**8.98** The nature, timing, and extent of audit procedures to assess sufficiency and appropriateness are affected by the effectiveness of the audited 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 the context of the audit objectives. The sufficiency and appropriateness of computer-processed information is assessed regardless of whether this

<sup>79</sup>See para. 8.105 for a discussion of the relationship between testimonial and documentary evidence.

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information is provided to auditors or auditors independently extract it. Assessing the sufficiency and appropriateness of computer-processed information includes considering the completeness and accuracy of the data for the intended purposes.

### *Sufficiency*

**8.99** Sufficiency is a measure of the quantity of evidence used to support the findings and conclusions related to the audit objectives.

**8.100** When appropriate, auditors may use statistical methods to analyze and interpret evidence to assess its sufficiency.

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

- 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.

### *Appropriateness*

**8.102** 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.

- 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 a meaningful or reasonable basis for measuring what is being evaluated. In other words, validity refers to the extent to which evidence represents what it is purported to represent.
- c. Reliability refers to the consistency of results when information is measured or tested and includes the concepts of being verifiable or supported. For example, in establishing the appropriateness of evidence, auditors may test its reliability by obtaining supporting evidence, using statistical testing, or obtaining corroborating evidence.

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

**8.103** The degree of assurance associated with a performance audit is strongly associated with the appropriateness of evidence in relation to the audit objectives. Examples follow.

- 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 audited entity. In these situations, the auditors may be provided information that the audited entity compiled in order to satisfy the audit objectives. The auditors 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 perform procedures to verify the information. These decisions call for use of 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 of the extent to which comparative information or statistics were evaluated or corroborated will likely be necessary to place the evidence in context for report users.



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- e. The audit objectives might focus on trend information based on data that the audited entity provided. In this situation, auditors may assess the evidence by using overall analytical tests of underlying data, combined with knowledge and understanding of the systems or processes used for compiling information.
  - f. The audit objectives might focus on identifying emerging and crosscutting issues using information that audited entities compiled or self-reported. In such cases, it may be helpful for the auditors 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.

**8.104** 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 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. Evidence may be obtained by observation, inquiry, or inspection. Each type of evidence has its own strengths and weaknesses. 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 used to support auditors' findings and conclusions are matters of the auditors' professional judgment based on the audit objectives and audit risk.

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- a. Evidence obtained when internal control is effective is generally more reliable than evidence obtained when internal control is weak or nonexistent.<sup>80</sup>
  - 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 obtained from management of the audited entity or others who have a direct interest in the audited entity.

**8.105** Testimonial evidence may be useful in interpreting or corroborating documentary or physical information. Documentary evidence may be used to help verify, support, or challenge testimonial evidence.

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

**8.107** When sampling is used, the appropriate selection method 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

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<sup>80</sup>See paras. 8.39 through 8.67 for a discussion of internal control.

effective if the auditors have isolated risk factors or other criteria to target the selection.

## Overall Assessment of Evidence

### Requirements: Overall Assessment of Evidence

**8.108** 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 performed to conclude on the validity and reliability of specific evidence.

**8.109** When assessing the overall 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. If auditors conclude that evidence is not sufficient or appropriate, they should not use such evidence as support for findings and conclusions.

**8.110** When the auditors identify limitations or uncertainties in evidence that is significant to the audit findings and conclusions, they should perform additional procedures, as appropriate.

### Application Guidance: Overall Assessment of Evidence

**8.111** 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.

**8.112** Sufficiency and appropriateness of evidence are relative concepts, which may be thought of as 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 identify 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.

**8.113** 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.

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- 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 appropriate when (1) using the evidence carries an unacceptably high risk that it could lead auditors to reach 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.

**8.114** Evidence has limitations or uncertainties when its validity or reliability 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.

**8.115** Additional procedures that could address limitations or uncertainties in evidence that are significant to the audit findings and conclusions include

- a. seeking independent, corroborating evidence from other sources;
- b. redefining the audit objectives or 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; and
- d. determining whether to report the limitations or uncertainties as a finding, including any related significant internal control deficiencies.

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## Findings

### Requirements: Findings

**8.116** As part of a performance audit, when auditors identify findings, they should plan and perform procedures to develop the criteria,

condition, cause, and effect of the findings to the extent that these elements are relevant and necessary to achieve the audit objectives.

**8.117** Auditors should consider internal control deficiencies in their evaluation of identified findings when developing the cause element of the identified findings when internal control is significant to the audit objectives.

### **Application Guidance: Findings**

**8.118** Findings may involve deficiencies in internal control; noncompliance with provisions of laws, regulations, contracts, and grant agreements; or instances of fraud.

**8.119** Given the concept of accountability for use of public resources and government authority, evaluating internal control in a government environment may also include considering internal control deficiencies that result in waste or abuse. Because the determination of waste and abuse is subjective, auditors are not required to perform specific procedures to detect waste or abuse in performance audits. However, auditors may consider whether and how to communicate such matters if they become aware of them. Auditors may also discover that waste or abuse are indicative of fraud or noncompliance with provisions of laws, regulations, contracts, and grant agreements.

**8.120** Waste is the act of using or expending resources carelessly, extravagantly, or to no purpose. Importantly, waste can include activities that do not include abuse and does not necessarily involve a violation of law. Rather, waste relates primarily to mismanagement, inappropriate actions, and inadequate oversight.

**8.121** The following are examples of waste, depending on the facts and circumstances:

- a. Making travel choices that are contrary to existing travel policies or are unnecessarily extravagant or expensive.
- b. Making procurement or vendor selections that are contrary to existing policies or are unnecessarily extravagant or expensive.

**8.122** Abuse is 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, but excludes fraud and noncompliance with provisions of laws, regulations, contracts, and grant agreements. Abuse also includes misuse of authority or position for personal financial interests or those of an immediate or close family member or business associate.

**8.123** 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).

**8.124** Criteria: To develop findings, criteria may include 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. The term program includes processes, projects, studies, policies, operations, activities, entities, and functions. Criteria provide a context for evaluating evidence and understanding the findings, conclusions, and recommendations in the report.

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

**8.126** Cause: The cause is the factor or factors responsible for the difference between the condition and the criteria, and 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

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program management. Auditors may assess whether the evidence provides a reasonable and convincing argument for why the stated cause is the key factor contributing to the difference between the condition and the criteria.

**8.127** Effect or potential effect: The effect or potential effect is the outcome or consequence resulting from the difference between the condition and the criteria. 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.

**8.128** The elements needed for a finding are related to 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 to determine 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 developing the other elements of a finding would not be necessary.

**8.129** The cause of a finding may relate to an underlying internal control deficiency. For example, auditors conducting a compliance audit may find that an audited entity has not complied with certain legislation. Upon further evaluation, the auditors may find the root cause of the finding to be that one of the entity's control activities was not properly designed. In this case, the finding would be an instance of noncompliance, but the cause of the finding would be an internal control deficiency.

**8.130** Considering internal control in the context of a comprehensive internal control framework, such as *Standards for Internal Control in the Federal Government* or *Internal Control—Integrated Framework*,<sup>81</sup> can help auditors to determine whether underlying internal control deficiencies

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<sup>81</sup>The COSO Framework and the Green Book provide suitable and available criteria against which management may evaluate and report on the effectiveness of the entity's internal control. The Green Book may be adopted by entities beyond those federal entities for which it is legally required, such as state, local, and quasi-governmental entities, as well as other federal entities and not-for-profit organizations, as a framework for an internal control system.

exist as the root cause of findings. When the audit objectives include explaining why a particular type of positive or negative program performance, output, or outcome identified in the audit occurred, the underlying deficiencies are referred to as cause. Identifying the cause of problems may assist auditors in making constructive recommendations for correction. 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.

**8.131** 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 program’s impact. 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

### Requirements: Audit Documentation

**8.132** 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, having no previous connection to the audit, to understand from the audit documentation the nature, timing, extent, and results of audit procedures performed; the evidence obtained; and its source and the conclusions reached, including evidence that supports the auditors’ significant judgments and conclusions.

**8.133** Auditors should prepare audit documentation that contains evidence that supports the findings, conclusions, and recommendations before they issue their report.

**8.134** 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.

**8.135** Auditors should document the following:

- a. the objectives, scope, and methodology of the audit;
- b. the work performed and evidence obtained to support significant judgments and conclusions, as well as expectations in analytical procedures, including descriptions of transactions and records examined (for example, by listing file numbers, case numbers, or other means of identifying specific documents examined, though copies of documents examined or detailed listings of information from those documents are not required); and
- c. supervisory review, before the audit report is issued, of the evidence that supports the findings, conclusions, and recommendations contained in the audit report.

**8.136** When auditors do not comply with applicable GAGAS requirements because of law, regulation, scope limitations, restrictions on access to records, or other issues affecting the audit, the auditors should document the departure from the GAGAS requirements and the impact on the audit and on the auditors' conclusions.

### Application Guidance: Audit Documentation

**8.137** 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 audit report, (2) aid auditors in conducting and supervising the audit, and (3) allow for the review of audit quality.

**8.138** 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 conduct 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

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the audit objectives, and (4) issues related to the audited entity's environment.

**8.139** When documenting departures from the GAGAS requirements, the audit documentation requirements apply to departures from unconditional requirements and from presumptively mandatory requirements when alternative procedures performed in the circumstances were not sufficient to achieve the objectives of the requirements.

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**Availability of Individuals  
and Documentation****Requirement: Availability of Individuals and Documentation**

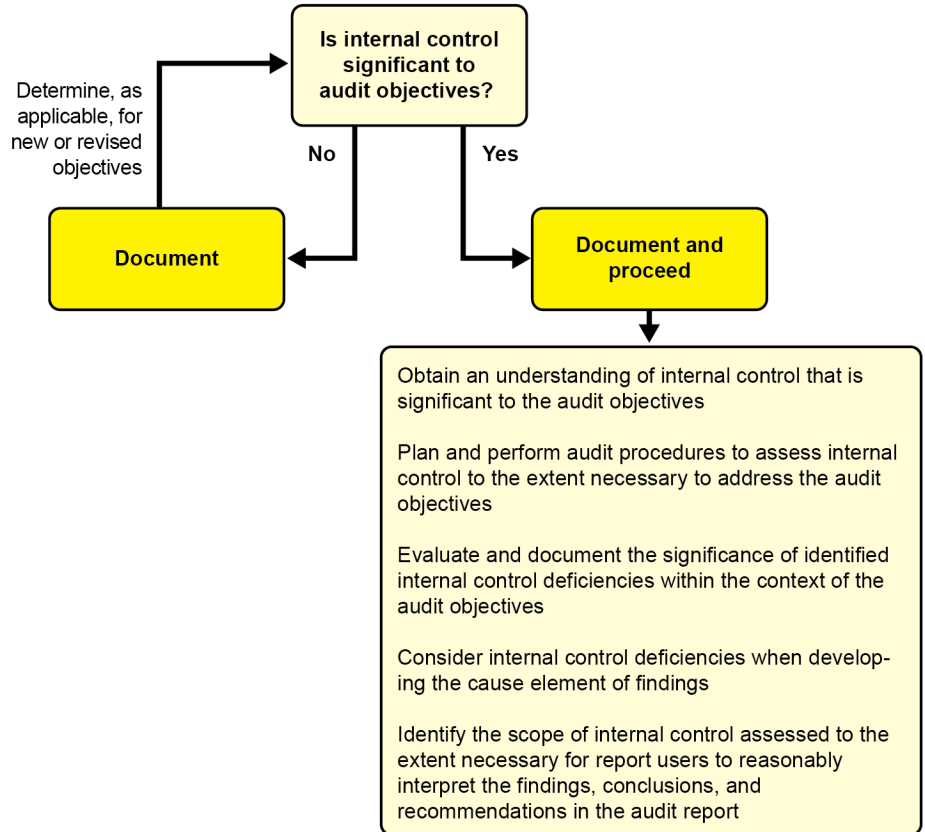
**8.140** Subject to applicable provisions of laws and regulations, auditors should make appropriate individuals and audit documentation available upon request and in a timely manner to other auditors or reviewers.

**Application Guidance: Availability of Individuals and Documentation**

**8.141** Underlying GAGAS audits is the premise that audit organizations in federal, state, and local governments and public accounting firms engaged to conduct audits in accordance with GAGAS cooperate in auditing programs of common interest so that auditors may use others' work and avoid duplication of efforts. 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 and to audit documentation.

Chapter 8: Fieldwork Standards for Performance Audits

Figure 4: Consideration of Internal Control in a Generally Accepted Government Auditing Standards Performance Audit



Source: GAO. | GAO-24-106786

# Chapter 9: Reporting Standards for Performance Audits

**9.01** This chapter contains reporting requirements and guidance for performance audits conducted in accordance with generally accepted government auditing standards (GAGAS). Reporting requirements establish the auditors' overall approach for communicating the results of a performance audit. For performance audits conducted in accordance with GAGAS, the requirements and guidance in chapters 1 through 5 and chapter 8 also apply.

**9.02** The reporting requirements for performance audits relate to reporting the auditors' compliance with GAGAS, the form of the report, the report contents, obtaining the views of responsible officials, report distribution, reporting confidential or sensitive information, and discovery of insufficient evidence after report release.

## Reporting Auditors' Compliance with GAGAS

### Requirements: Reporting Auditors' Compliance with GAGAS

**9.03** 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 conducted the audit in accordance with GAGAS:

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.

**9.04** Audit organizations that meet the independence requirements for internal audit organizations, but not those for external audit organizations, should include in the GAGAS compliance statement, where applicable, a statement that they are independent per the GAGAS requirements for internal auditors.

**9.05** 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 paragraph

9.03, modified to indicate the requirements that were not followed, or (2) language indicating that the auditors did not follow GAGAS.

## Report Format

### Requirements: Report Format

**9.06** Auditors should issue audit reports communicating the results of each completed performance audit.

**9.07** Auditors should issue the audit report in a form that is appropriate for its intended use, either in writing or in some other retrievable form.<sup>82</sup>

### Application Guidance: Report Format

**9.08** The purposes of audit reports are to (1) clearly communicate the results of audits to those charged with governance, the appropriate officials of the audited entity, and the appropriate oversight officials and (2) facilitate follow-up to determine whether appropriate corrective actions have been taken.

**9.09** Auditors may present audit reports using electronic media through which report users and the audit organization can retrieve them. 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.

## Report Content

### Requirements: Report Content, Including Objectives, Scope, and Methodology

**9.10** 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;

<sup>82</sup>See paras. 9.56 through 9.67 for a discussion of report distribution and reporting confidential or sensitive information.

(3) a summary of the views of responsible officials; and (4) if applicable, the nature of any confidential or sensitive information omitted.

**9.11** Auditors should communicate audit objectives in the audit report in a clear, specific, neutral, and unbiased manner that includes relevant assumptions. In order to avoid potential misunderstanding, when audit objectives are limited but users could infer broader objectives, auditors should state in the audit report that certain issues were outside the scope of the audit.

**9.12** Auditors should describe the scope of the work performed and any limitations, including issues that would be relevant to likely users, so that report users can 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, or excessive delays in, access to certain records or individuals.

**9.13** In describing the work performed 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 entities, 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.

**9.14** In reporting audit methodology, auditors should explain how the completed audit work supports the audit objectives, including the evidence-gathering and evidence-analysis techniques, in sufficient detail to allow knowledgeable users of their reports to understand how the auditors addressed the audit objectives. Auditors should identify significant assumptions made in conducting the audit; describe comparative techniques applied; describe the criteria used; and, when the results of sample testing significantly support 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.

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**Application Guidance: Report Content, Including Objectives, Scope, and Methodology**

**9.15** Report users need information regarding the audit objectives, scope, and methodology 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 the audit objectives, scope, or methodology.

**9.16** In reporting audit methodology, 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.

**9.17** The auditor may use the report quality elements of accurate, objective, complete, convincing, clear, concise, and timely when developing and writing the audit 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 the audit organization prepare accurate audit reports is to use a 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; the findings are adequately supported by the evidence in the audit documentation; and 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

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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 personnel.

- 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 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 understandability. 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 help clarify and summarize complex material.

- f. **Concise:** Being concise means that the report is no longer than necessary to convey and support the message. Extraneous detail detracts from a report and may even conceal the real message and 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 and oversight officials. Such communication alerts officials to matters needing immediate attention and allows them to take corrective action before the final report is completed.

## Reporting Findings, Conclusions, and Recommendations

### **Requirements: Reporting Findings, Conclusions, and Recommendations**

**9.18** In the audit report, auditors should present sufficient, appropriate evidence to support the findings and conclusions in relation to the audit objectives. Auditors should provide recommendations for corrective action if findings are significant within the context of the audit objectives.

**9.19** Auditors should report conclusions based on the audit objectives and the audit findings.

**9.20** 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. 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.

**9.21** 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 findings. To give the reader a basis for judging the prevalence and consequences of these findings, auditors should, as appropriate, 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. If the results cannot be projected, auditors should limit their conclusions appropriately.

**9.22** When reporting on the results of their work, auditors should disclose significant facts relevant to the objectives of their work and known to them that if not disclosed could mislead knowledgeable users, misrepresent the results, or conceal significant improper or illegal practices.

**9.23** When feasible, auditors should recommend actions to correct deficiencies and other findings 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 deficiencies and findings, and clearly state the actions recommended.

### **Application Guidance: Reporting Findings, Conclusions, and Recommendations**

**9.24** The extent to which the elements for a finding are developed depends on the audit objectives. Clearly developed findings assist management and oversight officials of the audited entity in understanding the need for taking corrective action.

**9.25** As discussed in paragraphs 8.108 through 8.115, 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. Describing limitations provides report users with a clear understanding of how much responsibility the auditors are taking for the information.

**9.26** Auditors may provide background information to establish the context for the overall message and to help the reader understand the findings and significance of the issues discussed. Appropriate background information may include information on how programs and operations work; the significance of programs and operations (e.g., dollars, effect, 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.

**9.27** 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 persuasiveness of the evidence supporting the findings and the soundness of the logic used to formulate the conclusions. Conclusions are more compelling if they lead to recommendations and convince a knowledgeable user of the report that action is necessary.

**9.28** Effective recommendations encourage improvements in the conduct of government programs and operations. Recommendations are effective when they are addressed to parties with the authority to act and when the recommended actions are specific, feasible, cost-effective, and measurable.

## Reporting on Internal Control

### Requirements: Reporting on Internal Control

**9.29** When internal control is significant within the context of the audit objectives, 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.

**9.30** When reporting on the scope of their work on internal control, auditors should identify the scope of internal control assessed to the extent necessary for report users to reasonably interpret the findings, conclusions, and recommendations in the audit report.

**9.31** When auditors detect deficiencies in internal control that are not significant to the objectives of the audit but warrant the attention of those charged with governance, they should include those deficiencies either in the report or communicate those deficiencies in writing to audited entity officials. If the written communication is separate from the audit report, auditors should refer to that written communication in the audit report.

#### **Application Guidance: Reporting on Internal Control**

**9.32** Auditors may identify the control components, underlying principles, control objectives, or specific controls assessed in describing the scope of their work on internal control. Auditors may also identify the level of internal control assessment performed, as discussed in paragraph 8.50. Control components and underlying principles that are not considered significant to the audit objectives may be identified in the scope if, in the auditors' professional judgment, doing so is necessary to preclude a misunderstanding of the breadth of the conclusions of the audit report and to clarify that control effectiveness has not been evaluated as a whole. Auditors may also identify and describe the five components of internal control so that report users understand the scope of the work within the context of the entity's internal control system.

**9.33** An internal control system is effective if the five components of internal control are effectively designed, implemented, and operating, and are operating together in an integrated manner. The principles support the effective design, implementation, and operation of the associated components and represent requirements necessary to establish an effective internal control system. If a principle is not applied effectively, then the respective component cannot be effective. If a principle or component is not effective, or the components are not operating together in an integrated manner, then an internal control system cannot be effective.

**9.34** When auditors detect deficiencies in internal control that do not warrant the attention of those charged with governance, determining

whether and how to communicate such deficiencies to audited entity officials is a matter of professional judgment.

### Reporting on Noncompliance with Provisions of Laws, Regulations, Contracts, and Grant Agreements

#### **Requirements: Reporting on Noncompliance with Provisions of Laws, Regulations, Contracts, and Grant Agreements**

**9.35** Auditors should report a matter as a finding when they conclude, based on sufficient, appropriate evidence, that noncompliance with provisions of laws, regulations, contracts, and grant agreements either has occurred or is likely to have occurred that is significant within the context of the audit objectives.

**9.36** Auditors should communicate findings in writing to audited entity officials when the auditors detect instances of noncompliance with provisions of laws, regulations, contracts, and grant agreements that are not significant within the context of the audit objectives but warrant the attention of those charged with governance.

#### **Application Guidance: Reporting on Noncompliance with Provisions of Laws, Regulations, Contracts, and Grant Agreements**

**9.37** Whether a particular act is, in fact, noncompliance with provisions of laws, regulations, contracts, and grant agreements may have to await final determination by a court of law or other adjudicative body.<sup>83</sup>

**9.38** When auditors detect instances of noncompliance with provisions of laws, regulations, contracts, and grant agreements that do not warrant the attention of those charged with governance, the auditors' determination of whether and how to communicate such instances to audited entity officials is a matter of professional judgment.

**9.39** When noncompliance with provisions of laws, regulations, contracts, and grant agreements either has occurred or is 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

<sup>83</sup>See paras. 8.27 through 8.29 for a discussion of investigations or legal proceedings.

would not compromise those proceedings and, for example, report only on information that is already a part of the public record.

## Reporting on Instances of Fraud

### Requirements: Reporting on Instances of Fraud

**9.40** Auditors should report a matter as a finding when they conclude, based on sufficient, appropriate evidence, that fraud either has occurred or is likely to have occurred that is significant to the audit objectives.

**9.41** Auditors should communicate findings in writing to audited entity officials when the auditors detect instances of fraud that are not significant within the context of the audit objectives but warrant the attention of those charged with governance.

### Application Guidance: Reporting on Instances of Fraud

**9.42** Whether a particular act is, in fact, fraud may have to await final determination by a court of law or other adjudicative body.<sup>84</sup>

**9.43** When auditors detect instances of fraud that do not warrant the attention of those charged with governance, the auditors' determination of whether and how to communicate such instances to audited entity officials is a matter of professional judgment.

**9.44** When auditors conclude fraud has occurred or is 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.

<sup>84</sup>See paras. 8.27 through 8.29 for a discussion of investigations or legal proceedings.

## Reporting Findings Directly to Parties outside the Audited Entity

### Requirements: Reporting Findings Directly to Parties outside the Audited Entity

**9.45** Auditors should report known or likely noncompliance with provisions of laws, regulations, contracts, and grant agreements or fraud directly to parties outside the audited entity in the following two circumstances.

- a. When audited 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 audited entity management fails to take timely and appropriate steps to respond to noncompliance with provisions of laws, regulations, contracts, and grant agreements or instances of fraud that (1) are likely to have a significant effect on the subject matter and (2) involve 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 audited entity's failure to take timely and appropriate steps directly to the funding agency.

**9.46** Auditors should comply with the requirements in paragraph 9.45 even if they have resigned or been dismissed from the audit prior to its completion.

**9.47** Auditors should obtain sufficient, appropriate evidence, such as confirmation from outside parties, to corroborate representations by audited entity management that it has reported audit findings in accordance with provisions of laws, regulations, or funding agreements.

When auditors are unable to do so, they should report such information directly, as discussed in paragraphs 9.45 and 9.46.

### **Application Guidance: Reporting Findings Directly to Parties outside the Audited Entity**

**9.48** The reporting in paragraph 9.45 is in addition to any legal requirements to report such information directly to parties outside the audited entity.

**9.49** Internal audit organizations do not have a duty to report outside the audited entity unless required by law, regulation, or policy.

## **Obtaining the Views of Responsible Officials**

### **Requirements: Obtaining the Views of Responsible Officials**

**9.50** Auditors should obtain and report the views of responsible officials of the audited entity concerning the findings, conclusions, and recommendations in the audit report, as well as any planned corrective actions.

**9.51** 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, provide a copy of the summary to the responsible officials to verify that the comments are accurately represented, and include the summary in their report.

**9.52** When the audited entity's comments are inconsistent or in conflict with the findings, conclusions, or recommendations in the draft report, 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 by sufficient, appropriate evidence.

**9.53** 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.

### Application Guidance: Obtaining the Views of Responsible Officials

**9.54** 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 audited entity's responsible officials and the corrective actions they plan to take. Obtaining the comments in writing is preferred, but oral comments are acceptable. 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. Technical comments address points of fact or are editorial in nature and do not address substantive issues, such as methodology, findings, conclusions, or recommendations.

**9.55** 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 engagement, and the parties are familiar with the findings and issues addressed in the draft report; or the auditors do not expect major disagreements with findings, conclusions, or recommendations in the draft report, or major controversies with regard to the issues discussed in the draft report.

## Report Distribution

### Requirements: Report Distribution

**9.56** Distribution of reports completed in accordance with GAGAS depends on the auditors' relationship with the audited organization and the nature of the information contained in the reports. Auditors should document any limitation on report distribution. Auditors should make audit reports available to the public, unless distribution is specifically limited by the terms of the engagement, law, or regulation.

*Report Distribution for Internal Auditors*

**9.57** If an internal audit organization in a government entity follows the Institute of Internal Auditors' *International Standards for the Professional Practice of Internal Auditing* as well as GAGAS, 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 or legal counsel as appropriate, and (3) control dissemination by indicating the intended users in the report.

*Report Distribution for External Auditors*

**9.58** An audit organization in a government entity should distribute audit reports to those charged with governance, to the appropriate audited entity officials, 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.

**9.59** A public accounting firm contracted to conduct an audit in accordance with GAGAS should clarify report distribution responsibilities with the engaging party. If the contracting firm is responsible for 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.

**Application Guidance: Report Distribution for External Auditors**

**9.60** Making an audit report available to the public can involve auditors posting the audit report to their publicly accessible websites or verifying that the audited entity has posted the audit report to its publicly accessible website.

## Reporting Confidential or Sensitive Information

### Requirements: Reporting Confidential or Sensitive Information

**9.61** If certain information is prohibited from public disclosure or is excluded from a report because of its confidential or sensitive nature, auditors should disclose in the report that certain information has been omitted and the circumstances that make the omission necessary.

**9.62** 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 and revise the report language as necessary to avoid report users drawing inappropriate conclusions from the information presented.

**9.63** When the audit organization is subject to public records laws, auditors should determine whether public records laws could affect 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. Auditors use judgment to determine the appropriate means to communicate the omitted information to management and those charged with governance considering, among other things, whether public records laws could affect the availability of classified or limited use reports.

### Application Guidance: Reporting Confidential or Sensitive Information

**9.64** If the report refers to the omitted information, the reference may be general and not specific. If the omitted information is not necessary to meet the audit objectives, the report need not refer to its omission.

**9.65** 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 such information and distribute the report only to persons authorized by law or regulation to receive it.

**9.66** Additional circumstances associated with public safety, privacy, or security concerns could 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 misuse of this information could cause. 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. In some instances, it may be appropriate to issue both a publicly available report with the sensitive information excluded and a limited use report. The auditors may consult with legal counsel regarding any requirements or other circumstances that may necessitate omitting certain information. Considering the broad public interest in the program or activity under audit assists auditors when deciding whether to exclude certain information from publicly available reports.

**9.67** In cases described in paragraph 9.63, auditors may communicate general information in a written report and communicate detailed information orally. Auditors may consult with legal counsel regarding applicable public records laws.

## Discovery of Insufficient Evidence after Report Release

### **Requirement: Discovery of Insufficient Evidence after Report Release**

**9.68** 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 in the same manner as that used to originally distribute the report to those charged with governance, the appropriate officials of the audited entity, the appropriate officials of the entities requiring or arranging for the audits, and other known users, 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 perform the additional audit work necessary to either reissue the report, including any revised findings or conclusions, or repost the original report if the additional audit work does not result in a change in findings or conclusions.

# Glossary

The following terms are provided to assist in clarifying the *Government Auditing Standards*. The most relevant paragraph numbers are provided for reference. When terminology differs from that used at an organization subject to generally accepted government auditing standards (GAGAS), auditors use professional judgment to determine if there is an equivalent term.

**Abuse:** 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, but excludes fraud and noncompliance with provisions of laws, regulations, contracts, and grant agreements. (paragraphs 6.23, 7.25, and 8.122)

**Agreed-upon procedures engagement:** Consists of auditors performing specific procedures on subject matter or an assertion and reporting findings without providing an opinion or a conclusion on it. (paragraph 1.18c)

**Appropriateness:** 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. (paragraph 8.102)

**Attestation engagement:** An examination, review, or agreed-upon procedures engagement conducted under the GAGAS attestation standards related to subject matter or an assertion that is the responsibility of another party. (paragraph 1.27a)

**Audit:** Either a financial audit or performance audit conducted in accordance with GAGAS. (paragraph 1.27b)

**Audit objectives:** What the audit is intended to accomplish. They identify the audit subject matter and performance aspects to be included. Audit objectives can be thought of as questions about the program that the auditors seek to answer based on evidence obtained and assessed against criteria. Audit objectives may also pertain to the current status or condition of a program. (paragraph 8.08)

**Audit organization:** A government audit entity or a public accounting firm or other audit entity that conducts GAGAS engagements. (paragraph 1.27c)

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**Glossary**

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**Audit procedures:** The specific steps and tests auditors perform to address the audit objectives. (paragraph 8.11)

**Audit report:** A report issued as a result of a financial audit, attestation engagement, review of financial statements, or performance audit conducted in accordance with GAGAS. (paragraph 1.27d)

**Audit risk:** The possibility that the auditors' findings, conclusions, recommendations, or assurance may be improper or incomplete. The assessment of audit risk involves both qualitative and quantitative considerations. (paragraph 8.16)

**Audited entity:** The entity that is subject to a GAGAS engagement, whether that engagement is a financial audit, attestation engagement, review of financial statements, or performance audit. (paragraph 1.27e)

**Auditor:** An individual assigned to planning, directing, performing engagement procedures or reporting on GAGAS engagements (including work on audits, attestation engagements, and reviews of financial statements) regardless of job title. Therefore, individuals who may have the title auditor, information technology auditor, analyst, practitioner, evaluator, inspector, or other similar titles are considered auditors under GAGAS. (paragraph 1.27f)

**Bias threat:** The threat that an auditor will, as a result of political, ideological, social, or other convictions, take a position that is not objective. (paragraph 3.30c)

**Cause:** The factor or factors responsible for the difference between the condition and the criteria, which may also serve as a basis for recommendations for corrective actions. (paragraphs 6.27, 7.29, and 8.126)

**Competence:** The knowledge, skills, and abilities, obtained from education and experience, necessary to conduct the GAGAS engagement. Competence enables auditors to make sound professional judgments. Competence includes possessing the technical knowledge and skills necessary for the assigned role and the type of work being done. This includes possessing specific knowledge about GAGAS. (paragraph 4.05)

**Condition:** A situation that exists. The condition is determined and documented during the engagement. (paragraphs 6.26, 7.28, and 8.125)

## Glossary

**Control objective:** The aim or purpose of specified controls; control objectives address the risks related to achieving an entity's objectives. (paragraph 1.27g)

**CPE programs:** Structured educational activities or programs with learning objectives designed to maintain or enhance the auditors' competence to address engagement objectives and perform work in accordance with GAGAS. (paragraph 4.32)

**Criteria:** 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 in the report. (paragraphs 6.25, 7.27, and 8.124)

**Directing:** Supervising the efforts of others who are involved in accomplishing the objectives of the engagement or reviewing engagement work to determine whether those objectives have been accomplished. (paragraph 4.11b)

**Education:** A structured and systematic process aimed at developing knowledge, skills, and other abilities; it is a process that is typically but not exclusively conducted in academic or learning environments. (paragraph 4.06)

**Effect or potential effect:** The outcome or consequence resulting from the difference between the condition and the criteria. (paragraphs 6.28, 7.30, and 8.127)

**Engagement:** A financial audit, attestation engagement, review of financial statements, or performance audit conducted in accordance with GAGAS. (paragraph 1.27h)

**Engagement partner or director:** The partner or director assigned overall responsibility by the audit organization for managing and achieving quality for the engagement and for being sufficiently and appropriately involved throughout the engagement. (paragraph 5.54a)

**Engagement quality review:** An objective evaluation of the engagement team's significant judgments and the conclusions reached thereon that

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**Glossary**

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the engagement quality reviewer performs and completes before the audit report is released. (paragraph 5.70)

**Engagement team (or audit team):** Auditors assigned to planning, directing, performing engagement procedures or reporting on GAGAS engagements. (paragraph 1.27i)

**Engaging party:** The party that engages the auditor to conduct a GAGAS engagement. (paragraph 1.27j)

**Entity objective:** What an entity wants to achieve; entity objectives are intended to meet the entity's mission, strategic plan, and goals and the requirements of applicable laws and regulations. (paragraph 1.27k)

**Examination:** Consists of obtaining reasonable assurance by obtaining sufficient, appropriate evidence about the measurement or evaluation of subject matter against criteria in order to be able to draw reasonable conclusions on which to base the auditor's opinion about whether the subject matter is in accordance with (or based on) the criteria or the assertion is fairly stated, in all material respects. (paragraph 1.18a)

**Experience:** Workplace activities that are relevant to developing professional proficiency. (paragraph 4.06)

**External audit organization:** An audit organization that issues reports to third parties external to the audited entity, either exclusively or in addition to issuing reports to senior management and those charged with governance of the audited entity. (paragraph 1.27l)

**Familiarity threat:** The threat that aspects of a relationship with management or personnel of an audited entity, such as a close or long relationship, or that of an immediate or close family member, will lead an auditor to take a position that is not objective. (paragraph 3.30d)

**Financial audits:** Provide an independent assessment of whether an entity's reported financial information (e.g., financial condition, results, and use of resources) is presented fairly, in all material respects, in accordance with recognized criteria. (paragraph 1.17)

**Finding:** An issue that may involve a deficiency in internal control; noncompliance with provisions of laws, regulations, contracts, or grant agreements; or instances of fraud. Elements of a finding generally include



## Glossary

criteria, condition, cause, and effect or potential effect. (paragraphs 6.17, 6.19, 7.19, 7.21, 8.116, and 8.118)

**Finding (in relation to a system of quality management):** Information about the design, implementation, and operation of the system of quality management that the audit organization has accumulated through the performance of monitoring activities and from other relevant sources, which indicates that one or more deficiencies may exist. (paragraph 5.111)

**Fraud:** Involves obtaining something of value through willful misrepresentation. Whether an act is, in fact, fraud is determined through the judicial or other adjudicative system and is beyond auditors' professional responsibility. (paragraph 8.73)

**Independence in appearance:** The absence of circumstances that would cause a reasonable and informed third party to reasonably conclude that the integrity, objectivity, or professional skepticism of an audit organization or member of the engagement team had been compromised. (paragraph 3.21b)

**Independence of mind:** The state of mind that permits the conduct of an engagement without being affected by influences that compromise professional judgment, thereby allowing an individual to act with integrity and exercise objectivity and professional skepticism. (paragraph 3.21a)

**Inputs:** The amount of resources (in terms of, for example, money, material, or personnel) that is put into a program. These resources may come from within or outside the entity operating the program. Measures of inputs can have a number of dimensions, such as cost, timing, and quality. (paragraph 8.38d)

**Inspection (in relation to a system of quality management):** A retrospective evaluation of the adequacy of the audit organization's quality management policies and procedures, its personnel's understanding of those policies and procedures, and the extent of its compliance with them. (paragraph 5.101)

**Integrity:** Auditors performing their work with an attitude that is objective, fact-based, nonpartisan, and nonideological with regard to audited entities and users of the audit reports and making decisions consistent with the public interest of the program or activity under audit. (paragraphs 3.09 and 3.10)

## Glossary

**Internal audit organization:** An audit organization that is accountable to senior management and those charged with governance of the audited entity and that does not generally issue reports to third parties external to the audited entity. (paragraph 1.27m)

**Internal control:** A process effected by an entity's oversight body, management, and other personnel that provides reasonable assurance that the objectives of an entity will be achieved. (paragraph 1.22b)

**Likelihood of occurrence:** The possibility of a deficiency impacting an entity's ability to achieve its objectives. (paragraph 8.56b)

**Magnitude of impact:** The likely effect that a deficiency could have on the entity achieving its objectives. (paragraph 8.56a)

**Management participation threat:** The threat that results from an auditor's taking on the role of management or otherwise performing management functions on behalf of the audited entity, which will lead an auditor to take a position that is not objective. (paragraph 3.30f)

**Methodology:** The nature and extent of audit procedures for gathering and analyzing evidence to address the audit objectives. (paragraph 8.11)

**Monitoring of quality:** A process comprising ongoing consideration and evaluation of the audit organization's system of quality management. (paragraph 5.88)

**Nature of the deficiency:** Involves factors such as the degree of subjectivity involved with the deficiency and whether the deficiency arises from fraud or misconduct. (paragraph 8.56c)

**Nonsupervisory auditor:** An auditor who plans or performs engagement procedures and whose work situation is characterized by low levels of ambiguity, complexity, and uncertainty. (paragraph 4.10a)

**Objectivity:** The basis for the credibility of auditing in the government sector. Objectivity includes independence of mind and appearance when conducting engagements, maintaining an attitude of impartiality, having intellectual honesty, and being free of conflicts of interest. (paragraph 3.11)

**Outcomes:** Accomplishments or results of a program. (paragraph 8.38g)

## Glossary

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**Outputs:** The quantity of goods or services produced by a program. (paragraph 8.38f)

**Partners and directors:** Auditors who plan engagements, perform engagement procedures, or direct or report on engagements and whose work situations are characterized by high levels of ambiguity, complexity, and uncertainty. Partners and directors may also be responsible for reviewing engagement quality prior to issuing the report, for signing the report, or both. (paragraph 4.10c)

**Peer review risk:** The risk that the review team (1) fails to identify significant weaknesses in the reviewed audit organization's system of quality management for its auditing practice, its lack of compliance with that system, or a combination thereof; (2) issues an inappropriate opinion on the reviewed audit organization's system of quality management for its auditing practice, its compliance with that system, or a combination thereof; or (3) makes an inappropriate decision about the matters to be included in, or excluded from, the peer review report. (paragraph 5.163)

**Performance audits:** Engagements that provide objective analysis, findings, and conclusions to assist management and those charged with governance and oversight to, among other things, improve program performance and operations, reduce costs, facilitate decision making by parties with responsibility to oversee or initiate corrective action, and contribute to public accountability. In a performance audit, the auditors measure or evaluate the subject matter of the audit and present the resulting information as part of, or accompanying, the audit report. (paragraphs 1.21 and 8.14)

**Period of professional engagement:** The period beginning when the auditors either sign an initial engagement letter or other agreement to conduct an engagement or begin to conduct an engagement, whichever is earlier. The period lasts for the duration of the professional relationship—which, for recurring engagements, could cover many periods—and ends with the formal or informal notification, either by the auditors or the audited entity, of the termination of the professional relationship or with the issuance of a report, whichever is later. (paragraph 3.23)

**Performing engagement procedures:** Performing tests and procedures necessary to accomplish the engagement objectives in accordance with GAGAS. (paragraph 4.11c)

## Glossary

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**Planning:** Determining engagement objectives, scope, and methodology; establishing criteria to evaluate matters subject to audit; or coordinating the work of the other audit organization. This definition excludes auditors whose role is limited to gathering information used in planning the engagement. (paragraph 4.11a)

**Presumptively mandatory requirements:** Auditors and the audit organization must comply in all cases where such a requirement is relevant except in rare circumstances discussed in paragraphs 2.03, 2.04, and 2.08. GAGAS uses *should* to indicate a presumptively mandatory requirement. (paragraph 2.02b)

**Professional behavior:** Behavior that includes auditors avoiding any conduct that could bring discredit to their work and putting forth an honest effort in performing their duties in accordance with the relevant technical and professional standards. (paragraph 3.16)

**Professional judgment:** Use of the auditor's professional knowledge, skills, and abilities, in good faith and with integrity, to diligently gather information and objectively evaluate the sufficiency and appropriateness of evidence. Professional judgment includes exercising reasonable care and professional skepticism. (paragraphs 3.109 through 3.117)

**Program:** Includes processes, projects, studies, policies, operations, activities, entities, and functions. (paragraph 8.08)

**Program operations:** The strategies, processes, and activities management uses to convert inputs into outputs. Program operations may be subject to internal control. (paragraph 8.38e)

**Public interest:** The collective well-being of the community of people and entities that the auditors serve. (paragraph 3.07)

**Quality objective:** The desired outcomes to be achieved by the audit organization in relation to the components of the system of quality management. (paragraph 5.29)

**Quality risk:** Risks that have a reasonable possibility of occurring and adversely affecting the achievement of one or more quality objectives individually or in combination with other risks. (paragraph 5.34)

**Reasonable and informed third party:** As evaluated by a hypothetical person, a person who possesses skills, knowledge, and experience to

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**Glossary**

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objectively evaluate the appropriateness of the auditor's judgments and conclusions. This evaluation entails weighing all the relevant facts and circumstances, including any safeguards applied, that the auditor knows, or could reasonably be expected to know, at the time that the evaluation is made. (paragraph 3.46)

**Reporting:** Determining the report content and substance or reviewing reports to determine whether the engagement objectives have been accomplished and the evidence supports the report's technical content and substance prior to issuance. This includes signing the report. (paragraph 4.11d)

**Response to address a quality risk:** The policies and procedures that the audit organization designs and implements to address one or more quality risks. (paragraph 5.40)

**Responsible party:** The party responsible for a GAGAS engagement's subject matter. (paragraph 1.27n)

**Review:** Consists of obtaining limited assurance by obtaining sufficient, appropriate review evidence about the measurement or evaluation of subject matter against criteria in order to express a conclusion about whether any material modifications should be made to the subject matter in order for it to be in accordance with (or based on) the criteria or to the assertion in order for it to be fairly stated. Review-level work does not include reporting on internal control or compliance with provisions of laws, regulations, contracts, and grant agreements. (paragraph 1.18b)

**Review of financial statements:** An engagement conducted under GAGAS for review of financial statements. (paragraph 1.27o)

**Safeguards:** Actions or other measures, individually or in combination, that auditors and the audit organization take that effectively eliminate threats to independence or reduce them to an acceptable level. (paragraph 3.49)

**Scope:** 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. (paragraph 8.10)

## Glossary

**Self-interest threat:** The threat that a financial or other interest will inappropriately influence an auditor's judgment or behavior. (paragraph 3.30a)

**Self-review threat:** The threat that an auditor or audit organization that has provided nonaudit services will not appropriately evaluate the results of previous judgments made or services provided as part of the nonaudit services when forming a judgment significant to a GAGAS engagement. (paragraph 3.30b)

**Service provider:** An individual or organization external to the audit organization that provides a human, technological, or intellectual resource that the audit organization uses in its system of quality management or in performing its engagements. (paragraph 5.79)

**Significance:** The relative importance of a matter within the context in which it is being considered, including quantitative and qualitative factors. In the performance audit requirements, the term significant is comparable to the term material as used in the context of financial statement engagements. (paragraph 8.15)

**Source documents:** Documents providing evidence that transactions have occurred (for example, purchase orders, payroll time records, customer orders, and contracts). Such records also include an audited entity's general ledger and subsidiary records or equivalent. (paragraph 3.92)

**Specialist:** An individual or organization possessing special skill or knowledge in a particular field other than accounting or auditing that assists auditors in conducting engagements. A specialist may be either an internal specialist or an external specialist. (paragraph 1.27p)

**Structural threat:** The threat that an audit organization's placement within a government entity, in combination with the structure of the government entity being audited, will affect the audit organization's ability to perform work and report results objectively. (paragraph 3.30g)

**Sufficiency:** A measure of the quantity of evidence used to support the findings and conclusions related to the audit objectives. (paragraph 8.99)

**Supervisory auditor:** An auditor who plans engagements, performs engagement procedures, or directs engagements, and whose work

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**Glossary**

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situation is characterized by moderate levels of ambiguity, complexity, and uncertainty. (paragraph 4.10b)

**System of Quality Management:** A system designed, implemented, and operated by an audit organization that provides it with reasonable assurance that the audit organization and its personnel fulfill their responsibilities in accordance with professional standards and applicable laws and regulations and perform and report on engagements in accordance with such standards and requirements. (paragraph 5.05)

**Technical comments:** Comments that address points of fact or are editorial in nature and do not address substantive issues, such as methodology, findings, conclusions, or recommendations. (paragraphs 6.62, 7.59, and 9.54)

**Those charged with governance:** The individuals responsible for overseeing 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. Those charged with governance may also be part of the entity's management. In some audited 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 engagement. (paragraph 1.04)

**Unconditional requirement:** Requirement with which auditors and the audit organization must comply in all cases where such requirement is relevant. GAGAS uses *must* to indicate an unconditional requirement. (paragraph 2.02a)

**Undue influence threat:** The threat that influences or pressures from sources external to the audit organization will affect an auditor's ability to make objective judgments. (paragraph 3.30e)

**Waste:** The act of using or expending resources carelessly, extravagantly, or to no purpose. Waste can include activities that do not include abuse and does not necessarily involve a violation of law. (paragraphs 6.21, 7.23, and 8.120)

# Acknowledgments

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## Comptroller General's Advisory Council on Government Auditing Standards (2022- 2026)

Erica Forhan, Chair  
Moss Adams LLP

David Berry  
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Irving L. Dennis  
American Cornerstone Institute

Renee Flasher  
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Lorin Venable  
U.S. Department of Defense, Office of Inspector General

Theresa Watson  
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## Deschutes County Office of Internal Audit

### 2024 Proposed Goals and Objectives

DRAFT for Audit Committee Review

**Mission: To support continuous government improvement through accountability, transparency, and trust.**

#### Goal 1: Increase public trust in Deschutes County government.

Obj 1 Provide an independent assessment of County government.

Obj 2 Address topics that are most relevant to community members.

Obj 3 Create communications that are timely and accessible.

Obj 4 Report on County operations and adherence to legal and regulatory requirements.

Obj 5 Investigate and report on alleged fraud, waste, inefficiency, or abuse.

Obj 6 Support the Audit Committee in fulfilling its role of providing oversight of County finances and operations.



#### Goal 2: Be a trusted advisor to County elected officials and management.

Obj 7 Assess potential risk to operations and outcomes and inform County elected officials and management.

Obj 8 Establish an annual audit work plan based upon the risk assessment and available resources.

Obj 9 Maintain open communication with management before, during and through completion of audits.

Obj 10 Maintain professional standards to ensure conformance Governmental Auditing Standards

Obj 11 Evaluate management requests for consultation when they are in alignment with skills and availability and do not compromise audit independence.



### Goal 3: Create positive change in County Government



- Obj 12 Plan and scope audit work to maximize impact.
- Obj 13 Develop actionable recommendations to improve efficiency, transparency and accountability, service delivery, economy, equity, ethical conduct, compliance, and governance.
- Obj 14 Ensure that recommendations are supported by sufficient and appropriate evidence.
- Obj 15 Track and report on management recommendation resolution.

### Goal 4: Strengthen team knowledge, skills, and fulfillment.



- Obj 16 Foster workplace culture of trust, dignity, and respect where staff feel valued and confident in their performance.
- Obj 17 Identify sufficient resources and technology to assure that audits can be completed.
- Obj 18 Develop a training program consistent with meeting continuing professional education and certification requirements.

## 2011 Goals and Objectives

**Mission: To improve performance and enhance the internal control environment of Deschutes County Government and to provide accountability to its citizens.**

**Goal 1: Examine and evaluate the effectiveness and efficiency of operations, the reliability of financial reporting, enhance the internal control environment, and compliance with applicable laws and regulations.**

Objective 1: Establish an audit work plan based upon a risk assessment and available resources.

Objective 2: Identify sufficient resources to assure that audits can be completed. Internal audits might require additional resources.

Objective 3: Maintain professional standards in order to report in conformance Governmental Auditing Standards

Objective 4: Assure that internal audit maintains an excellent working relationship with management and the audit committee. Establish appropriate communication before, during and through completion of audits.

Objective 5: Investigate reports of fraud, waste or abuse as under ordinance or as may be requested by the County Administrator.

Objective 6: Coordinate audit activities with the external auditors.

**Goal 2: Provide information to County management, employees and interested public on how to improve internal functions and processes.**

Objective 1: Provide written internal audit reports at the completion of audit work within 30 days.

Objective 2: Assist the audit committee in fulfilling responsibility of financial oversight.

Objective 3: Provide follow-up reports within year of report issuance to assess implementation of recommendations.

**Goal 3: Improve access to management, employees and the public of internal audit work being performed.**

Objective 1: Provide employees direct access to internal audit reports.

Objective 2: Provide information to the public on internal audit work being performed.

## 2011 Mission and Goals

*2011 goals ordered around process: audit, report, access*

Mission: To improve performance and enhance the internal control environment of Deschutes County Government and to provide accountability to its citizens.

Goal 1: Examine and evaluate the effectiveness and efficiency of operations, the reliability of financial reporting, enhance the internal control environment, and compliance with applicable laws and regulations.

Goal 2: Provide information to County management, employees and interested public on how to improve internal functions and processes.

Goal 3: Improve access to management, employees and the public of internal audit work being performed.

## 2024 Mission and Goals

*2024 goals oriented around audience: community, electeds,  
management, audit team*

Mission: To support continuous government improvement through accountability, transparency, and trust.

Goal 1: Increase public trust in Deschutes County government.

Goal 2: Be a trusted advisor to County elected officials and management.

Goal 3: Create positive change in County Government

Goal 4: Strengthen team knowledge, skills, and fulfillment.

2011 Orde 2011 Description	2024 Description
<p>G1 Objective 1.1: Establish an audit work plan based upon a risk assessment and 1 available resources.</p> <p>G3 Objective 3.2: Provide information to the public on the nature of internal audit 11 work being performed.</p> <p>G2 Objective 2.1: Provide written internal audit reports at the completion of audit 7 work within 30 days.</p> <p>G1 Objective 1.5: Investigate reports of fraud, waste or abuse as under ordinance or as may be requested by 5 the County Administrator.</p> <p>G2 Objective 2.2: Assist the audit committee in fulfilling responsibility of 8 financial oversight</p> <p>G1 Objective 1.1: Establish an audit work plan based upon a risk assessment and 1 available resources.</p> <p>G1 Objective 1.1: Establish an audit work plan based upon a risk assessment and 1 available resources.</p> <p>G1 Objective 1.4: Assure that internal audit maintains an excellent working relationship with management and the audit committee. Establish appropriate communication before, during and 4 through completion of audits.</p> <p>G1 Objective 1.3: Maintain professional standards in order to report in conformance Governmental Auditing 3 Standards</p>	<p>G1 Obj 1 Provide an independent assessment of County government.</p> <p>G1 Obj 2 Address topics that are most relevant to community members.</p> <p>G1 Obj 3 Create communications that are timely and accessible.</p> <p>G1 Obj 4 Report on County operations and adherence to legal and regulatory requirements.</p> <p>G1 Obj 5 Investigate and report on alleged fraud, waste, inefficiency, or abuse.</p> <p>G1 Obj 6 Support the Audit Committee in fulfilling its role of providing oversight of County finances and operations.</p> <p>G2 Obj 7 Assess potential risk to operations and outcomes and keep County elected officials and management informed about</p> <p>G2 Obj 8 Establish an annual audit work plan based upon the risk assessment and available resources.</p> <p>G2 Obj 9 Maintain open communication with management before, during and through completion of audits.</p> <p>G2 Obj 10 Maintain professional standards to ensure conformance Governmental Auditing Standards</p>



<p>G1 Objective 1.4: Assure that internal audit maintains an excellent working relationship with management and the audit committee. Establish appropriate communication before, during and 4 through completion of audits.</p>	<p>G2 Obj 11 Evaluate management requests for consultation when they are in alignment with skills and availability and do not compromise audit independence.</p>
<p>G1 Objective 1.1: Establish an audit work plan based upon a risk assessment and 1 available resources.</p>	<p>G3 Obj 12 Plan and scope audit work to maximize impact.</p>
<p>G2 Objective 2.1: Provide written internal audit reports at the completion of audit work within 30 days. 7</p>	<p>G3 Obj 13 Develop actionable recommendations to improve efficiency, transparency and accountability, service delivery, economy, equity, ethical conduct, compliance, and governance.</p>
<p>G2 Objective 2.1: Provide written internal audit reports at the completion of audit 7 work within 30 days.</p>	<p>G3 Obj 14 Ensure that recommendations are supported by sufficient and appropriate evidence.</p>
<p>G2 Objective 2.3: Provide follow-up reports within year of report issuance to assess implementation of 9 recommendations.</p>	<p>G3 Obj 15 Track and report on management recommendation resolution.</p>
<p>[Redacted] G1 Objective 1.2: Identify sufficient resources to assure that audits can be completed. Internal audits might require 2 additional resources.</p>	<p>G4 Obj 16 Foster workplace culture of trust, dignity, and respect where staff feel valued and confident in their performance. G4 Obj 17 Identify sufficient resources and technology to assure that audits can be completed.</p>
<p>[Redacted] G1 Objective 1.6: Coordinate audit 6 activities with the external auditors.</p>	<p>G4 Obj 18 Develop a training program consistent with meeting continuing professional education requirements.</p>
<p>G3 Objective 3.1: Provide employee 10 direct access to internal audit reports.</p>	<p>[Redacted]</p>

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Office of the County Internal Auditor

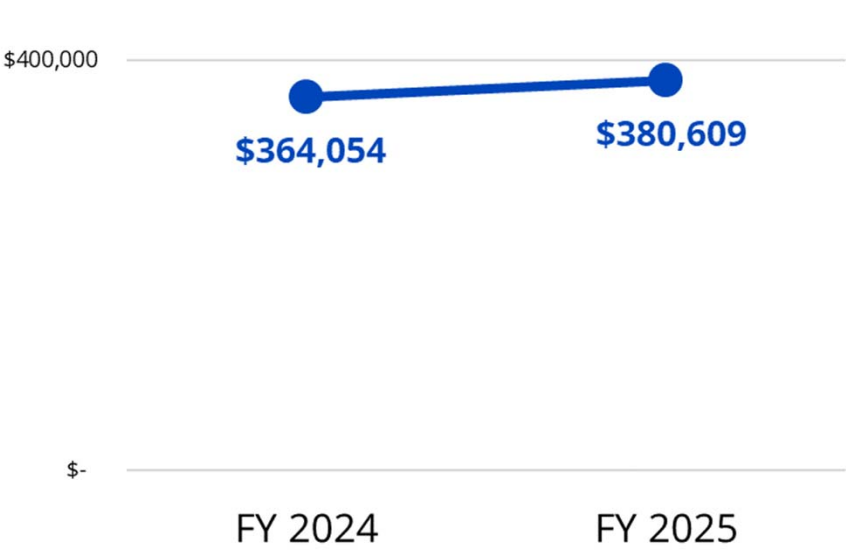
# Budget Proposal

## Fiscal Year 2025

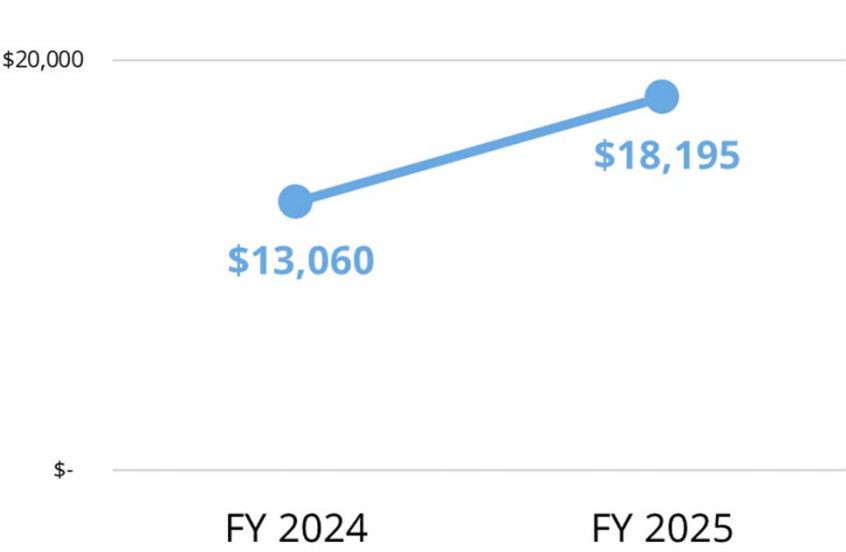


March 8, 2024

# Previous Year Comparison

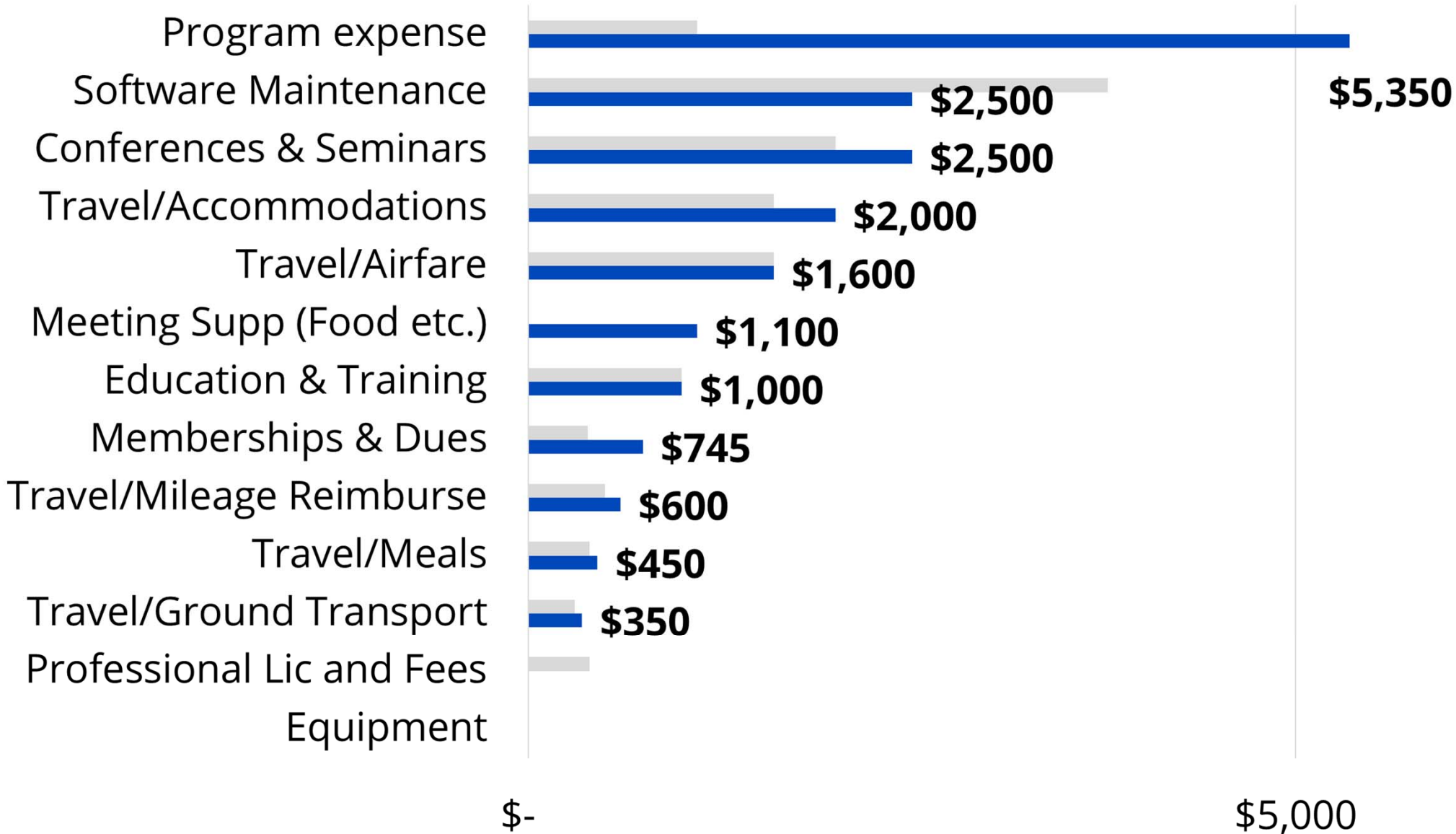


**Personnel**



**Materials and Services**





# Budget Adopted: June 19

# Popular Annual Financial Report

For the Fiscal Year Ended June 30, 2023



DESCHUTES COUNTY, OREGON



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## Introduction

Residents of Deschutes County,

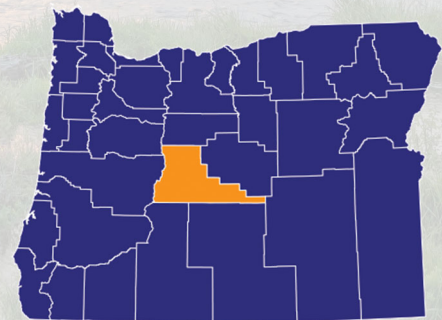
The purpose of the Deschutes County Popular Annual Financial Report (PAFR) is to provide residents with a relatively quick read of the highlights from the County’s Annual Comprehensive Financial Report (ACFR) for the fiscal year ended June 30, 2023, and to provide insight into long-term trends of the County’s largest financial indicators.

The ACFR is a detailed and complete financial presentation prepared in conformance with the United States Generally Accepted Accounting Principles (GAAP) and is available in its entirety online at [www.deschutes.org/finance](http://www.deschutes.org/finance). The ACFR was audited by Moss Adams LLP, an independent auditing firm, and received a clean opinion.

Respectfully Submitted,

Robert Tintle, MPA  
Chief Financial Officer

Jana Cain, CPA  
Controller



# Net Position

Deschutes County's net position as of June 30, 2023 was approximately **\$250 million**. Net Position is broken into two types: Capital Assets and Other Assets.

**Net position—Capital assets** represents the current value of County infrastructure, offset for amounts owed.

Infrastructure includes the County's investment in:

- Roads
- Vehicles and equipment
- Buildings for providing services

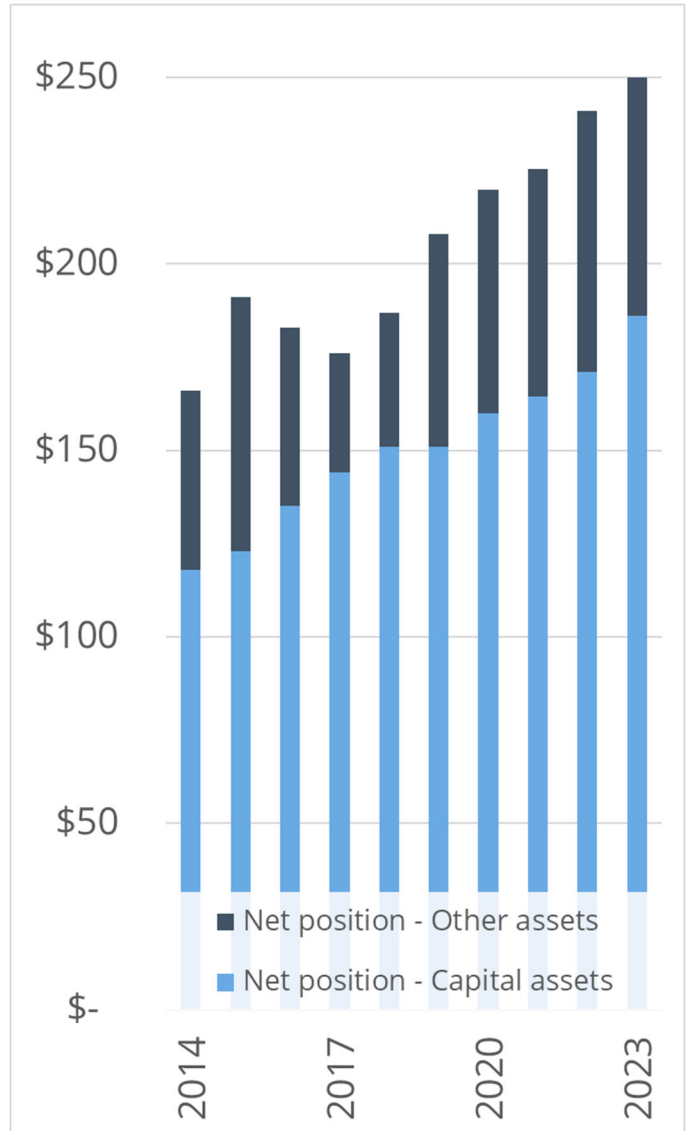
The net position of capital assets could be viewed in a similar manner as home-equity (i.e. in 2023, capital assets are worth \$186 million more than what is owed).

**Net position—Other assets** represents the current value of all other assets, offset for amounts owed.

- Cash reserves
- Inventory
- Loans and other receivables (businesses or people owing the County money)

The current value in net position of all other assets could be viewed in a similar manner to that of a checking account (i.e. other assets are worth \$64 million more than what is owed).

Net Position (in millions)

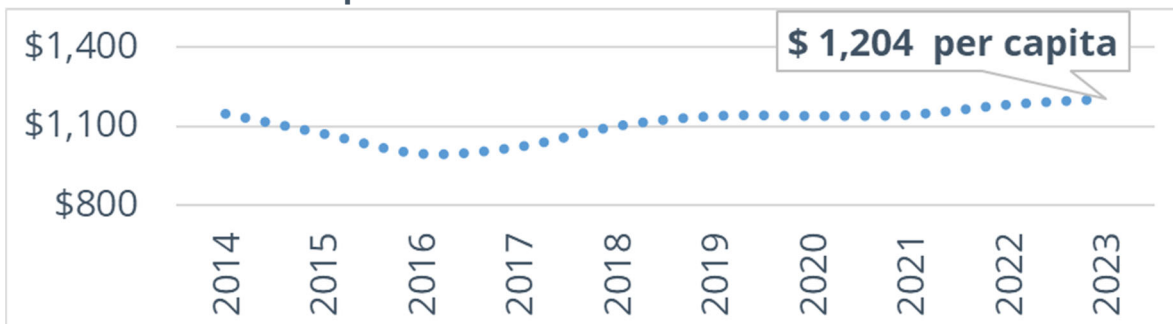


The graphics below show the last 10 years of net position as well as the net position per capita:

Net Position (in millions)

	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Net position - Capital assets	\$ 118	\$ 123	\$ 135	\$ 144	\$ 151	\$ 151	\$ 160	\$ 164	\$ 171	\$ 186
Net position - Other assets	48	68	48	32	36	57	60	61	70	64
<b>Total Net Position</b>	<b>\$ 166</b>	<b>\$ 191</b>	<b>\$ 183</b>	<b>\$ 176</b>	<b>\$ 187</b>	<b>\$ 208</b>	<b>\$ 220</b>	<b>\$ 225</b>	<b>\$ 241</b>	<b>\$ 250</b>

Net Position Per Capita



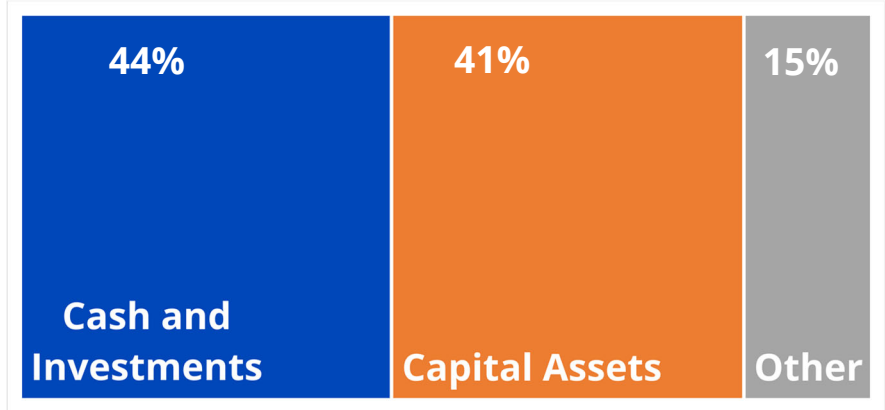
# Assets

Total assets held by Deschutes County as of June 30, 2023 was **\$587 million**, an **increase of 6%** from the prior year.

During fiscal year 2023, the County invested significantly in capital assets which support long-term service delivery. Capital assets increased by \$39.3 million primarily due to major transportation projects and Solid Waste improvements, including the Negus Transfer Station in Redmond.

“Other” assets are made up of receivables and inventory.

## Assets by Percent



## Assets (in millions)

	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Cash and Investments	\$ 125	\$ 127	\$ 141	\$ 148	\$ 164	\$ 191	\$ 197	\$ 245	\$ 268	\$ 256
Capital Assets	184	184	190	193	194	193	199	199	203	243
Other	(15)	34	24	63	49	55	73	80	82	88
<b>Total Assets</b>	<b>\$ 294</b>	<b>\$ 345</b>	<b>\$ 355</b>	<b>\$ 404</b>	<b>\$ 407</b>	<b>\$ 439</b>	<b>\$ 469</b>	<b>\$ 524</b>	<b>\$ 553</b>	<b>\$ 587</b>

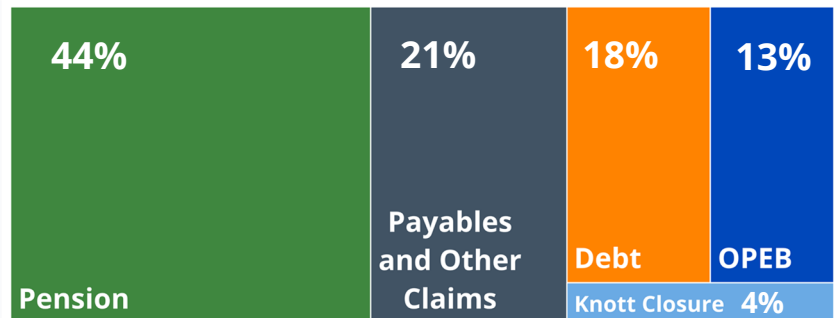
# Liabilities

Total liabilities incurred by Deschutes County as of June 30, 2023 was **\$336 million**, a **7% increase**.

In August of 2022, the County received \$21.4 million from issuing new debt for improvements to the Negus Transfer Station. This debt has a true interest cost of 3.3% and is scheduled for repayment over a 20-year period.

Future pension and other post-employment benefits (OPEB) payments continue to be the largest County liabilities.

## Liabilities by Percent



## Liabilities (in millions)

	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Pension	\$ -	\$ -	\$ 46	\$ 96	\$ 87	\$ 102	\$ 121	\$ 143	\$ 142	\$ 147
Debt	79	72	66	59	55	52	47	42	38	51
OPEB	17	46	20	33	34	35	35	36	44	44
Payables and Other Claims	22	26	29	29	35	34	35	67	77	80
Knott Closure	10	10	11	11	9	8	11	10	12	14
<b>Total Liabilities</b>	<b>\$ 128</b>	<b>\$ 154</b>	<b>\$ 172</b>	<b>\$ 228</b>	<b>\$ 220</b>	<b>\$ 231</b>	<b>\$ 249</b>	<b>\$ 298</b>	<b>\$ 313</b>	<b>\$ 336</b>

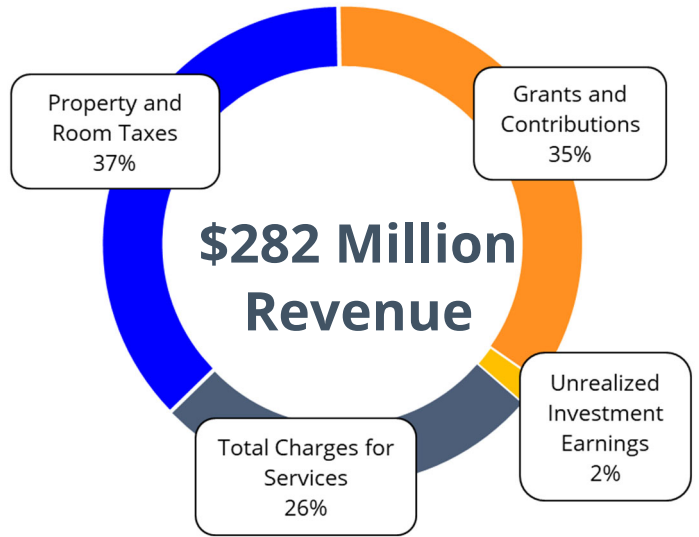
# Revenues

Deschutes County revenues for Fiscal Year 2023, were **\$282 million**, an increase of 14.1% over the prior year.

**Taxes** include both property tax revenue and room-tax revenue. Total tax revenue for the year was \$104 million, a 5.1% increase over the prior year. This was driven by a 5.6% increase in assessed property value and an addition of 1,169 new property tax accounts.

**Charges for Services** include payments made by residents for a specific service provided to the resident. Total charges for services for the year was \$74 million, a 3.8% increase over the prior year.

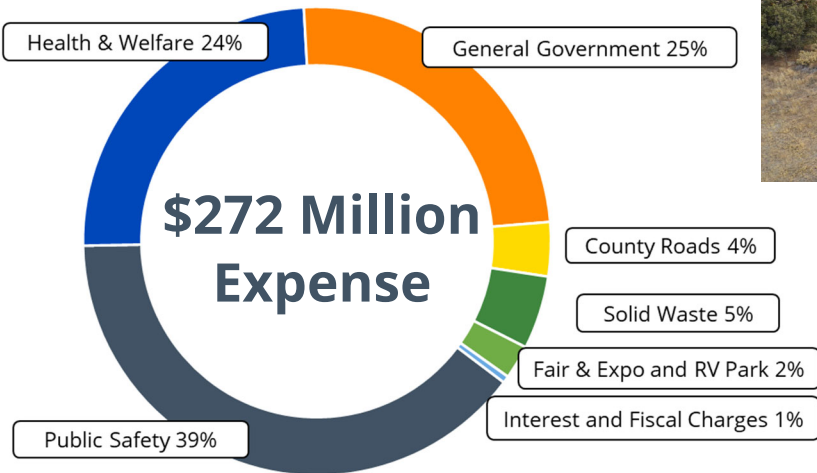
**Grants and Contributions** include payments made for services by the Federal, State, and other local governments. Grants and contributions totaled \$99 million, an 18.7% increase from the prior year. The increase was primarily driven by Health and Welfare programs as well as American Rescue Plan Act (ARPA) funding.



Roundabout at Hamhook and Deschutes Market

Deschutes County expenses for Fiscal Year 2023, were **\$272 million** (a 17.4% increase from the prior year).

# Expenses



**Public Safety** and **General Government** expenses increased by 23.6% and 37.8%, respectively, due primarily to rising personnel and technology costs.

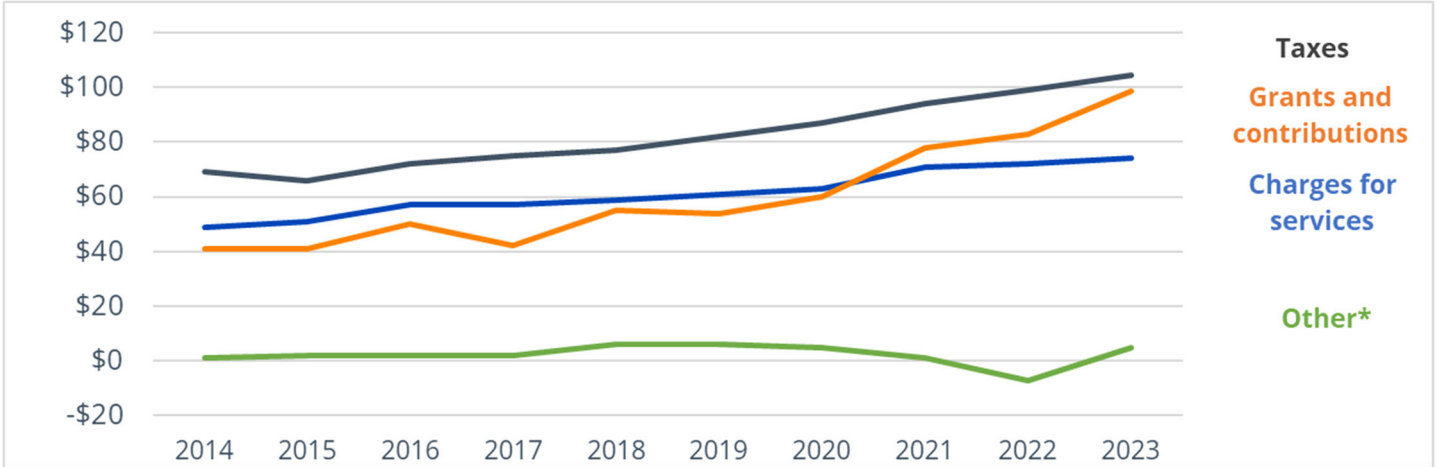
**Health & Welfare** expenses increased by 19.4%. However, revenues for this service area increased by 41.4% as a result of expanded services to County residents.

**County Roads** costs decreased due to a large portion of fiscal year 2023 funds spent on capital projects. These multi-year projects are not reported as expenses, but rather as capital assets on the Statement of Net Position.

**Solid Waste** expenses increased primarily due to the costs incurred to identify a new landfill site as the Knott Landfill is projected to reach capacity in 2029.

**Fair & Expo** expenses increased 30.7% due to multiple new and expanded event offerings in fiscal year 2023. New events included the High Desert Stampede, Fairwell Festival, and Cascade Equinox Festival.

# Revenues — 10 Year History

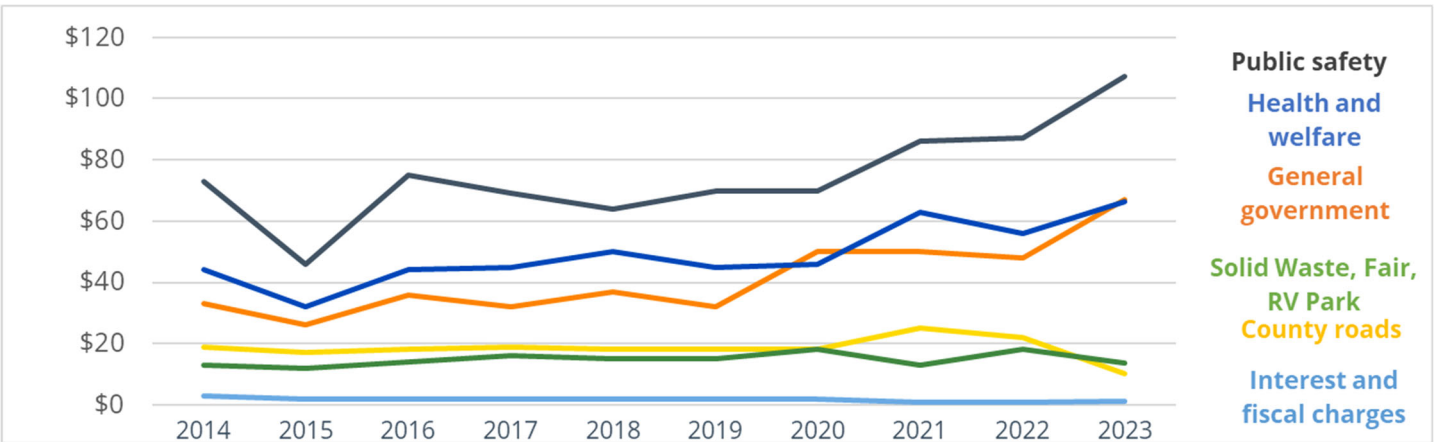


Revenues (in millions)

	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Taxes	\$ 69	\$ 66	\$ 72	\$ 75	\$ 77	\$ 82	\$ 87	\$ 94	\$ 99	\$ 104
Charges for services	49	51	57	57	59	61	63	71	72	74
Grants and contributions	41	41	50	42	55	54	60	78	83	99
Other*	1	2	2	2	6	6	5	1	(7)	5
<b>Total Revenues</b>	<b>\$ 160</b>	<b>\$ 160</b>	<b>\$ 181</b>	<b>\$ 176</b>	<b>\$ 197</b>	<b>\$ 203</b>	<b>\$ 215</b>	<b>\$ 244</b>	<b>\$ 247</b>	<b>\$ 282</b>

\* FY22 other revenues decreased due to unrealized investment losses.

# Expenses — 10 Year History



Expenses (in millions)

	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Public safety	\$ 73	\$ 46	\$ 75	\$ 69	\$ 64	\$ 70	\$ 70	\$ 86	\$ 87	\$ 107
Health and welfare	44	32	44	45	50	45	46	63	56	66
General government	33	26	36	32	37	32	50	50	48	67
County roads	19	17	18	19	18	18	18	25	22	10
Solid Waste, Fair & Expo, RV Park	13	12	14	16	15	15	18	13	18	20
Interest and fiscal charges	3	2	2	2	2	2	2	1	1	1
<b>Total Expenses</b>	<b>\$ 185</b>	<b>\$ 135</b>	<b>\$ 189</b>	<b>\$ 183</b>	<b>\$ 186</b>	<b>\$ 182</b>	<b>\$ 204</b>	<b>\$ 238</b>	<b>\$ 232</b>	<b>\$ 272</b>

# Debt

During fiscal year 2023, Deschutes County borrowed \$21.4 million to finance improvements to the Negus Transfer Station. This increased the debt to **\$54.9 million** (\$265 per County resident). In November of 2023 (after 2023 fiscal year-end), the County borrowed an additional \$26.6 million; \$20.6 million for the expansion of the Deschutes County Courthouse, and \$6.0 million to refinance prior debt at favorable repayment terms.

On June 30, 2023, Deschutes County owed:

Debt (in millions)	Bonded Debt	Premium (Discount)	Total
General Government	\$ 21.3	\$ 0.7	\$ 22.0
Pension	5.8	-	5.8
Solid Waste	23.2	3.0	26.2
Fair & Expo and RV Park	0.9	-	0.9
<b>Total debt</b>	<b>\$ 51.2</b>	<b>\$ 3.7</b>	<b>\$ 54.9</b>

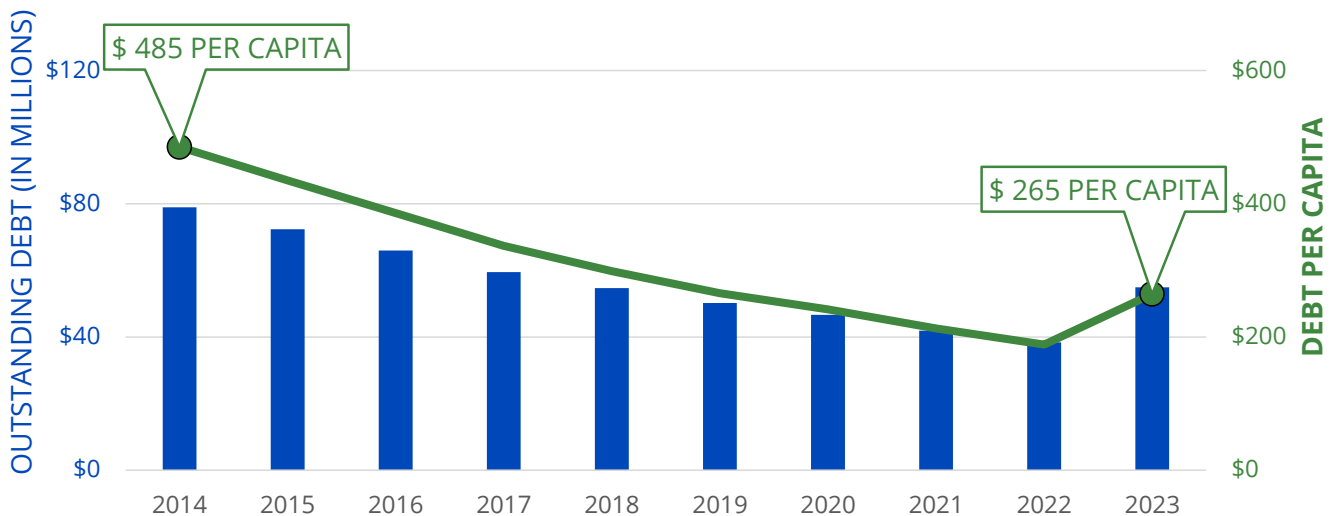
The County's creditworthiness was evaluated in November 2023 and maintained its rating of Aa1 as measured by Moody's Investors Service. Moody's rating of Aa1 represents that Deschutes County is a "High Quality" investment to municipal bond investors. In their ratings rationale, Moody's noted improving resident income levels as well as the County's solid financial profile with healthy and stable reserves and liquidity.



Knott Landfill

The chart below presents the amount of debt outstanding each year, as well as the amount attributable to each resident in Deschutes County. The debt per capita metric illustrates the County's debt burden in relation to an individual resident.

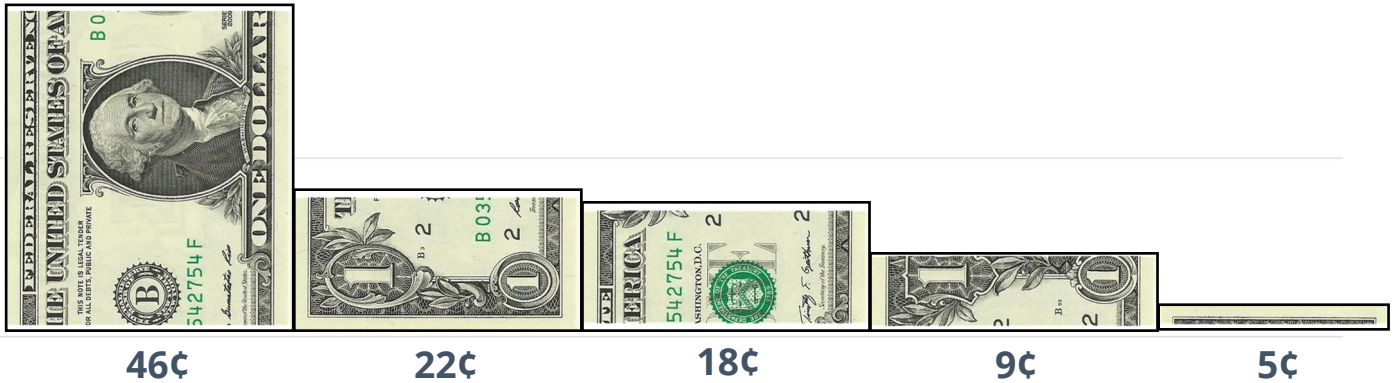
## 10 Year History of Debt



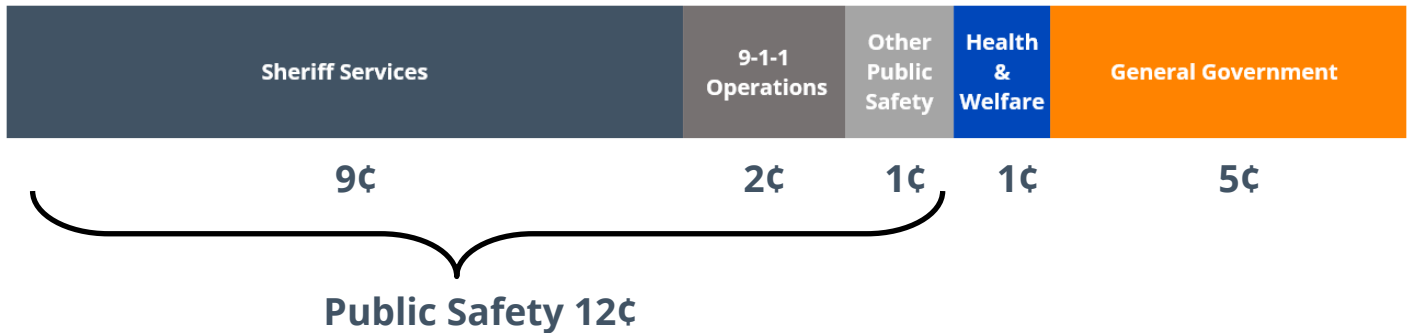
# Where do your taxes go?

Although Deschutes County is the tax collector for all taxing districts within the county, overall **only 18 cents of each dollar paid in taxes is retained by the County**. The remaining 82 cents is passed through to other government agencies to provide for schools, police and fire departments, parks, libraries, and more.

**NOTE:** Tax allocations based on the City of Bend Taxing District (Tax Code 1001). All other city/rural allocations are similar.



Deschutes County uses its taxes to fund Public Safety, Health & Welfare, and General Government.



**Public Safety** includes the Sheriff's Office, Deschutes 9-1-1, Community Justice, District Attorney's Office (including Victims' Assistance), and Justice Court.

**Health & Welfare** includes Deschutes County Health Services and Veterans' Services.

**General Government** includes a variety of departments, such as the Assessor's Office, Clerk's Office including elections, and Community Justice.

# Property Taxes

$$\text{Assessed Value} \times \text{Tax Rate} = \text{Tax Bill}$$

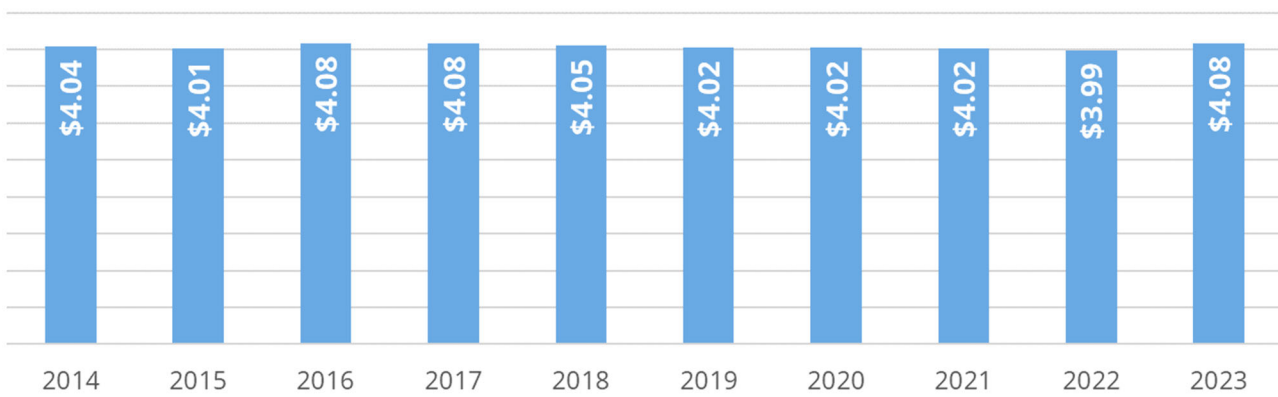
In Oregon, property taxes are billed based on the **assessed value** of a property multiplied by the approved (levied) **tax rate**.

Deschutes County is funded, in part, by five separate tax levies.

- General Deschutes County Levy: District Attorney, Assessor, Community Justice, and more, for all residents.
- Countywide Law Enforcement Levy: County Jail, Civil Unit, and Search and Rescue for all residents.
- Rural Law Enforcement Levy: Detectives, Patrol, and Records for residents outside of city limits.
- 9-1-1 Levy: Traditional 9-1-1 services for all residents.
- Extension and 4-H Levy: Extension and 4-H services for all residents.

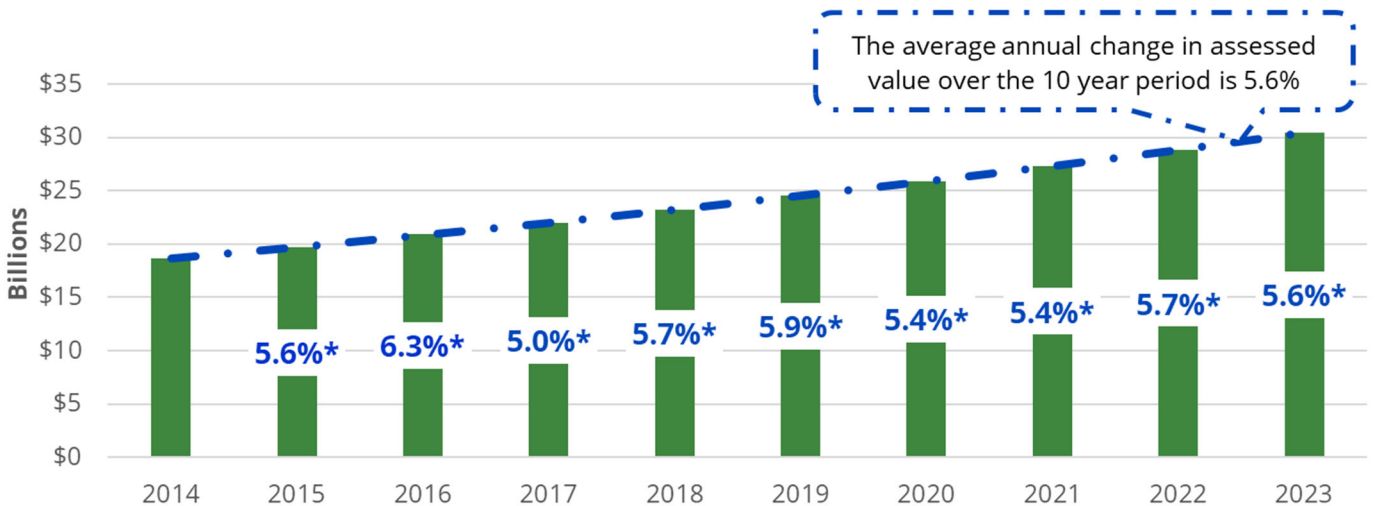
The cumulative total of **tax rates** levied and the **assessed value** for the past 10 years are shown below.

## 10 Year History of the Tax Rates\*



\*Rate per \$1,000 of assessed value (excludes expired local option levies)

## 10 Year History of Assessed Value



\*% Change in Assessed Value from prior year

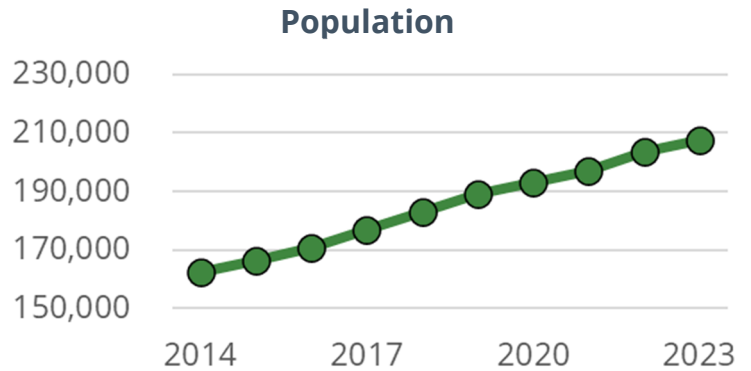


# Demographics and Staffing Ratio

**Population** for Deschutes County has increased by 28% over the 10 year period. This translates into an average annual growth rate of **2.8%**. The average annual growth rate for the State or Oregon overall was 0.8% during the same period.

Deschutes County's population increased by 2.1% in 2023 to 207,561.

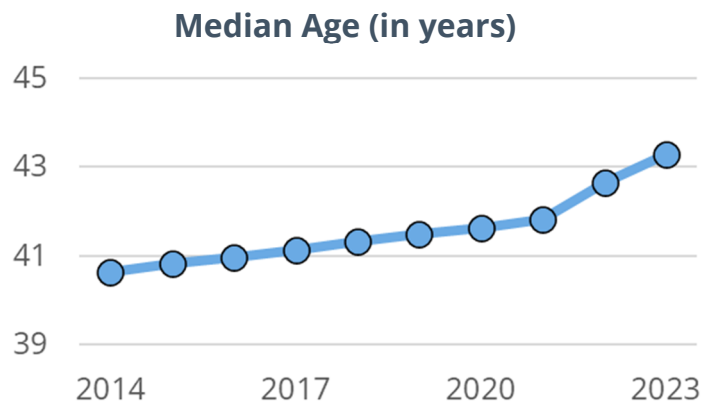
Source: Portland State University



**Median Age** for Deschutes County has increased by 2.65 years since 2014. The median age for the United States over that same period hovered around 38 years old.

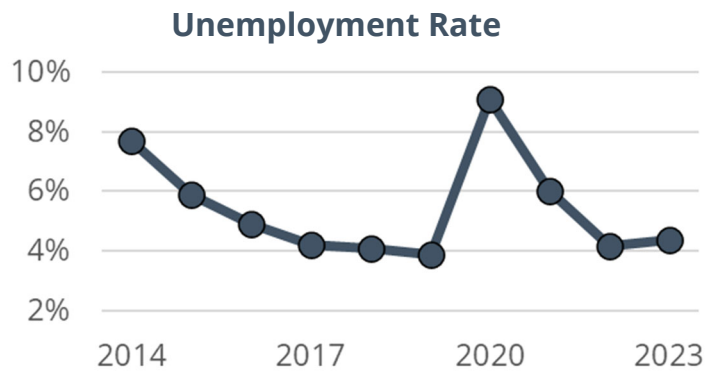
At the end of Fiscal Year 2023, 50% of County residents were older than **43.28** years and 50% were younger.

Source: Portland State University



**Unemployment Rate** for Deschutes County for Fiscal Year 2023 ended at **4.4%**. Deschutes County started the 10 year period shown with an unemployment rate of 7.7%.

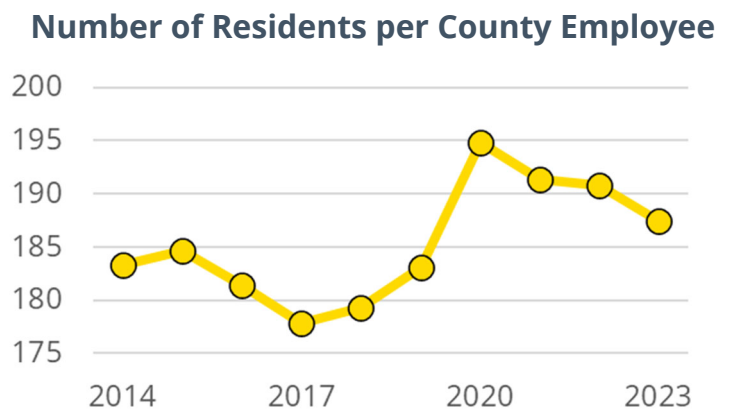
Source: Oregon Employment Department



**Population Per Full-Time Employee** for Deschutes County has remained stable over the last 10 years. At the end of Fiscal Year 2023, there were **187** residents per County employee.

This data point provides insight into the size of government versus the population governed.

Source: Deschutes County



# Additional Information

## Disclosures:

- **Intended audience:** Residents seeking high-level financial information concerning the County.
- **Measurement focus:** The financial data presented in the Popular Annual Financial Report (PAFR) uses the same measurement focus and basis of accounting as the County's Annual Comprehensive Financial Report (ACFR).
- **Financial information:** Financial information from the ACFR's government-wide financials have been reproduced (full-accrual). Fund-level information has not been provided, but is available in the ACFR. All financial entities (including component units), as presented in the ACFR, have been consolidated in the PAFR.
- **Departures from accounting terminology:** In preparing the PAFR, minor departures were made from standard *generally accepted accounting principal (GAAP)* prescribed terminology. Such departures were made in an attempt to avoid confusion concerning the materials presented. Highlighted departures from GAAP are:
  - "Assets" as used in this report, at times, include both Assets and Deferred Outflows.
  - "Liabilities" as used in this report, at times, include both Liabilities and Deferred Inflows.
  - "Net Position - Other Assets" includes both Restricted & Unrestricted Net Position.
  - "Net Position - Capital Assets" is Net Investment in Capital Assets.
- **Volatility due to changes in accounting measurement:** Over the course of the 10 years presented, the Government Accounting Standards Board (GASB) has made modification to how certain items are presented (e.g. pensions and other post-employment benefits). Such changes in recognition practices introduced volatility to the 10 year trend information, as presented.

---

## Contact Information:

Deschutes County Finance Department  
 1300 NW Wall Street, Suite 200  
 Bend, Oregon 97703  
[finance@deschutes.org](mailto:finance@deschutes.org)

*Special thanks to Finance Department staff and their commitment to the underlying debits/credits.*



Government Finance Officers Association

Award for  
Outstanding  
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Financial Reporting

Presented to

**Deschutes County  
Oregon**

For its Annual Financial Report  
For the Fiscal Year Ended

June 30, 2022

*Christopher P. Morrill*

Executive Director/CEO



FINANCE



# Transition Audits

Proposal to extend to department directors in addition to elected official



# Elected Official Transition Audits

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# 2 in the past 2.5 years

**Treasurer  
(221 Hours)**

[Link to  
Treasurer Report](#)

**District  
Attorney  
(98 Hours)**

[Link to  
DA Report](#)

- Purpose:
- Smooth transition
  - Risk assessment



# Typical Objectives

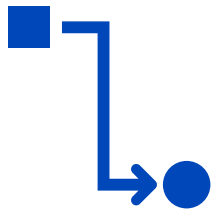
- 1** Overview of history of the office and financial trends
- 2** Statutory requirements unique to the office
- 3** County policy in high-risk areas:
  - Cash handling
  - Information technology
  - Contracting
  - Procurement cards
  - Physical access
  - Equipmentprevious audits inform risk assessment
- 4** Be aware of compliance issues





# Typical Findings / Recommendations

**Establish a transition plan**



**Update policies and procedures**



**Update contractor or vendor documents**

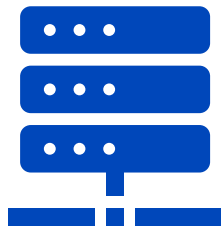


# Proposed: Include Department Heads

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# Who we missed

Information  
Technology



Forestry



Solid Waste



# Benefits and Drawbacks

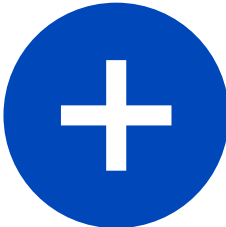
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Action plan for a new official

Highlights need for transition planning

Introduction to Internal Audit

Unexpected audit hours



# Upcoming

---

**Veteran  
Services  
Office**



# Any thoughts?

---

## Memorandum of Understanding

This Memorandum of Understanding ("MOU") is entered into by and between the Deschutes County Administrator ("Administrator") and the Deschutes County Internal Auditor ("Auditor") on this 1 day of February, 2024.

### Recitals:

WHEREAS, The Deschutes County Office of the Internal Auditor has traditionally offered policy reviews through feedback to management on new policies and amendments to policy;

WHEREAS, This role is supported by Deschutes County Code which states that,

The purpose of having the Office is to provide independent objective assurance *and consulting services* designed to add value and improve Deschutes County's operations through improved performance and enhanced control environment thereby providing greater accountability to its residents. DC 2.14.001 (emphasis added);

WHEREAS, According to Deschutes County Code, "the County Internal Auditor has neither a management nor a policy role; and no operational authority nor responsibility." DC 2.14.025 (A);

WHEREAS, The Office of the Internal Auditor can provide policy reviews to Deschutes County managers to support improvements in internal control while maintaining independence; and

WHEREAS, Consulting services performed by the Office of Internal Audit must be approved by the County Administrator after consultation with the Audit Committee. (DC 2.14.030 (C)); now therefore it is agreed as follows:

### Terms:

1. Staff from the Deschutes County Office of Internal Audit will provide policy reviews as a framework for conversations and suggestions on new or changing Deschutes County policies while maintaining independence. Services include:
  - Participating as a non-voting member of the Policy Advisory Committee.
  - Providing feedback to department heads and elected officials when policies are added or amended, as requested.
  - Providing feedback to management about policies that are implemented in response to audit recommendations, as requested.

- 2. The term "Policy Reviews" does not include audit work conducted within the context of an audit following Government Auditing Standards. The term "Policy" includes department or office documented policies and procedures in addition to official Deschutes County Policies.
- 3. Providing policy reviews does not impair Internal Audit independence because Internal Audit is solely offering a review not drafting policy and is not a voting member of the Policy Advisory Committee.
- 4. Internal audit staff will provide feedback based on professional knowledge. A representative from Internal Audit will attend Policy Advisory Committee meetings. Internal Audit staff will respond to requests for policy reviews from management in a timely manner with tracked changes to proposed policies.
- 5. All policy reviews will include the following language.

This policy review is intended to supplement information management should consider when establishing policy and does not constitute an audit under Government Auditing Standards. The policy review may not include all information that should be considered and does not imply auditor endorsement of the policy. Management assumes all management responsibilities, will evaluate the adequacy and results of the policy review, and will accept responsibility for results.

- 6. Policy reviews do not constitute an audit under Government Auditing Standards.
- 7. Policy reviews shall be overseen by the department head or elected official responsible for the policy.
- 8. Management assumes all management responsibilities, will oversee services, will evaluate the adequacy and results of the policy review, and will accept responsibility for results.

Deschutes County Internal Auditor: Edge

Date: 1/29/24

Deschutes County Administrator: Nick White

Date: 1/29/2024





**Recommendations**  
**5**

# Fair and Expo Cash Handling

**The Office of County Internal Audit:**

Elizabeth Pape, CIA, CFE – County Internal Auditor  
Aaron Kay – Performance Auditor

**Take survey by  
clicking here**

**Audit committee:**

Daryl Parrish, Chair - Public member  
Jodi Burch – Public member  
Joe Healy - Public member  
Kristin Toney - Public member  
Summer Sears – Public member  
Stan Turel - Public member  
Patti Adair, County Commissioner  
Charles Fadeley, Justice of the Peace  
Lee Randall, Facilities Director



To request this information in an alternate format, please call (541) 330-4674 or send email to [internal.audit@Deschutes.org](mailto:internal.audit@Deschutes.org)

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  - Background on Fair and Expo ..... 1
- 2. Finding: Incomplete financial procedures increase risks..... 4**
- 3. Management Response ..... 9**
- 4. Appendix A: Objective, Scope, and Methodology ..... 11**
  - Objectives and Scope ..... 12
  - Methodology ..... 13

## Highlights:

### Why we performed this audit:

As a money-making County enterprise, Fair and Expo has a higher revenue-related risk-profile than other County departments.

### What we recommended:

We recommended that Fair and Expo management:

- conduct a fraud risk assessment and implement procedures to address risks.
- outline major financial processes and determine whether any roles are conflicting.
- design efficient reconciliation processes between financial systems.
- document security controls for all financial information systems.

## Fair and Expo Cash Handling

### What we found:

We found that Fair and Expo did not have complete policies and procedures to ensure that revenue due to the organization was received and deposited. Fair and Expo had not conducted assessments to document risks in areas such as:

- overall fraud risks,
- segregation of duties within financial processes,
- risks associated with using separate financial information systems, and
- information system user access and transaction authority.

Despite a vulnerable control environment, we did not observe any instances of fraud or theft.

## 1. Introduction

The Deschutes County Audit Committee authorized the review of cash handling practices for the Fair and Expo Center in the Internal Audit Program Work Plan for 2024-2025. Internal audits of fiscal controls are routinely performed for identified County departments or functions. Audit objectives, scope, and methodology can be found in **Appendix A**.

### Background on Fair and Expo

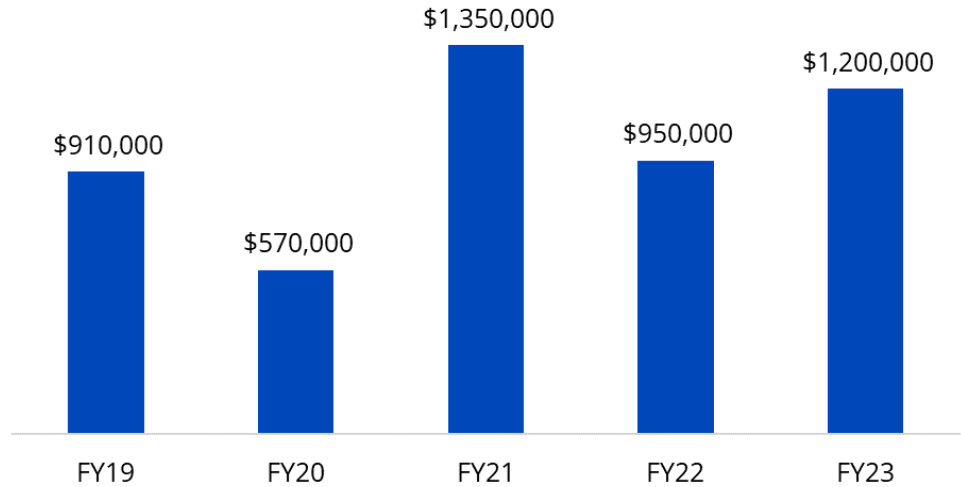
The Fair and Expo Center is a County-operated 320-acre facility located in Redmond. Fair and Expo's largest event is the annual Deschutes County Fair, but it also hosts over 400 events annually with an emphasis on events supporting youth, agriculture, and community. In addition to events, Fair and Expo operates a 105-space RV park, which is open year-round. Fair and Expo supports County operations by acting as a response and evacuation center, as well as a staging area for fires and other disasters. Most recently, it served as the host site for the Deschutes County Circuit Court during the Covid-19 pandemic.

The County classifies Fair and Expo finances as an enterprise fund due to the department's business-like operations aimed at generating revenue to sustain its operations. In addition to revenue generated directly by Fair and Expo, operations are supplemented by County transient room tax.

Since 2019 revenue has been variable but is trending up.<sup>1</sup>

**Figure I**

Fair and Expo revenue increased from \$910,000 in 2019 to \$1.2 million in 2023.



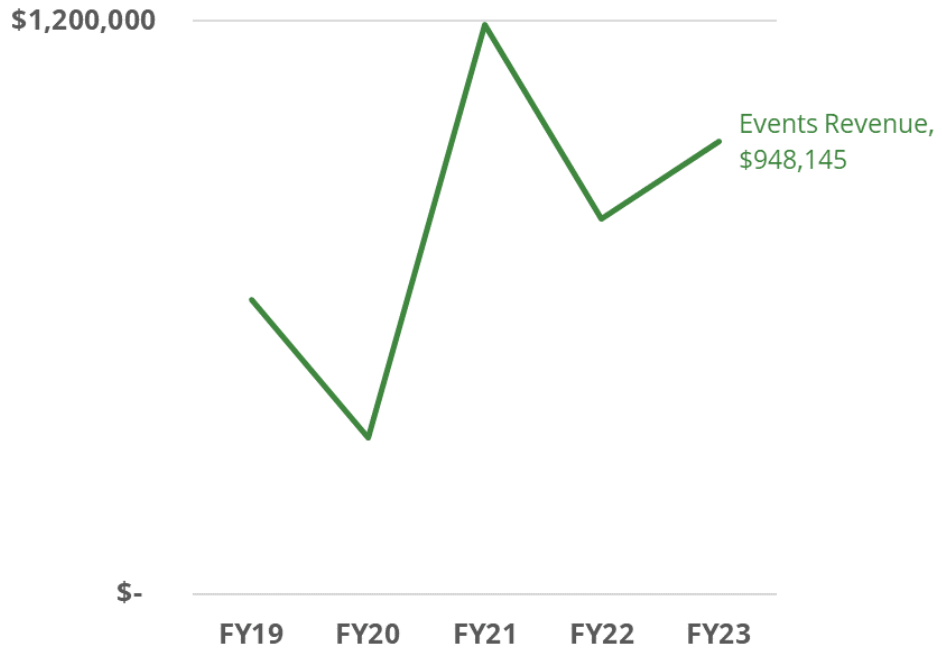
Source: Deschutes County Financial Information

Fair and Expo revenue is comprised of a few different categories, with the largest source being event revenue. These are fees that are paid by outside organizers who rent Fair and Expo facilities for private events. These include large events such as music festivals and small events such as weddings.

<sup>1</sup> The audit did not include funds assigned to the Annual County Fair, the County Fair Food and Beverage Fund, the Fair and Expo Food and Beverage Fund or the RV Park. These funds have either been the subject of recent audits or will be the subject of future audits in fiscal year 2024 or 2025.

**Figure II**

Event revenue fluctuated from 2019 to 2023

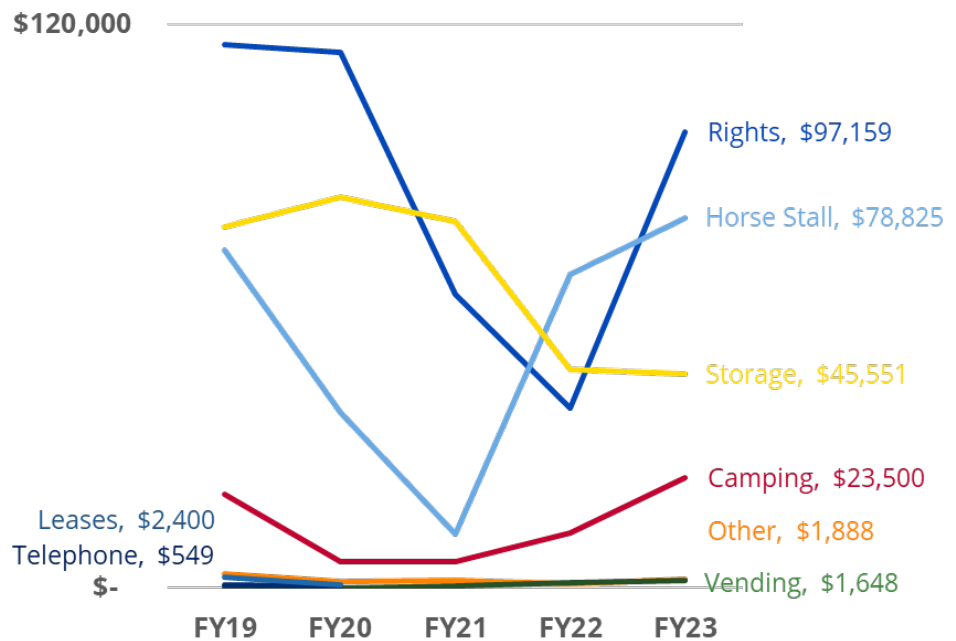


Source: Deschutes County Financial Information

Other categories of revenue are much smaller comprising of signage rights, horse stall rentals, RV storage, camping, vending machine revenue, and other smaller categories.

**Figure III**

Smaller Fair and Expo revenue streams



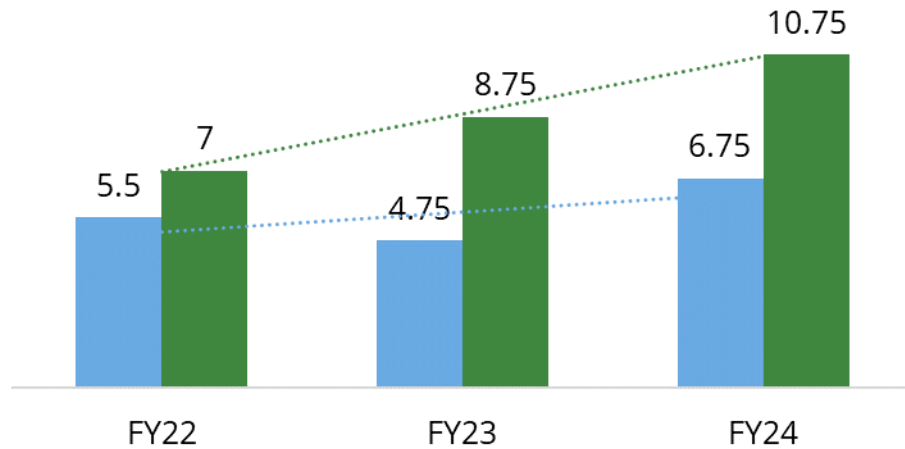
Source: Deschutes County Financial Information

Fair and Expo staffing has increased since Fiscal Year 2022 from

12.5 full-time equivalent employees to 17.5 in 2024. Operations staff grew from 7 to 10.75. Administrative staff experienced a smaller increase, from 5.5 to 6.75.

**Figure IV**

**Operations** staff increased more than **Administrative** staff.



Source: Deschutes County Budget Books

**2. Finding: Incomplete financial procedures increase risks**

As a business-type County enterprise, Fair and Expo has a higher revenue-related risk-profile than other County departments or elected offices which are more public service oriented. Yet Fair and Expo did not have complete policies and procedures to ensure that revenue due to the organization was received and deposited. Fair and Expo had not conducted assessments to document risks in areas such as overall fraud risks, segregation of duties within financial processes, risks associated with using separate financial information systems, and information system user access and transaction authority. Despite a vulnerable control environment, we did not observe any instances of fraud or theft.

Fair and Expo did not have comprehensive financial policies and procedures even though they are required by County policy. Staff verbally explained some procedures, but not all were documented. Documented procedures were limited to

information system instructions with screen shots. They did not include other critical processes such as custody, reconciliation, and reporting. The absence of substantial documented procedures appears to be long-standing and was noted by auditors in a 2007 report.

Staff may not have prioritized documenting procedures because they had not conducted a fraud risk assessment of their operations. Fraud risk assessments serve as the foundation for developing a robust and comprehensive set of procedures within an organization. Conducting a fraud risk assessment before designing procedures will help staff understand the importance of procedures and why they must be followed. By identifying potential vulnerabilities and weaknesses, Fair and Expo can proactively address and mitigate the risk of fraudulent activities through the design and implementation of tailored procedures specific to their unique working environment. By documenting the assessment process, the department creates the framework for long-term resilience, continuous learning, and adaptive capabilities for any future improvements.

- 1. Fair and Expo management should conduct a fraud risk assessment and document outcomes.**
- 2. Fair and Expo management should document procedures to address the risks identified in the fraud risk assessment.**

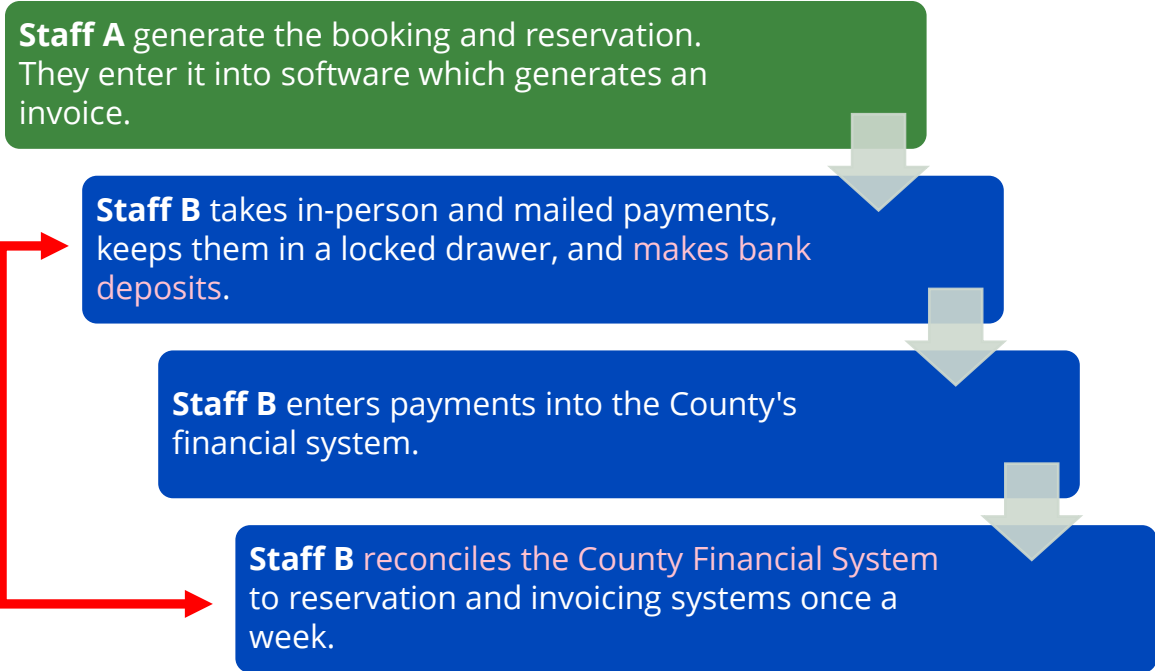
Policies governing cash controls are in place to keep people from stealing money from the County, but they can also seem redundant or inefficient. Without documented policies staff may engage in high-risk activities that seem to increase efficiency but also increase the likelihood of fraud. Auditors observed multiple cases of high-risk business activities where internal controls were missing or insufficient.

#### **Staff assigned conflicting duties.**

There are fewer eyes on the process, and it is easier to conceal



theft when there are conflicting duties. For example, at a high level the process of booking an event through posting it in the County financial system involved four steps.



**Figure V**

Most duties were performed by one person, creating conflicts.

There were too many duties concentrated in the Staff B role. Of particular concern is that the same person made bank deposits and reconciled the financial system with the reservation and invoicing systems. These duties should always be performed by different people when possible. If duties cannot be separated, other controls need to be put in place.

County financial policy requires directors to design and implement effective cash handling controls, including adequate segregation of duties.

In addition to putting more eyes on the process, segregating duties also creates opportunities for cross training and succession planning. There are a few different options for segregating duties. Fair and Expo may need to add staff to distribute duties more effectively. As noted in the **Background** section, the number of Operations staff has increased faster than Administrative staff. Other options include re-assigning duties to other existing staff or implementing dual controls where two staff work together to complete a task.

**3. *When designing procedures, Fair and Expo management should outline major financial processes, along with staff assigned to specific activities, and determine whether any roles are conflicting.***

**Manual reconciliation process was inefficient and led to less confidence about finances.**

Fair and Expo used three different software packages to process events: Event Pro (reservations and booking), Square (invoicing and payments), and Munis (financial reporting). A fourth system was used for RV storage. It was not possible to automatically reconcile transactions in these systems. In a sample of 20 events from Fiscal Year 2023, there were discrepancies between systems for eight events. There were no missing transactions, but the reconciliation process was inefficient and required help from Fair and Expo staff researching records. This is a long-standing finding and was noted by auditors in 2007.

The software systems are not integrated, so reconciliation between systems was manual. Staff relied on an excel spreadsheet with date and event names to track transactions between systems, but the process was inefficient and based on text and date fields that did not always correspond.

Transactions in one system could easily be missing from others. With a manual reconciliation process, there is less confidence that all booked events were invoiced and that all receipts were entered into the County's financial system. It is also less efficient because it takes longer to track transactions between systems.

County financial policy requires directors to design and implement effective cash handling controls. Effective controls for information systems include communication networks for linking technology and reconciliation of systems.

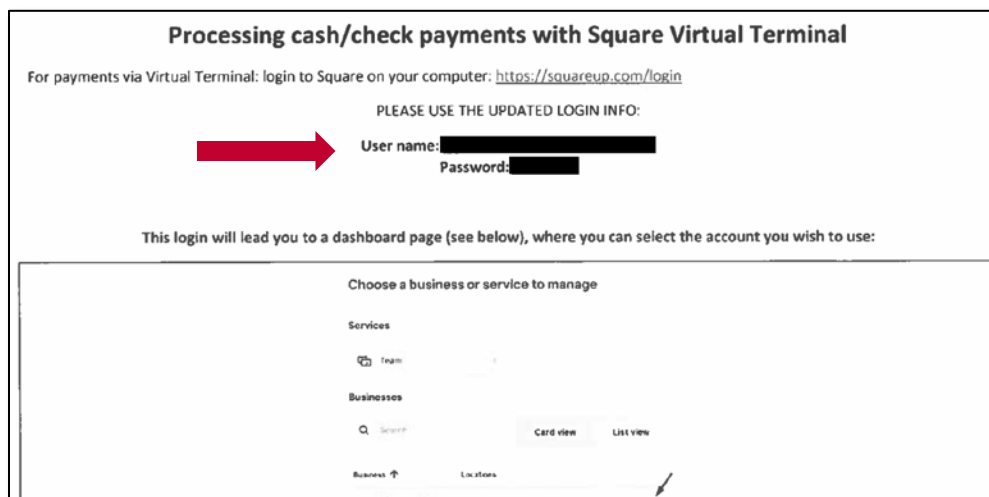
**4. Fair and Expo management should design and document an efficient reconciliation process across systems. It might be helpful to create a log of unique identifiers from each system to record how records relate to one another.**

**Staff shared the password to payment software.**

County Information Technology policy requires that employees keep passwords confidential and change them frequently. Multiple Fair and Expo staff shared the same password to access event invoicing and payment software. The account was assigned to the generic public contact email address. Staff had not configured the software for multiple users.

**Figure VI**

Instructions, including the shared password, were kept in binders at every Square terminal. (username and password redacted in this image, but available in the original document)



Without unique accounts, multiple staff could delete bookings or change the bank account information without being identified. The risk was higher because the software was web-based and did not require logging into the County network for access. The password was also kept in binders at terminals, so anyone with access to the building could also access sensitive financial information. Even former employees could have access because staff did not change the password on the account for ten months.

Since the start of the audit, staff have set up unique user profiles with passwords and multifactor identification. They now have

distinct roles; for example, only the Deschutes County Chief Financial Officer can change the bank account. Each staff member has their own identifier and password. But these improvements did not address the underlying cause, management had not documented data security controls including system access and who can execute transactions.

5. ***Fair and Expo management should document data security controls for all financial information systems including who has access to data and rights to execute transactions. Each user should have unique access credentials.***

### 3. Management Response



Fair & Expo Cash Handling Audit

Management Responses

First and foremost, Fair & Expo appreciates working with the Audit department and their willingness to engage and discuss items, and to work to understand the unique intricacies of the Fair & Expo department, its enterprise fund status, and the operations of the Fair & Expo department. While we may not fully agree with all related findings or elements, we do appreciate the opportunity to share our perspective, and the additional consideration shown by the Internal Audit team in areas of concern.

Fair & Expo also believes it is key to identify, as the Cash Handling Audit identifies, that despite recommendations for improved documentation or improved control strategies, **no instances of fraud or theft were observed or identified.**

Incomplete financial procedures increase risks.

1: Fair & Expo management should conduct a fraud risk assessment and document outcomes.

We agree with this recommendation. Fair & Expo has informally conducted fraud risk assessments on an ongoing basis, without documentation. Moving forward, a formalized and documented fraud risk Assessment will be conducted on a regular basis.

2: Fair & Expo management should document procedures to address the risks identified in the fraud risk assessment.

We agree with this recommendation. Fair & Expo has informally conducted fraud risk assessments on an ongoing basis, without documentation. Moving forward, a formalized and documented fraud risk assessment will be conducted on a regular basis. This documentation will be utilized to formulate, or update documented financial procedures.

Staff assigned conflicting duties.

3: When designing procedures, Fair & Expo management should outline major financial processes, along with staff assigned to specific activities, and determine whether any roles are conflicting.

We agree with this recommendation and are working to create separation or clarity and/or documented steps between assigned financial duties. In the current system, while an individual employee may perform multiple duties, multiple parties have access to/or awareness of the activities to provide additional layers of oversight and to identify any item that may be out of compliance.

Manual Reconciliation process was inefficient and led to less confidence about finance.

4: Fair and Expo management should design and document an efficient reconciliation

process across systems. It might be helpful to create a log of unique identifiers from each system to record how records relate to one another.

We agree with this recommendation; however, our current systems are not compatible with this recommendation. Fair & Expo has proactively researched new computer systems that are capable of handling the complex process necessary to operate as an enterprise fund; and to reconcile as a County Department. F&E went as far as to make an investment in new software, that ultimately was unable to improve upon current concerns; as well as working with Deschutes County IT to try to design a custom solution; both without success. To date, no single system has been identified as a solution; but efforts are ongoing.

Staff shared the password to payment software.

5: Fair and Expo management should document data security controls for all financial information systems including who has access to data and rights to execute transactions. Each user should have unique access credentials.

We agree with this recommendation. During the audit it was discovered that the software utilized had made updates, allowing for new controls to be put in place. F&E worked with Deschutes County Finance to adjust software, and shared passwords are no longer utilized.

Deschutes County Fair & Expo Center  
3800 Airport Way, Redmond OR 97756  
(541) 548-2711  
EXPO.DESCHUTES.ORG

#### 4. Appendix A: Objective, Scope, and Methodology

The County Internal Auditor was created by the Deschutes County Code as an independent office conducting performance audits to provide information and recommendations for improvement.

The audit included limited procedures to understand the systems

of internal control around revenues. Audit findings result from incidents of non-compliance with stated procedures and/or departures from prudent operation. The findings are, by nature, subjective. The audit disclosed certain policies, procedures and practices that could be improved. The audit was neither designed nor intended to be a detailed study of every relevant system, procedure, or transaction. Accordingly, the opportunities for improvement presented in the report may not be all-inclusive of areas where improvement may be needed and does not replace efforts needed to design an effective system of internal control.

Management has responsibility for the system of internal controls, including monitoring internal controls on an ongoing basis to ensure that any weaknesses or non-compliance are promptly identified and corrected. Internal controls provide reasonable but not absolute assurance that an organization's goals and objectives will be achieved.

## Objectives and Scope



*"Audit objectives" define the goals of the audit.*

Objectives included:

1. Review of internal controls for cash handling with the Fair and Expo Center as outlined in County Finance policy for cash handling (F-11). Identify areas to improve efficiency and effectiveness. Additionally, review management of any change cash, petty cash, receipts, credit cards, judgements, collections, and billings, as applicable.
2. Be aware of any issues with compliance with federal and state regulations and requirements, as may be applicable.

Scope and timing:

The audit occurred in October – December 2023. Included in review of cash handling of Fair and Expo accounting for Fund 6159651. The audit did not include funds assigned to the Annual

County Fair, the County Fair Food and Beverage Fund, the Fair and Expo Food and Beverage Fund or the RV Park. These funds have either been the subject of recent audits or will be the subject of future audits in fiscal year 2024 or 2025. The focus of the review was on event revenue, rentals, and other small payments. The scope of the audit did not include all aspects of the internal controls employed.

## Methodology



*Audit procedures are created to address the audit objectives.*

Audit procedures included:

- Interviewing staff related to cash handling, receipting, and billing procedures (staff reviewed and answered the County's cash handling checklist provided in the Deschutes County cash handling policy F-11).
- Reviewing documents provided.
- Reviewing and analyzing receipt transaction data for the identified funds; and
- Reconciling transactions between systems. We relied on a random sample of 20 transactions out of a population of 237. With 8 discrepancies identified, the projection to the population is between 46 and 144 discrepancies at the 95% confidence level.

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.

(2018 Revision of Government Auditing Standards, issued by the Comptroller General of the United States.)



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***Please take a survey on this report by clicking this link:***

<https://forms.office.com/g/f8ewGXMyBw>

***Or use this QR Code:***



If you would like to receive future reports and information from Internal Audit or know someone else who might like to receive our updates, sign up at

<http://bit.ly/DCInternalAudit>.

Office of the County Internal Auditor

# Fair and Expo Center

Cash Handling  
2324-8



March 8, 2024

# Background

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# By the Numbers



320 Acres

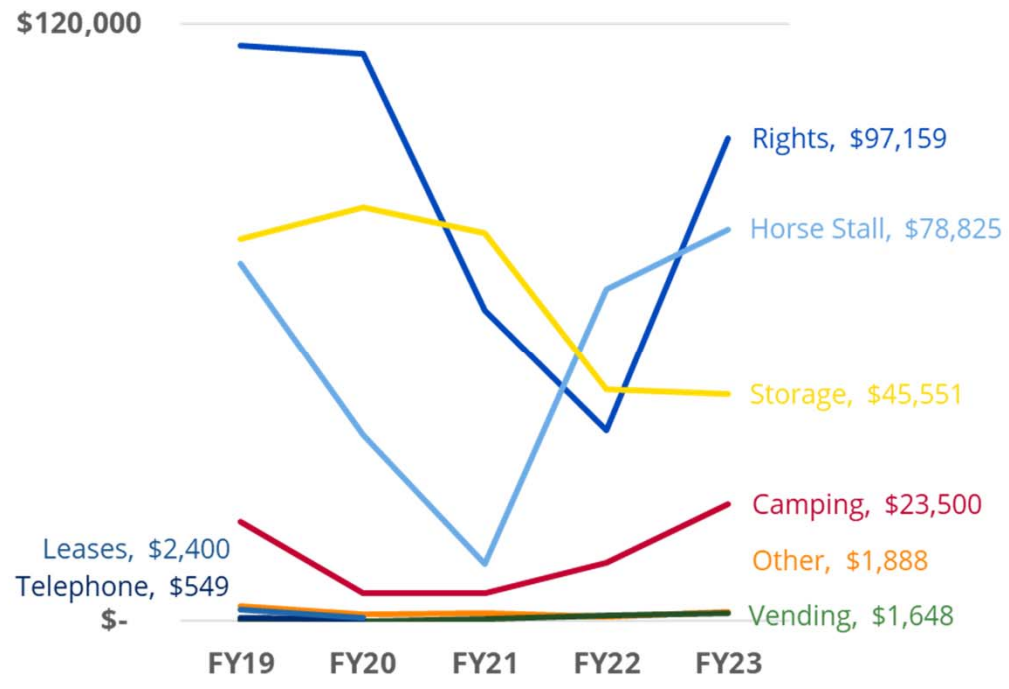
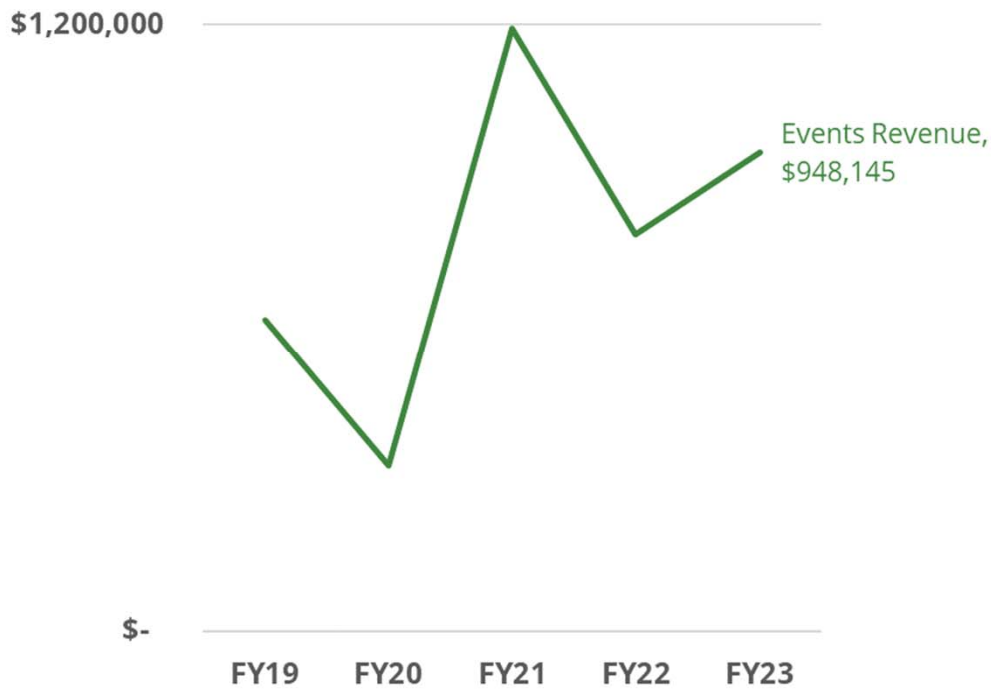
400 Events

17.5 Staff

\$1.2 Million in Revenue



# Most Revenue for Events



# Audit Objective

- 1. Review internal controls for cash handling as outlined in County Finance policy for cash handling (F-11).**
- 2. Be aware of any issues with compliance with federal and state regulations and requirements, as may be applicable.**

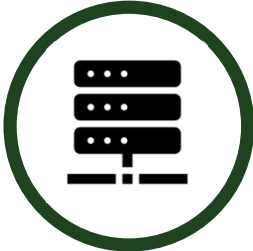


# Fieldwork

Interview  
and  
checklist



Reconciled  
systems  
with Munis



Best  
practices



# Findings and Recommendations

---



# Incomplete procedures increase risks



Deschutes County Administrative Policy No. F-11  
Effective Date: March 19, 2007

## CASH HANDLING PRACTICES POLICY

### STATEMENT OF POLICY

It is the policy of Deschutes County to ensure that County directors and managers design, implement and monitor effective cash handling controls.

### APPLICABILITY

This policy applies to all County departments and County service districts under the governance of the Board of County Commissioners.

### POLICY AND PROCEDURE

This policy sets out overall guidance on cash handling practices.

Cash includes the following:

- Currency (paper money and coin)
- Checks
- Credit card slips
- Money orders
- Travelers checks
- Bank drafts, etc.

1) County directors and managers shall design, implement and monitor effective cash handling controls. Cash handling procedures shall be distributed to all appropriate staff.

2) Management will periodically review internal control policies and procedures pertaining to cash to ensure they are working as intended. It is critical that managers promote an effective internal control environment. Effective internal controls minimize the potential for errors or irregularities to occur, and if they do occur, will detect such errors or irregularities in a timely manner during the normal course of business.

3) To assist directors and managers establish and monitor their cash handling systems, the Internal Audit Program shall develop and circulate a Cash Handling Guide (Guide), which is attached hereto and incorporated herein as Exhibit A. The Guide highlights the internal controls that are required by County departments.

Management should utilize the Guide and checklist as a reference. Some items may not apply to every cash handling system, depending on the quantity of the cash transactions and the functions of the department. Implementation of some of these controls may not be possible due to limited resources. In these cases, compensating controls shall be developed.

4) Exemptions from implementing any internal control policy or procedure must be granted in writing by the County Administrator or his/her designee.

5) Required procedures

a) Cash shall be turned over to the Finance Department or deposited in a designated bank depository within 24 hours of receipt in accordance with Finance policy P-1999-075.

It is the policy of Deschutes County that County directors and managers design, implement, and monitor cash handling controls.

Internal Audit assistance: Guide

Required Procedures  
24-hour deposits  
Pre-numbered receipts  
Bank accounts: F-7  
Over/Short reporting: F-9



# Fraud Risk Assessment

Australian Government  
Commonwealth Fraud Prevention Centre

Learn about fraud and fraudsters  
How to assess risks



Risk identification



Risk analysis



Risk evaluation



Risk treatment



# 1. Recommendation

---

Conduct a fraud risk assessment and document outcomes.



Have conducted informal fraud risk assessments, but not documented



## 2. Recommendation

---

Document procedures to address the risks identified in the fraud risk assessment.



**Agree**

Will use to update procedures



# Incompatible duties

**Staff A** generate the booking and reservation. They enter it into software which generates an invoice.

**Staff B** takes in-person and mailed payments, keeps them in a locked drawer, and makes bank deposits.

**Staff B** enters payments into the County's financial system.

**Staff B** reconciles the County Financial System to reservation and invoicing systems once a week.



## 3. Recommendation

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Outline major financial processes, along with staff assigned to specific activities, and determine whether any roles are conflicting.



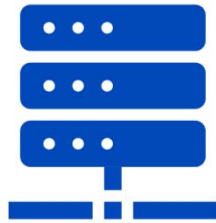
**Agree**

Will create separation or clarify roles. Currently others have access or awareness to provide oversight



# Manual reconciliation = Less confidence

---



Event Pro-  
Reservations  
and Booking



Square-  
Invoicing and  
Payments



Munis-  
Financial  
Reporting

Name—Date—Amount



## 4. Recommendation

Design and document an efficient reconciliation process across systems. It might be helpful to create a log of unique identifiers from each system to record how records relate to one another.



**Agree**

Have not found a technical solution that works. Did not address a log of unique identifiers.

*Less Focus on Root Cause*





# Shared passwords create risk

## Processing cash/check payments with Square Virtual Terminal

For payments via Virtual Terminal: login to Square on your computer: <https://squareup.com/login>

PLEASE USE THE UPDATED LOGIN INFO:

User name: [REDACTED]

Password: [REDACTED]

This login will lead you to a dashboard page (see below), where you can select the account you wish to use:

The screenshot shows a dashboard titled "Choose a business or service to manage". It features several sections: "Services" with a "Team" link, "Businesses" with a search bar and "Card view" / "List view" toggle, and a "Business" section with an upward arrow and "Locations" text. A mouse cursor is pointing at the bottom right of the dashboard area.



## 5. Recommendation

Document data security controls for all financial information systems including who has access to data and rights to execute transactions. Each user should have unique access credentials.



**Agree**

Staff no longer sharing a password. Did not address data security controls.

*Less Focus on Root Cause*



# Questions and Comments?

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## Complete the Survey!



# The Office of County Internal Audit

## Overtime and Compensatory Time: Enhanced oversight will improve transparency.

#23/24-6



# Background on OT and CT

Overtime = hours worked > 40 hours.

Comp time = agreed conversion of overtime to leave

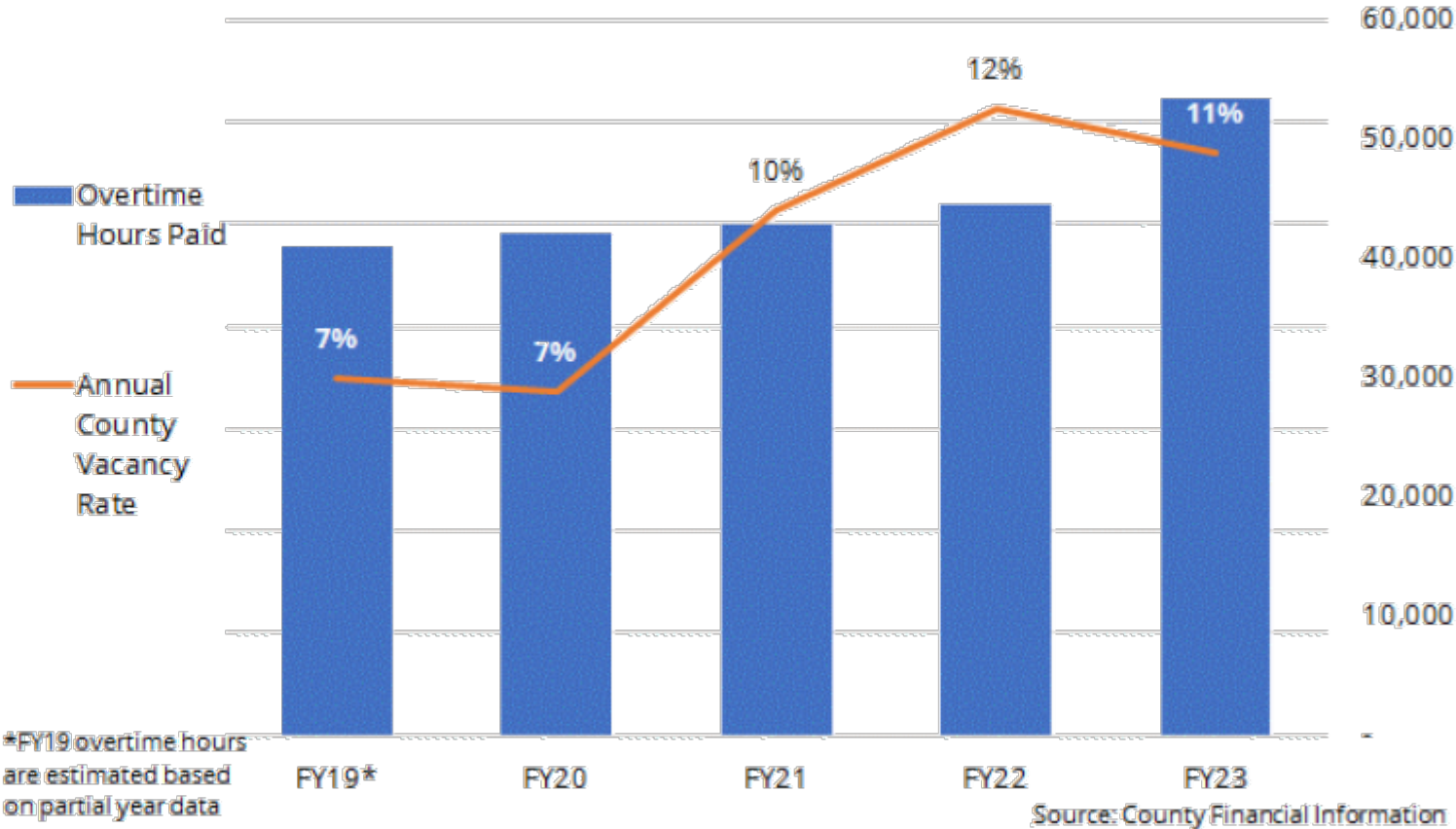
Overtime Paid at 1.5x (plus)

Comp leave used counts toward 40 hours work week

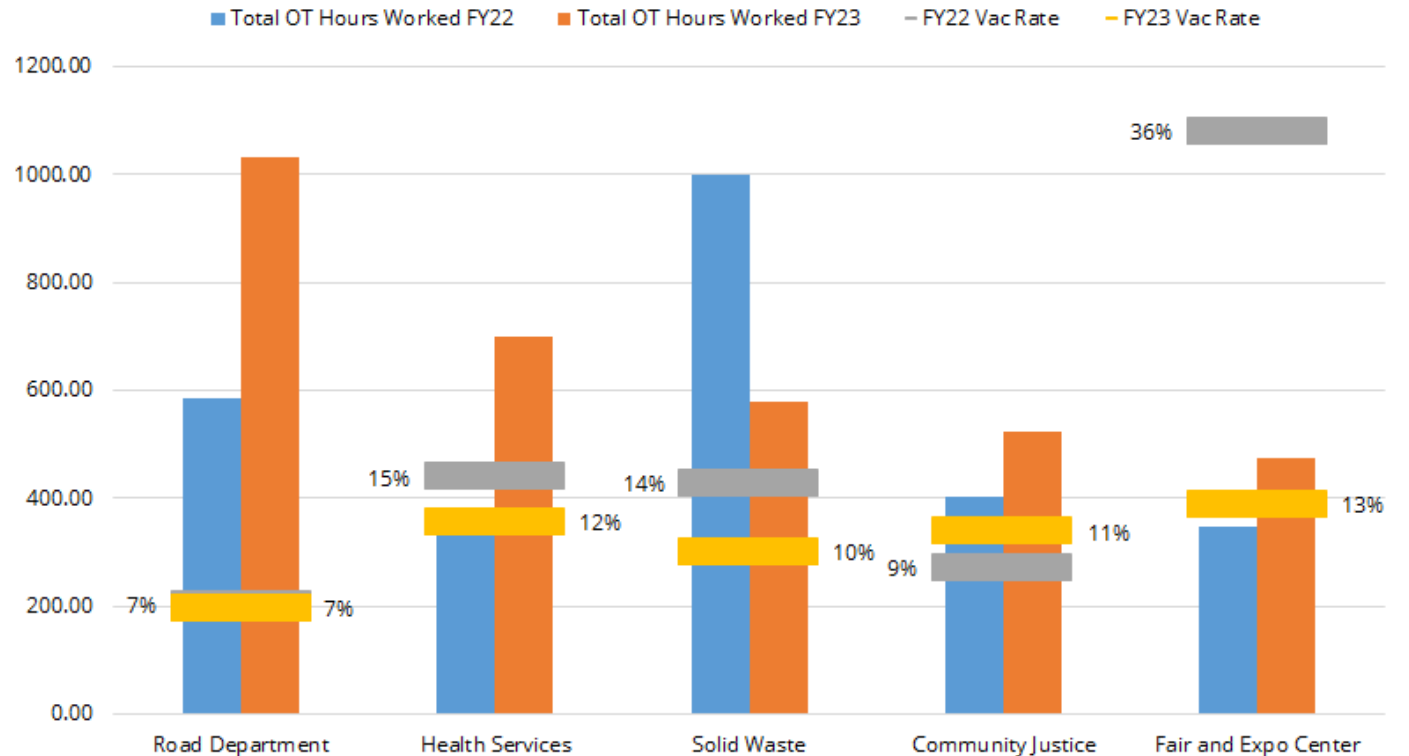


# The vacancy explanation

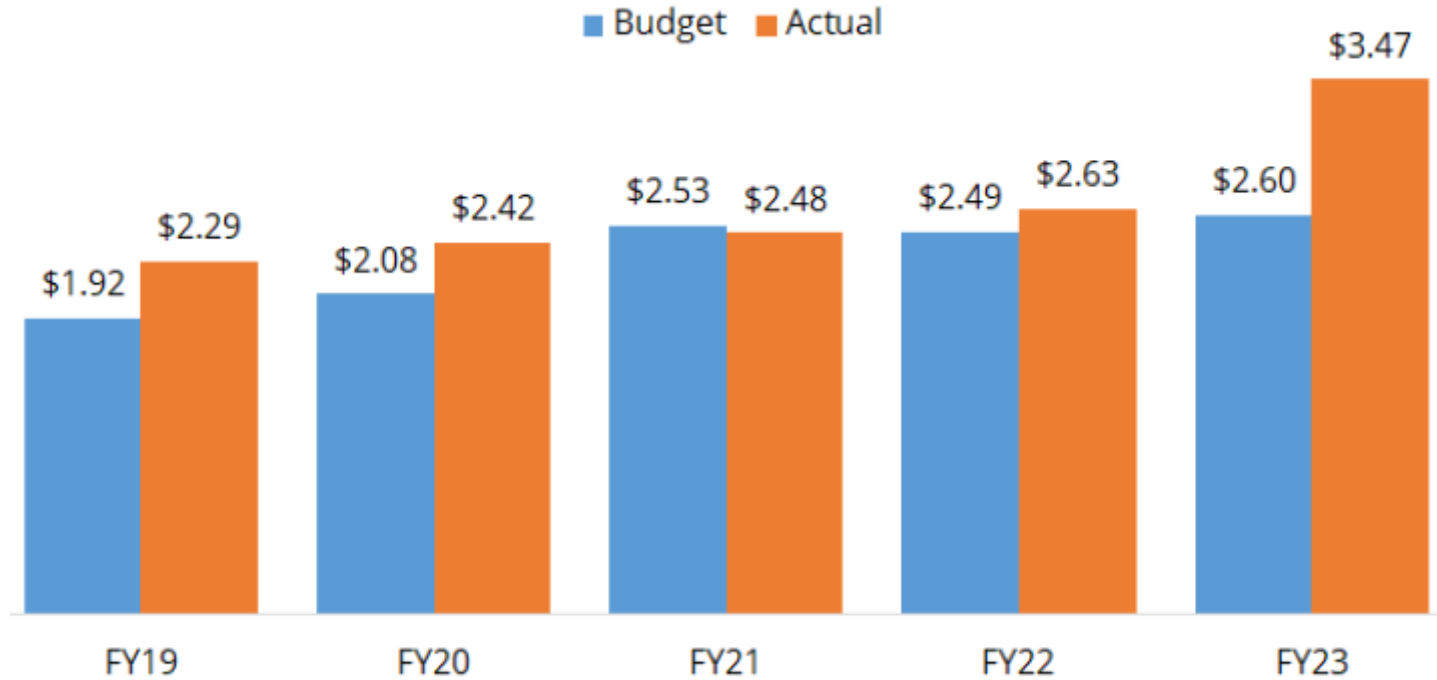
**Figure V**  
Higher vacancy rates seen over the last three fiscal years correlate into increased overtime hours.



# The vacancy explanation (not all)



# Overtime budgeting



Source: County Financial Information

shown in millions





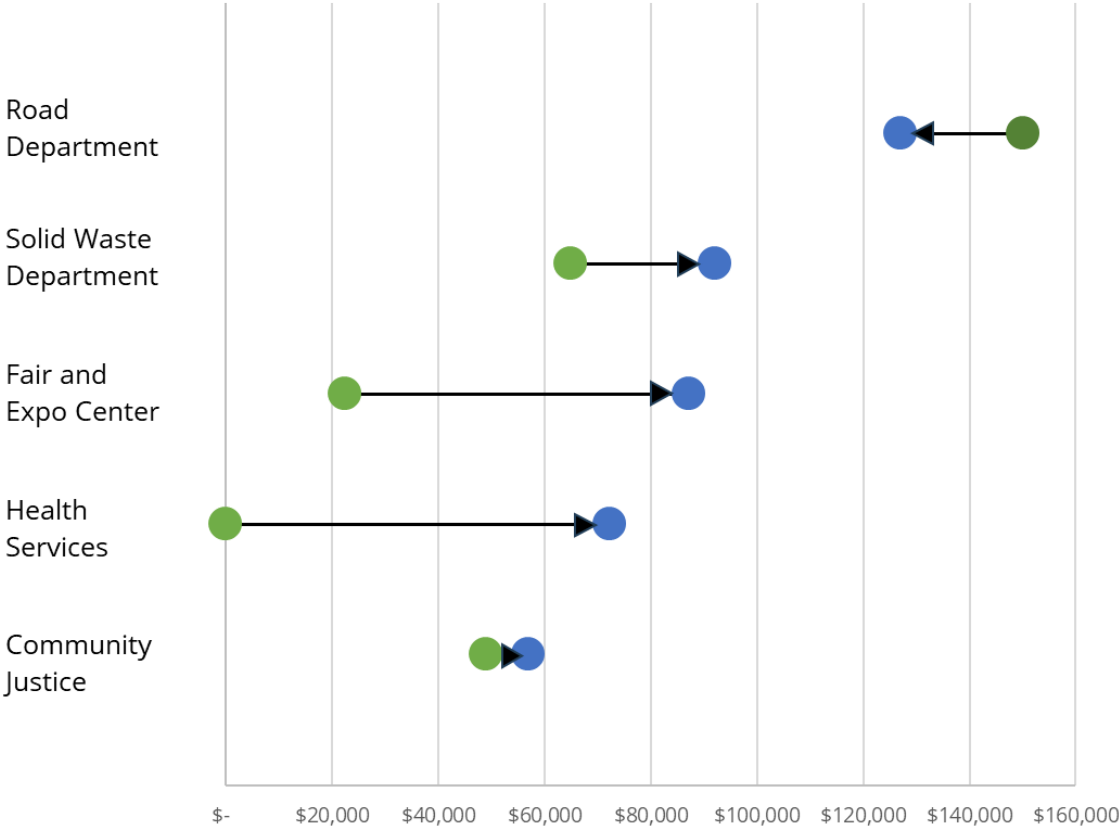
# Overtime budgeting

Given the Sheriff's Office overtime usage, underestimating their FY23 budget to actual costs had a large impact.



# Overtime budgeting (all others)

Among departments with over 50k in overtime expenses, the Road Department was the most efficient in managing their overtime budget for FY2023.



# Finding – Inadequate budgeting for overtime expenses is obscured within overall personnel costs.

Item 3.



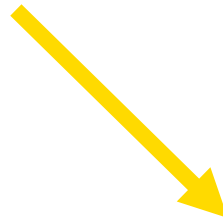
## Budget to Actuals Report Health Services - Admin - Fund 274 FY24 YTD November 30, 2023 (unaudited)

**41.7%**  
Year Complete

### Total Personnel Costs



Regular Employees
Extra Help (Temp Employee)
On Call
Overtime
Time Management
Health-Dental Ins (ISF)
Retiree Health Insurance
PERS Employee-Employer
PERS - Fund 575 for D-S
PERS - Reserve Fund
FICA
Workers' Comp Insurance
Unemployment Insurance
Life-Long Term Disability
FSA Administration Fee
Paid Leave Oregon



RESOURCES	Fiscal Year 2023			Fiscal Year 2024			Projection	%	\$ Variance
	Budget	Actuals	%	Budget	Actuals	%			
OHP Capitation	367,074	367,074	100%	435,349	158,505	36%	435,349	100%	-
Interest on Investments	97,750	390,781	400%	262,007	257,650	98%	562,030	215%	300,023
State Grant	379,180	142,133	37%	160,000	207,433	130%	160,000	100%	-
Other	160,495	33,725	21%	9,000	139,541	999%	161,977	999%	152,977
Federal Grants	454,405	592,179	130%	-	-	-	-	-	-
<b>TOTAL RESOURCES</b>	<b>1,458,904</b>	<b>1,525,892</b>	<b>105%</b>	<b>866,356</b>	<b>763,128</b>	<b>88%</b>	<b>1,319,356</b>	<b>152%</b>	<b>453,000</b>
<b>REQUIREMENTS</b>	<b>Budget</b>	<b>Actuals</b>	<b>%</b>	<b>Budget</b>	<b>Actuals</b>	<b>%</b>	<b>Projection</b>	<b>%</b>	<b>\$ Variance</b>
Personnel Services	6,738,820	6,093,176	90%	6,519,513	2,550,705	39%	6,736,196	103%	(216,683)
Materials and Services	6,998,683	6,732,321	96%	7,534,229	2,992,237	40%	7,577,904	101%	(43,675)
Capital Outlay	12,000	-	0%	43,750	-	0%	43,750	100%	-
Administration Allocation	(11,228,846)	(11,228,846)	100%	(12,596,186)	-	0%	(12,596,186)	100%	-
<b>TOTAL REQUIREMENTS</b>	<b>2,520,656</b>	<b>1,596,650</b>	<b>63%</b>	<b>1,501,306</b>	<b>5,542,943</b>	<b>369%</b>	<b>1,761,664</b>	<b>117%</b>	<b>(260,358)</b>
<b>TRANSFERS</b>	<b>Budget</b>	<b>Actuals</b>	<b>%</b>	<b>Budget</b>	<b>Actuals</b>	<b>%</b>	<b>Projection</b>	<b>%</b>	<b>\$ Variance</b>
Transfers In- OHP Mental Health	80,771	80,771	100%	81,250	-	0%	81,250	100%	-
Transfers Out	(230,635)	(230,635)	100%	(300,174)	(125,070)	42%	(300,174)	100%	-
<b>TOTAL TRANSFERS</b>	<b>(149,864)</b>	<b>(149,864)</b>	<b>100%</b>	<b>(218,924)</b>	<b>(125,070)</b>	<b>57%</b>	<b>(218,924)</b>	<b>100%</b>	<b>-</b>
<b>FUND BALANCE</b>	<b>Budget</b>	<b>Actuals</b>	<b>%</b>	<b>Budget</b>	<b>Actuals</b>	<b>%</b>	<b>Projection</b>	<b>%</b>	<b>\$ Variance</b>
Beginning Fund Balance	3,884,332	4,007,465	103%	3,665,544	3,786,843	103%	3,786,843	103%	121,299
Resources over Requirements	(1,061,752)	(70,758)	-	(634,950)	(4,779,814)	-	(442,308)	-	192,642
Net Transfers - In (Out)	(149,864)	(149,864)	-	(218,924)	(125,070)	-	(218,924)	-	-
<b>TOTAL FUND BALANCE</b>	<b>\$ 2,672,716</b>	<b>\$ 3,786,843</b>	<b>142%</b>	<b>\$ 2,811,670</b>	<b>(\$ 1,118,041)</b>	<b>-40%</b>	<b>\$ 3,125,611</b>	<b>111%</b>	<b>\$313,941</b>

- A** Projection includes adjustment for anticipated unearned revenue. Amounts will be finalized at fiscal year-end.
- B** Includes carryforward of \$125k in unspent FY23 PacificSource Behavioral Health Workforce Diversity Grant.
- C** Personnel projections include anticipated 3% vacancy.



# Recommendation #1

---

The Finance Department monthly financial reports should include overtime expenses for major funds when the projected personnel services requirements exceed budgeted levels.



# Finding – Insufficient documentation regarding premium pay decisions hinders transparency. Item 3.

---

Records of exempt overtime decisions found only in the department.



# Recommendation #2

---

The County should establish a centralized documentation repository for all payroll decisions that grant overtime compensation to exempt status employees.



# Finding – The County's comp time expiration rule is confusing and unnecessary. Item 3.



Employees have 180 days to use leave.

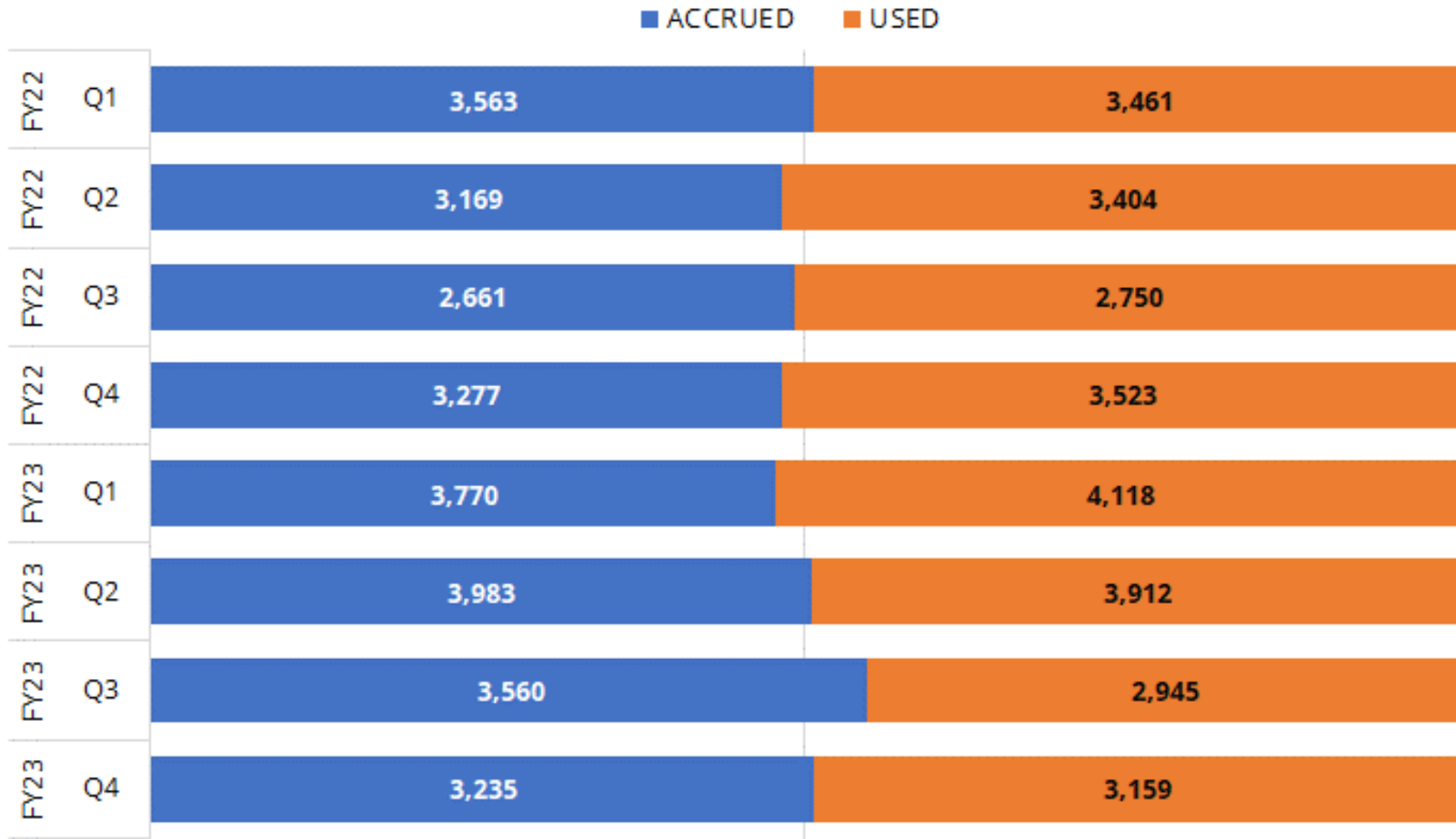


Employees have 50-96 hours balance limitation.

Both serve to limit the liability for the County, but 180-day rule is not being enforced. However, even without enforcement employees are providing stability.



# Comp time usage in balance



Source: County Financial Information





# Recommendation #3

---

The County should determine if the 180-day mandate is still relevant and adjust practices/revise policy based upon the determination.



# Recommendation #4

Lane County issues payouts for:

- Transitions between non-exempt to exempt status
- Transfers between departments

**The County should incorporate policies which include payouts for comp leave balances in cases of departmental transfer or promotion to exempt status.**

- Improves payroll tracking for a leave category no longer applicable.
- Department that approved the leave is responsible for the leave.



Original map copyright 2005 digital-topo-maps.com



# Finding - Leave time granted to part-time employees does not align with the Fair Labor Standards Act definition of comp time.

The County is providing part time staff with the option to apply worked hours over their authorized hours as comp time.

S	M	T	W	Th	F	S
OFF	8 - Reg	8 - Reg	8 - Reg	6 - Reg 2 - Add	4 - Add CT	OFF

Employee authorized for 30 hours per week (.75 FTE)  
 Works 36 hours in the week (no OT)  
 Employee chooses 2 additional hours pay at straight time and 4 hours of comp time leave at a 1:1 rate

*FLSA Comp Time – "...earned at a rate not less than one and one-half hours for each hours of employment for which overtime compensation is required..."*



# Recommendation #5

---

The County should establish and document comprehensive leave options and procedures specifically tailored to part-time employees.



Governance




# System Controls

## NOVAtime issues already reported on:

- 1. Negative balances are required for payroll manual adjustments to leave balances.
- 2. Reporting options limited.
- 3. Test accounts within the live system.
- 4. Records differences between NOVAtime and Munis.

Vacation and Sick Leave #21/22-17 December 2022



Deschutes County,  
Oregon

Recommendations


10

### Vacation and Sick Leave

The Office of County Internal Audit  
David Givans, CPA, CIA – County Internal Auditor  
Aaron Kay – Performance Auditor  
[internal.audit@deschutescounty.gov](mailto:internal.audit@deschutescounty.gov)

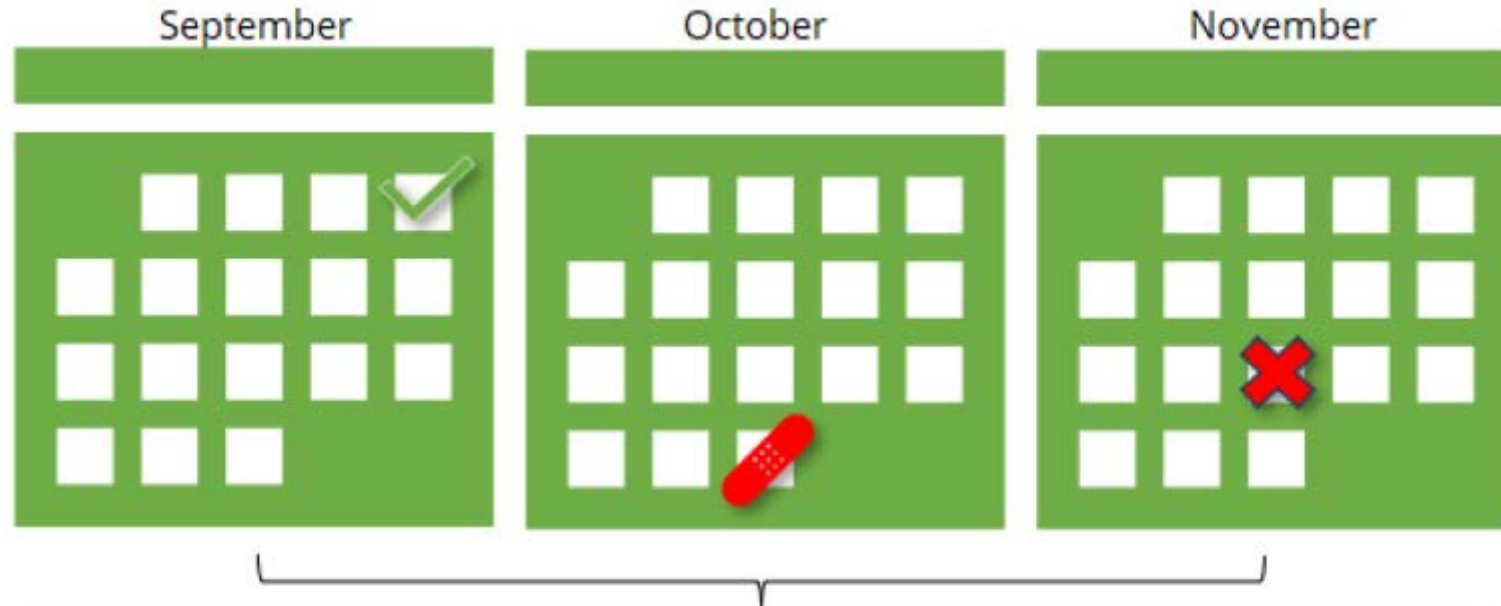
Audit committee:  
Daryl Parrish, Chair - Public Member  
Jodi Burch - Public Member  
Joe Healy - Public Member  
Scott Reich - Public Member  
Summer Sears - Public Member  
Stan Turel - Public Member  
Patti Adair, County Commissioner  
Charles Fadeley, Justice of the Peace  
Lee Randall, Facilities Director

Take survey by clicking [HERE](#)

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# Finding - NOVAtime system controls do not consistently restrict employees from exceeding their accrued comp time leave balance in certain instances.



In this example the employee begins September with 10 hours of leave. In the first week of September, they request to use 8 hours in the third week of November. They mistakenly use 8 hours of comp time at the end of October for an illness. When the approved date in November comes around, the system takes the 8 hours of approved leave even though the employee only has 2 in the leave bank.



# Recommendation #6

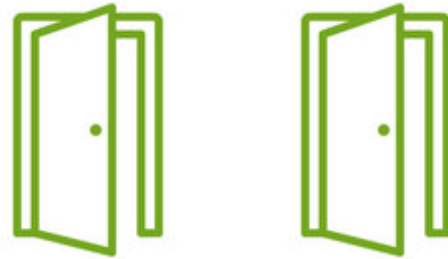
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The Finance Department should develop stronger controls around negative comp time leave balances.



# Finding - Generic user accounts compromise NOVAtime security.

NOVAtime Account



Users sharing ID and passwords



# Recommendation #7

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The Finance Department should assign individual user accounts for each Human Resources staff member needing access to the NOVAtime system.

Transparency  
Accountability



# Finding - Data accuracy issues persist with the presence of former employee accounts in the County's timekeeping system.



NOVAtime Account



Former director

# Recommendation #8

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The Finance Department should remove supervisor-level access for all noted former employees.

Transparency  
Accountability



# Comp time - observation only

CBA/Policy allowances on applying comp time into regular working hours allows for manipulation of the system.

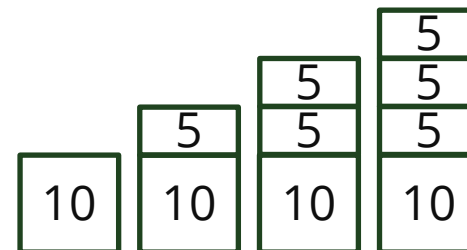
Comp time from comp time hours

S	M	T	W	Th	F	S
OFF	10 - CT	10 -Reg	10 -Reg	10 -Reg	10 - OT	OFF

10 hours of CT used

30 hours worked

Additional 15 hours of CT is accrued



# Comp time - observation only

CBA/Policy allowances on applying comp time into regular working hours allows for manipulation of the system.

Overtime from comp time hours

S	M	T	W	Th	F	S
OFF	12 - CT	12 - CT	12 - CT	12 - CT	OFF	OFF

First 40 hours of CT paid at regular rate

Next 8 hours of CT paid at the scheduled OT rate (1.5x)

CT hours gained at 1.5x rate then compensated at 1.5x rate



# Audit Objectives

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- 1. Does overtime and comp time align with budgeted department costs?
- 2. Does overtime and comp time comply with policies and procedures?
- 3. Does overtime and comp time create disparities across employees?



# Observation

## Gender Identity

	<b>Deschutes County Workforce</b>	<b>% of OT Hours Paid</b>	<b>% of OT Hours Paid w/o DCSO</b>	<b>% of CT Hours Accrued</b>
Women	56.89%	36.57%	54.93%	54.37%
Men	43.04%	63.43%	45.07%	45.63%



# Observation

## Racial Identity

	Deschutes County Workforce	% of OT Hours Paid	% of CT Hours Accrued
White	89%	92%	89%
Non-White	11%	8%	11%





# Observation

## Age

Age Range (years)	Workforce earning OT	% of OT Hours Paid	Workforce accruing CT	% of CT Hours Accrued
20-30	13%	10%	11%	9%
30-40	29%	28%	32%	31%
40-50	28%	30%	28%	30%
50-60	20%	23%	21%	26%
60-70	9%	8%	8%	3%
70-80	0%	0%	1%	1%



# Observation

## Base Pay

Base Rate in \$	Workforce earning OT	% of OT Hours Paid	Workforce accruing CT	% of CT Hours Accrued
10-20	1%	0%	1%	1%
20-30	29%	7%	28%	18%
30-40	41%	41%	48%	57%
40-50	21%	37%	22%	23%
50-60	5%	10%	2%	2%
60-70	2%	3%		
70-80	1%	2%		



# Observation

## Length of Service

Length of Service (years)	Workforce earning OT	% of OT Hours Paid	Workforce accruing CT	% of CT Hours Accrued
0-5	50%	29%	48%	44%
5-10	21%	26%	24%	23%
10-15	8%	12%	8%	11%
15-20	12%	20%	12%	14%
20-25	6%	10%	5%	7%
25-30	2%	3%	2%	2%



# Observation

## CBA

CBA	Deschutes County Workforce	% of OT Hours Paid	% of CT Hours Accrued
911EU	7%	16%	9%
AFSCME	36%	8%	30%
DCSEA	26%	48%	20%
FOPPO	3%	0%	5%
IUOE	12%	8%	26%
NON-REPRESENTED	17%	20%	10%



# Observation

## PERS Tier

PERS	Deschutes County Workforce	% of OT Hours Paid	% of CT Hours Accrued
Tier 1	4%	5%	2%
Tier 2	11%	19%	10%
OPSRP	85%	75%	88%



# Observation

## Job Class Analysis

Top 10 Avg OT hours paid with more than 10 ee's	Top 10 Avg CT hours accrued with more than 10 ee's	Top 10 Avg CT Balances with more than 10 ee's
PUBLIC SAFETY DISPATCHER II	PW EQUIPMENT OPERATOR, HEAVY	PW EQUIPMENT OPERATOR, HEAVY
SERGEANT	PUBLIC SAFETY DISPATCHER II	PUBLIC SAFETY DISPATCHER II
PUBLIC SAFETY DISPATCHER I	PW EQUIPMENT OPERATOR, LIGHT	PW EQUIPMENT OPERATOR, LIGHT
DEPUTY SHERIFF	PUBLIC SAFETY DISPATCHER I	COMMUNITY JUSTICE SPECIALST
MAINTENANCE SPECIALIST II	PAROLE & PROBATION OFFICER	SERGEANT
DEPUTY SHERIFF, CORRECTIONS	MAINTENANCE SPECIALIST II	DEPUTY SHERIFF
LIEUTENANT	COMMUNITY JUSTICE SPECIALST	DEPUTY SHERIFF, CORRECTIONS
PW EQUIPMENT OPERATOR, HEAVY	CODE COMPLIANCE SPECIALIST	PAROLE & PROBATION OFFICER
9-1-1 CALL TAKER	EQUIPMENT MECHANIC	LANDFILL SITE ATTENDANT
LANDFILL SITE ATTENDANT	LANDFILL SITE ATTENDANT	BEHAVIORAL HLTH SPEC I



# Observation

Department	# of FT/PT employees working during FY22/23	# of employees eligible for OT during period	% of employees eligible for OT	# of employees with paid OT	# of employees with CT accrual	# of employees with both OT/CT	Total # of employees working OT	Total Hours of OT worked	% of eligible employees working overtime
911	67	53	79%	27	1	25	53	17,995	100%
Assessor's Office	42	37	88%	2	19	4	25	467	68%
Clerk's Office	14	10	71%	5	2	3	10	182	100%
Community Development	80	52	65%	38	1	10	49	2,070	94%
Community Justice	97	76	78%	9	14	35	58	3,440	76%
County Administration	27	12	44%	1	3	5	9	388	75%
District Attorney's Office	82	41	50%	9	7	18	34	1,045	83%
Facilities	32	26	81%	4	1	14	19	1,349	73%
Fair and Expo Center	12	8	67%	7	0	1	8	2,901	100%
Finance	22	8	36%	3	6	1	10	389	125%
Health Services	503	211	42%	61	49	46	156	3,927	74%
Houselessness	2	1	50%	1	0	0	1	45	100%
Human Resources	10	4	40%	2	1	2	5	426	125%
IT	21	1	5%	1	0	0	1	1	100%
Justice Court	5	3	60%	0	2	1	3	126	100%
Legal Dept	9	2	22%	0	1	1	2	21	100%
Road Department	68	57	84%	6	14	32	52	7,818	91%
Sheriff's Office	256	232	91%	118	6	103	227	68,013	98%
Solid Waste	46	40	87%	16	0	24	40	4,998	100%
Veterans Services	6	5	83%	1	0	3	4	313	80%
<b>TOTALS (AVGS)</b>	1401	879	(63%)	311	127	328	766	115,910	(87%)



# Don't forget to fill out the survey!

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## Questions/ Comments?





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# Thank you





**Recommendations**  
**62**

# 2023 Global Follow-up Report

## Outstanding recommendations – Administration, Clerk’s Office, Fair and Expo, Human Resources, and Finance

**The Office of County Internal Audit:**  
Elizabeth Pape, CIA, CFE – County Internal Auditor  
Aaron Kay – Performance Auditor

**Audit committee:**  
Daryl Parrish, Chair - Public member  
Jodi Burch – Public member  
Joe Healy - Public member  
Kristin Toney – Public member  
Summer Sears – Public member  
Stan Turel - Public member  
Patti Adair, County Commissioner  
Charles Fadeley, Justice of the Peace  
Lee Randall, Facilities Director



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## 2023 Global Follow-up Executive Summary

Since December 2019, the Office of County Internal Audit has released 23 audit reports comprising a total of 190 recommendations, with subsequent follow-ups. This report emphasizes the achievements made thus far and identifies areas requiring further attention. The table below summarizes the current status of those audit reports:

Resolved	Underway	Planned
<b>Fully completed.</b> Auditor will no longer monitor	<b>In Progress.</b> Auditor will continue to monitor.	<b>Agreed to without progress.</b> Auditor will continue to monitor.

Link to Audit Report	Key Follow-up Findings	Status of Recommendations		
		Resolved	Underway	Planned
<a href="#">Treasurer Transition</a>	County investment practices have been improved.	22	0	0
<a href="#">HR - Cash Handling</a>	Improved fiscal controls and operational efficiency.	13	1	0
<a href="#">Juvenile - Cash Handling</a>	Stronger controls for handling customer payments.	4	0	0
<a href="#">Cellular Costs - Verizon</a>	Expected completion in September 2024.	5	3	1
<a href="#">CDD - Cash Handling</a>	Policy revisions need to be completed.	1	1	0
<a href="#">Munis Security and Workflows</a>	Enhanced financial controls have been implemented.	16	2	0
<a href="#">Munis Vendor Master</a>	Improved efficiency and compliance in financial processes.	9	2	1
<a href="#">Munis P-Cards</a>	Written procedures have been documented; further action is necessary.	3	1	3
<a href="#">County Clerk Transition</a>	Progress towards resolution has stalled.	4	1	4
<a href="#">2021 County Fair Ticketing</a>	The County Fair continues to improve as its popularity increases.	14	3	0
<a href="#">Munis Analyses</a>	Enhancing efficiency, accuracy, and compliance in financial processes.	6	2	2

Link to Audit Report	Key Follow-up Findings	Status of Recommendations		
		Resolved	Underway	Planned
<a href="#">Management of Pandemic Case Investigation and Contact Tracing</a>	Temporary labor management needs further improvement.	0	3	2
<a href="#">Adult Parole and Probation – Cash Handling</a>	Streamlining fiscal controls for infrequent client payments.	1	0	0
<a href="#">Administration and Risk – Cash Handling</a>	Optimization of County infrastructure for OLCC permit payments and review.	3	0	0
<a href="#">Assessor's Office – Cash Handling</a>	The Office has stronger fiscal controls and processes.	10	0	0
<a href="#">Initial Cybersecurity Assessment</a>	Cybersecurity is a top priority.	0	2	1
<a href="#">Justice Court – Cash Handling</a>	Improved reconciliation process for external payments.	2	0	0
<a href="#">Sheriff's Office - Cash handling</a>	Continued progress for a stronger control environment.	0	3	0
<a href="#">Vacation and Sick Leave</a>	System data has improved, but policies revisions remain.	5	4	1
<a href="#">Elected District Attorney Transition</a>	Progress has been made improving any future transitions.	4	1	0
<a href="#">Treasurer Transition 2022</a>	Collaborating to define newly elected independent County Treasurer position.	7	0	0
<a href="#">Office of the District Attorney – Cash Handling</a>	Documented processes mitigate the risk of fraudulent activities.	1	0	0

## 1. Introduction

### Audit Authority

The Deschutes County Audit Committee has suggested that follow-ups occur within nine months of the reports. The Audit Committee would like to make sure departments satisfactorily address any prior recommendations that have not been completed at the time of the initial or subsequent follow-ups. The Office of County Internal Audit follows up on all recommendations until resolution. The details of this follow-up and the associated commentary are included at the end of the report in **Appendix A**.

### Background on Audits Issued

This is the fifteenth annual global follow-up looking back at all recommendations included in prior follow-ups. 128 of the 190 recommendations were successfully resolved during the initial follow-up process. Of the remaining 62 open recommendations, 28 have now been resolved for an overall four-year resolution rate of 76.84%.<sup>1</sup> **Appendix C** provides the details of the 23 issued reports over the last four years and the percentage of recommendations resolved in each report. In interpreting recommendation status, Internal Audit may sometimes raise or lower the status provided by the department based on communication received from the department.

## 2. Progress towards resolution

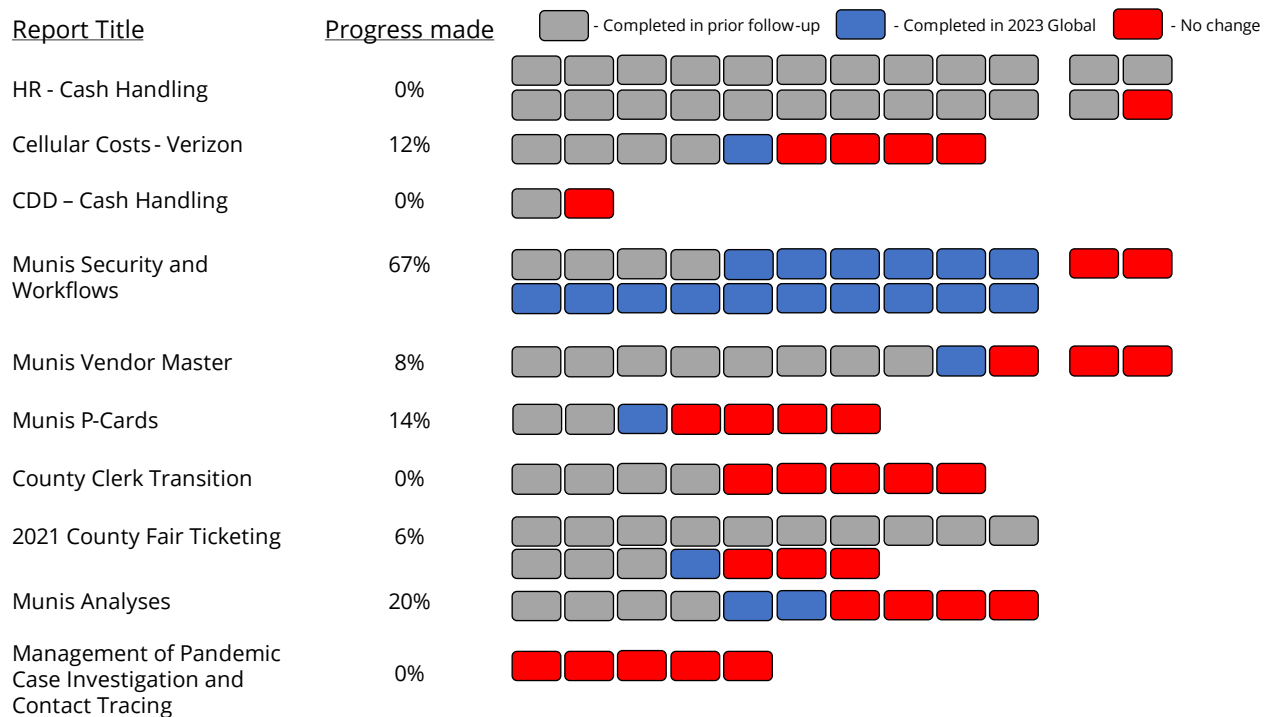
Status updates were requested on 10 of the 23 audit reports with outstanding recommendations including an explanation of the current action plan towards resolution. Each of these reports has undergone at least one follow-up report that was completed more than six months ago, providing ample time for offices and departments to address the recommendations. **Figure I**

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<sup>1</sup> Prior rates were measured at three-year intervals.

illustrates the progress made in implementing the recommendations since the last information request; however, a lack of visible movement does not imply no work has been performed but rather indicates that the matter is not yet fully resolved.

**Figure I** – Percent of resolved recommendation progress between the last follow-up and the 2023 Global Follow-up. Some audit reports saw **no progress** in the percentage of recommendations resolved.



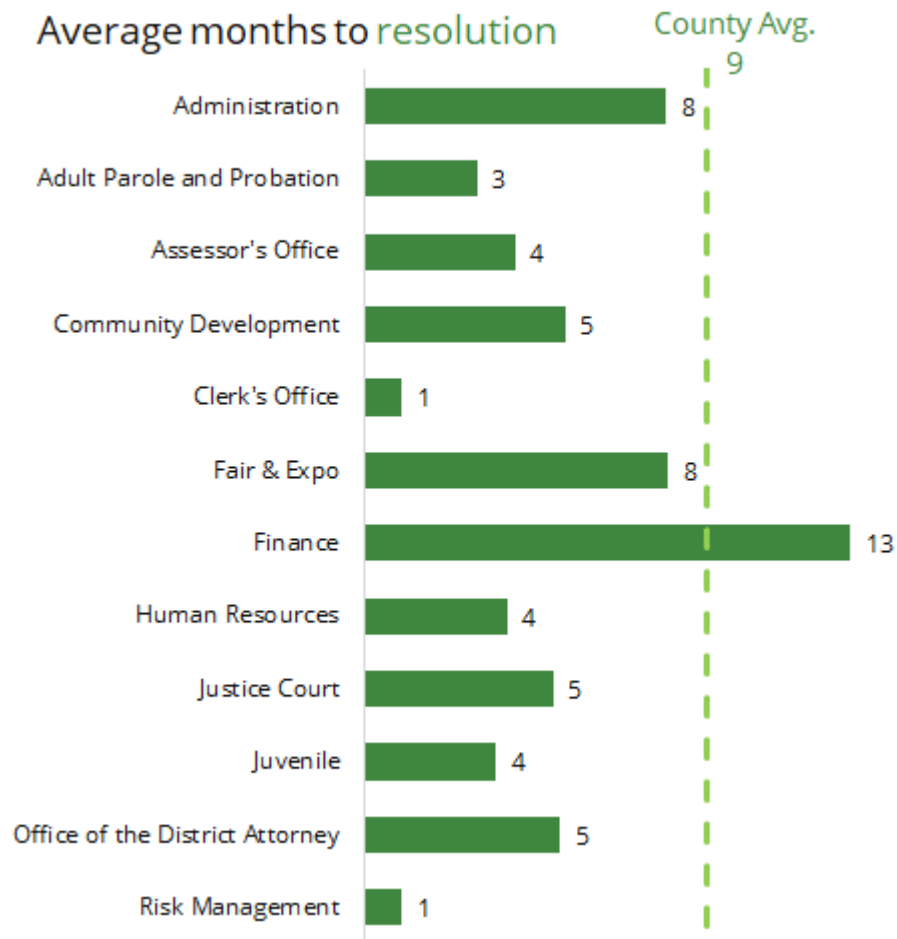
### 3. Duration to resolution

Certain recommendations can be implemented or resolved more swiftly than others. Typically, those pertaining to organizational governance tend to require a more extended timeframe for completion. Internal Audit is monitoring the time it takes offices/departments to address the recommendations. It is noteworthy that, at times, the audited department may not be the primary entity responsible for resolving a given recommendation. A notable example is found in the Administration and Risk Management Cash Handling audit of 2022, where a recommendation was put forth to leverage

electronic systems for liquor license review processing. Despite County Administration being the focus of the audit, the responsibility for resolution fell on the shoulders of the department with an existing electronic permitting system and involvement in the liquor license review process—namely, CDD, which consequently became the process owner. This highlights the nuanced nature of recommendation resolution, where the responsible party may not always align with the subject of the audit.

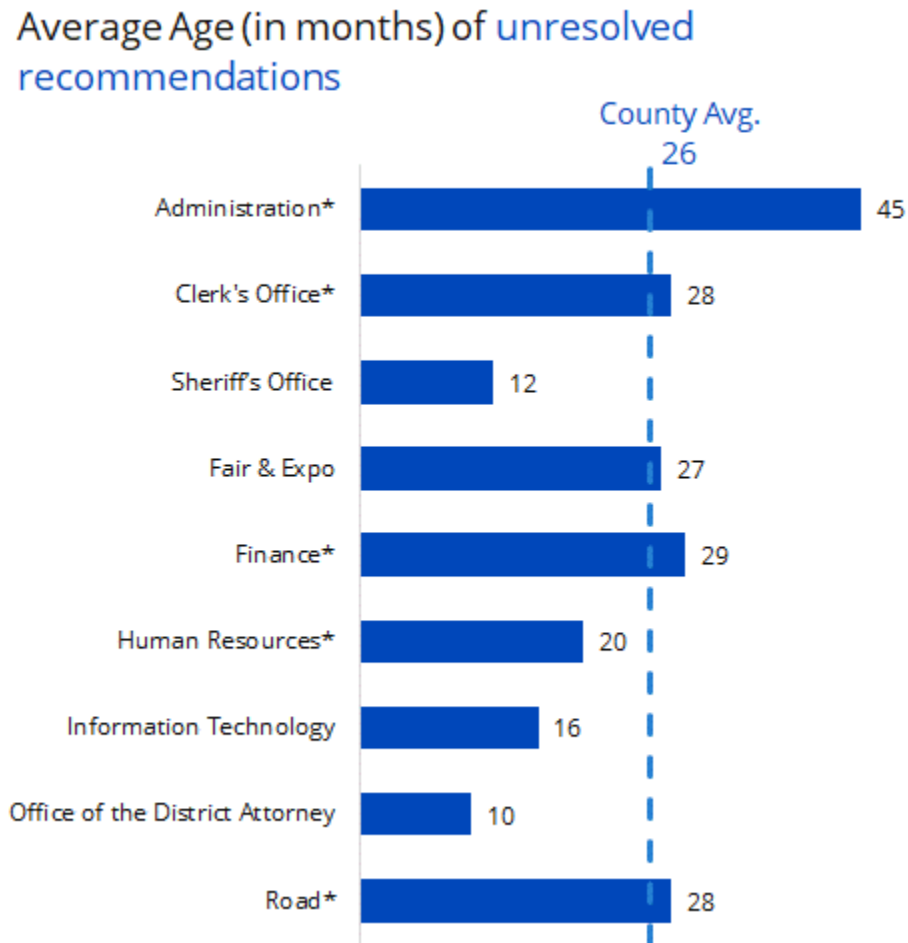
The average months to resolution (9) is markedly lower than the average age in months of unresolved recommendations (26). This indicates that easier to implement recommendations are being addressed quickly while a backlog of recommendations is building.

**Figure II** – Average duration (in months) in took to resolve recommendations.





**Figure III -**  
Average time recommendations have remained outstanding for Deschutes County.



The unresolved items marked with an asterisk (\*) in **Figure III** include recommendations related to contract, policy, or code revision. As previously mentioned, these take longer to complete. A case in point would be the recommendation to the Road Department to amend the County code for noxious weed program information to a more appropriate party than the County Clerk. County code text amendments necessitate thorough legal review and engagement in public meetings for readings and approvals to complete, contributing to the prolonged duration for resolution. Other policy revisions in progress include County Administration collaborating with IT to draft a new policy for mobile device access to County information and HR updating CBA language to reflect current leave practices as those agreements are negotiated. The Finance Department indicated their draft policy revisions are complete and will be forwarded to the newly created Policy Advisory Committee. Refer to **Appendix A** for detailed comments.

## 4. Auditor Highlights

Some recommendations warrant special recognition for successful resolution, length of outstanding status, and high risk.

### Successful Resolution

Implemented recommendations are a chance to highlight improved County practices and areas of decreased risk. These are areas where the County deserves recognition for making operations more effective and efficient.

The Finance Department resolved Munis security and workflow recommendations related to maintaining internal controls. These improvements are vital in preventing fraud, errors, and unauthorized activities within the County's financial operations. Specifically, these recommendations focus on the key principles of segregation of duties, disbursement controls, and regular review of roles and permissions in the Munis system. By implementing and adhering to these foundational principles, the Finance Department aims to enhance the reliability, accuracy, and integrity of its financial operations, ensuring transparency, compliance, and effective risk management. Several of these recommendations were issued before the hiring of the County CFO, Robert Tintle. As illustrated by the progress depicted in **Figure I**, the CFO has actively sought to comprehend the nature of these recommendations and has been working diligently to address them.

### Long outstanding recommendations

Some recommendations are complicated and take longer to implement. This is why auditors track recommendation status for four years. But in some cases, management does not prioritize risk identified by auditors and recommendations languish without attention.

**Figure III** highlighted revisions to policies concerning mobile device access to County information and financial controls have been pending for over three years and should be prioritized by the County. The Policy Advisory Committee, tasked with ensuring

policies are relevant, efficient, and aligned with County objectives, currently has numerous pending policy revisions awaiting review.

Human Resources has not addressed a recommendation related to Munis implementation. The recommendation will increase efficiency and control of receipted transactions but has remained unresolved for over four years. Updated comments from Human Resources Director, Kathleen Hinman, indicate that the adoption of the system into regular duties is currently in progress. These comments can be found in **Appendix A**.

### High risk recommendations

Some recommendations are related to exceptionally high areas of risk. Even though these recommendations have not been open for as long as some other recommendations, they are areas that deserve increased attention from management.

Among the unresolved recommendations, the one posing the highest risk to the organization is the implementation of a comprehensive cybersecurity program. This recommendation emphasizes the establishment of a framework for assessing risks, implementing security controls and procedures, and continuously monitoring their effectiveness. In the current era of increasing cyber threats, an organization's vulnerability to cyber-attacks can have severe consequences, including data breaches, financial losses, and reputational damage. A robust cybersecurity program is crucial to safeguard sensitive information, maintain operational continuity, and protect against evolving cyber threats. Therefore, prioritizing the implementation of a thorough cybersecurity strategy is essential for mitigating substantial risks associated with potential cyber incidents. The County Information Technology Director's, Tania Mahood, said "The hope is to have a framework in place that meets the business needs, provides metrics, process, and procedures in place by (Fiscal Year) 2025." More detailed comments can be found in **Appendix A**.

**5. Appendix A: Updated workplan (status as of December 2023)**

Audit	Recommendation	Updated Status	Updated Comment
HR – Cash Handling	It is recommended for Human Resources to consider using Munis to enter and provide receipts and bill and manage receivables.	Underway	HR met with Finance to learn more about the process. HR staff (newly hired Admin Assistant) will be trained on the process by Tax staff who do this regularly. Additionally, Finance built a query for our use to capture all receipts.
Cellular Costs - Verizon	It is recommended for the County to consider updating the Cell Phone Policy to address management and expectations around utilization. This would include monitoring and routine assessment as to whether an employee truly needs the device/phone, what services, and what plan best fits their intended usage.	Underway	<b>Admin-</b> Draft policy updates are complete and will be shared with departments for their feedback.
Cellular Costs - Verizon	It is recommended for departments to periodically review their cellular plans by line to align them with plan design, device, availability, usage, and cost.	Completed	As indicated in the initial response, Administrator Anderson and Deputy Administrator Kropp followed up with departments under their administrative direction to directly address the cost and efficiency findings noted in the report.
Cellular Costs - Verizon	It is recommended for the County to consider updating policies regarding cellular devices to improve adherence to policy, reduce costs, and reduce risks. The policy improvements should consider addressing: <ul style="list-style-type: none"> <li>• relationship of stipend levels to the cost of cellular phone services to the County;</li> <li>• developing plan selection criteria for business needs aligned with anticipated usage to right size costs;</li> <li>• developing legal and information technology framework to assure that technologies, data, and security are aligned and appropriate given the rise in new technologies and software;</li> </ul>	Underway	<b>Admin-</b> Draft policy updates are complete and will be shared with departments for their feedback.

Audit	Recommendation	Updated Status	Updated Comment
	<ul style="list-style-type: none"> <li>• criteria for selecting between employee phone (stipend) and County owned phone;</li> <li>• monitoring and modification of plan levels (including elimination of devices) for actual usage below anticipated;</li> <li>• utilizing free devices and upgrades to maintain the level of technology as well as getting credits for devices sold back.</li> <li>• establishing when devices require mandatory applications and restrictions from modification for protecting data; and</li> <li>• addressing applicability of policy to non-employee users.</li> </ul>		
Cellular Costs - Verizon	It is recommended the County consider how to address the risks that come with allowing mobile device access or external computer access to internal County information and who and how the risks will be mitigated.	Underway	<b>Admin-</b> Admin is working with IT to develop a standalone policy to address these risks.
Cellular Costs - Verizon	It is recommended the County provided forms for cell phone allowance be updated to reflect any updated policy language.	<b>Planned</b>	<b>Admin-</b> Once the policy is updated, forms will be updated
CDD - Cash Handling	It is recommended the County consider updating fiscal policy to allow Finance the authority to manage increases and decreases in petty cash.	Underway	<b>Finance-</b> Updated policies have been drafted and will be sent to the newly created Policy Advisory Committee.
Munis Security and Workflows	It is recommended for segregation of duties to be considered in the overall design of roles given to users.	<b>Completed</b>	IT has created a query to pull access by user. IT and Finance have established monthly meetings to evaluate current roles. An annual review will be utilized going forward.

Audit	Recommendation	Updated Status	Updated Comment
Munis Security and Workflows	It is recommended Finance segregate significant duties within the system and provide greater guidance on approvals. This might include additional policy and procedural requirements to discourage self-approvals and further describe proper forwarding of approvals.	Completed	Based on how the workflow system is set up, it would be rare if this occurred. Finance performs a monthly review of workflow for requisitions, POs, contracts, and invoices to confirm a transaction has not been self-approved. An official policy is not needed as the system is designed to prevent this from occurring and the proper detective controls have been implemented.
Munis Security and Workflows	It is recommended that periodically IT and Finance join forces to perform a segregation of duties review by user of their assigned permissions. Internal audit can provide guidance on how to carry out this review.	Completed	IT has created a query to pull access by user. IT and Finance have established monthly meetings to evaluate assigned permissions. An annual review will be utilized going forward.
Munis Security and Workflows	It is recommended periodically IT and Finance review the history for the "Munis" roles and make sure that it is not being assigned without reason and that it is not being used to approve any transactions.	Completed	IT has created a query to pull access by user. IT and Finance have established monthly meetings to evaluate current roles. An annual review will be utilized going forward.
Munis Security and Workflows	It is recommended for the procedures for establishing new Munis users be updated to include a provision to include the association with their employee number, if applicable.	Completed	All employees of the County do have an employee number within Munis. However, temporary or contact staff do not have an associated number. IT provides a report to Finance annually identifying the reason for any active user in Munis without an associated employee number.
Munis Security and Workflows	It is recommended for the County Administrator be included in workflow for all disbursements in excess of department limits.	Completed	Finance has determined that there are already compensating controls mitigating risk of unauthorized approvals. Additionally, effective January 1, 2024, signing authority approval limits have increased for department heads to \$50,000, the County Administrator up to \$250,000, and the Board for amounts over \$250,000. This reduces the quantities of approvals over \$50,000 as there are less issues with the higher limits. The County Administrator (CA) is

Audit	Recommendation	Updated Status	Updated Comment
			<p>already set up in workflow for items over \$50,000 (effective 1/1/24), however, as the CFO approves items prior to the County Administrator, if the CA has already physically signed documents, it is unnecessary to forward those items within Munis, thus duplicating approvals. Finance has evaluated the cost/benefit of items going directly to the CA in Munis workflow and has determined it is inefficient when the CA has already signed documents outside of the system and the documentation is attached within Munis.</p>
<p>Munis Security and Workflows</p>	<p>It is recommended the County Administrator (or designee) receive the Finance designed disbursement control reports on at least a monthly basis and review for any anomalies (approvals made without the County Administrator or Board designee). The Information Technology department should assure the monitoring reports are working as designed.</p>	<p>Completed</p>	<p>Workflow approvals for the CFO, County Administrator and Board are currently being reviewed by the Controller, a licensed CPA, who is outside of the approval process at these higher levels. The reports are working as designed.</p>
<p>Munis Security and Workflows</p>	<p>It is recommended the Board of County Commissioners clarify by policy (perhaps in Policy F-15 – Department purchasing thresholds) that the purchasing approval thresholds also apply to all payments being made and excluding certain payments that by statute can be made by the County Treasurer. It would also be a place where they direct whether the County Administrator should review and approve any payments coming to them for approval.</p>	<p>Completed</p>	<p><b>Finance-</b> Policy F-15 was reviewed, updated, and approved by the Board on November 29, 2023. Signing authority limits were updated. The current language was evaluated and considered sufficient as written.</p>

Audit	Recommendation	Updated Status	Updated Comment
Munis Security and Workflows	It is recommended for Finance to work with departments on the rollout of using the purchase card rebate program and who should benefit from the purchase card rebate.	Completed	All departments benefit from revenues associated with the purchase card rebate program. Offsetting revenues received within Finance reduces the internal service charges allocated to departments, thus benefiting all departments proportionally. No need to change the current process.
Munis Security and Workflows	It is recommended for the department considering use of a purchase card to see what payment arrangements can be made with their vendor that maximizes the potential discount on timely payment.	Completed	Finance currently reviews invoices over \$50,000 to determine if there is an option to pay with a purchase card. If the vendor charges a fee to pay via a purchasing card, we do not pay by this method as it would increase costs to the departments. A majority of the vendors we have evaluated charge a processing fee based on the total invoice amount which eliminates the benefit of using a purchasing card.
Munis Security and Workflows	It is recommended for vendors who are to be setup for payment through purchase card be setup from the beginning by the department.	Underway	Finance is evaluating this process.
Munis Security and Workflows	It is recommended for Finance to regularly collect on purchase card rebates and post them to the County accounting records.	Completed	<b>Finance-</b> This is completed annually. The last rebate request was in November 2023.
Munis Security and Workflows	It is recommended for the County to consider some of the workflows they have not been using.	Underway	Finance and IT will review all process codes in January 2024 and annually thereafter.
Munis Security and Workflows	It is recommended for the County to consider and document how they are controlling roles, permissions, and workflows for Munis.	Completed	<b>Finance-</b> The process has been documented.



Audit	Recommendation	Updated Status	Updated Comment
Munis Vendor Master	It is recommended for the County to consider how to implement electronic signatures across County departments and functions based on the associated risks and requirements.	Completed	County purchased centralized electronic signature software, DocuSign. IT is in the process of implementing Countywide.
Munis Vendor Master	It is recommended that Finance and County departments investigate if they are receiving all of the discounts they can get by paying in a timely manner.	Underway	Finance is evaluating this recommendation.
Munis Vendor Master	It is recommended for Finance to work with departments to utilize the discounts field when discounts are available.	Underway	Finance is evaluating this recommendation.
Munis Vendor Master	It is suggested that vendors be evaluated as to whether a better type could be assigned that better reflects the service or product they provide.	Planned	Finance is evaluating this recommendation.
Munis P-Cards	It is recommended Finance update policies and procedures to assure adherence to the delegated purchasing authority. This might include changes to policy, altering P-Card limits, or modifying Munis processing.	Completed	Procedures were formally documented in May 2022. The CFO approves all changes to P-Card limits and new P-Card requests. County RFP for a new p-card program is still planned.
Munis P-Cards	It is recommended for cardholders to enter in invoice/receipt numbers to help prevent duplicate payments.	Underway	Initial tests were performed. Finance is still determining the best solution.
Munis P-Cards	It is recommended the policy clarify whether an employee can have more than one P-Card assigned to them; whether other employees can use the P-Card; and whether non-employees can be provided a P-Card.	Planned	<b>Finance-</b> Procedures were formally documented in May 2022. Policy will be evaluated and updated as necessary after a new procurement professional is hired and issuance of RFP for a new p-card program. The Board approved the new position in June 2023 and the position is expected to be hired in Q1 2024.

Audit	Recommendation	Updated Status	Updated Comment
Munis P-Cards	It is recommended for the policy to address deployment of these high-dollar P-Cards and procedures and controls over their usage.	Planned	<b>Finance-</b> Procedures were formally documented in May 2022. Policy will be evaluated and updated as necessary after a new procurement professional is hired and issuance of RFP for a new p-card program. The Board approved the new position in June 2023 and the position is expected to be hired in Q1 2024.
Munis P-Cards	It is recommended for the County to consider the suggested policy improvements (1-8) in an updated policy and any associated changes to procedures.	Planned	<b>Finance-</b> Procedures were formally documented in May 2022. Policy will be evaluated and updated as necessary after a new procurement professional is hired and issuance of RFP for a new p-card program. The Board approved the new position in June 2023 and the position is expected to be hired in Q1 2024.
County Clerk Transition	It is recommended for the Clerk's Office identify and proceed with developing contracts and contract renewals with significant vendors.	Planned	<b>Clerk-</b> No progress made - refer to prior comments from April 2022: We plan to have all contracts and renewals up to date as soon as possible. Estimated date is difficult to pinpoint as we will be working with vendors.
County Clerk Transition	It is recommended the Clerk's Office enter any contracts into the County financial system as contracts so that effective approvals and contract management can occur.	Planned	<b>Clerk-</b> No progress made - refer to prior comments from April 2022: As contracts are brought up to date, we are intending to enter and track them in Munis.
County Clerk Transition	It is recommended for the County to consider addressing the remaining recommendations from the Office of Homeland Security.	Underway	<b>Clerk-</b> No progress made - refer to prior comments from April 2022: We are taking appropriate steps to address recommendations from Homeland Security. Date of completion is undeterminable at this time.
County Clerk Transition	It is recommended for the Clerk's Office to see if the recording software provider can further improve the audit trail.	Planned	<b>Clerk-</b> No progress made - refer to prior comments from April 2022: A software change will need to be made and the timeframe of this update is currently unknown as enhancements from this vendor are provided in a prioritized order. Date of completion is undeterminable at this time.

Audit	Recommendation	Updated Status	Updated Comment
County Clerk Transition	It is recommended for the County to amend code section 8.35.070(D) to direct the notification responsibilities to a more appropriate party than the County Clerk.	Planned	<b>Clerk-</b> No progress made - refer to prior comments from April 2022: This recommendation is noted and will be incorporated into a future update to Code Section 8.35, which is currently not scheduled in the near term.
2021 County Fair Ticketing	It is recommended for fair management to split out convenience fee revenue and associated ticketing costs to improve transparency of the ticketing technology net cost.	Underway	Fair & Expo will work with the Finance department to create an additional category for the receipt of "ticketing" or "convenience" fees for the 2024 Fair to allow for transparency of ticketing technology expense.
2021 County Fair Ticketing	It is recommended for Fair & Expo management to formalize written procedures over financial areas of the County Fair (including change, gate receipts, and concessions). {The County Internal Auditor created a listing of observed procedures that should help in the creation of procedures.}	Completed	Fair & Expo created written procedures for financial areas of the annual County Fair, including Admission Revenues, change procedures, and Food & Beverage Concessionaire revenues received in advance of the 2023 Fair & Rodeo.
2021 County Fair Ticketing	It is recommended for Finance to develop a change policy (possibly through an amendment to the petty cash policy F-8) to address the requirements for change cash issuance and its accountability.	Underway	<b>Finance-</b> Updated policies have been drafted and will be sent to the newly created Policy Advisory Committee.
2021 County Fair Ticketing	It is recommended for the County to use an expanded contract form for a contractor used for handling monies and include a background check, Legal Counsel review, Risk Management review, and appropriate bonding.	Underway	Fair & Expo will update the specialized contract for any/all contractors who handle cash as part of the admissions process; with input from Legal, and Risk management departments. Fair & Expo has and will continue to require bonding by the admissions coordinator; which began in 2022.
Munis Analyses	It is recommended that Finance develop procedures to review for duplicate invoice payments and, at least annually, perform a duplicate invoice search/review.	Completed	Finance completes this process annually.

Audit	Recommendation	Updated Status	Updated Comment
Munis Analyses	It is recommended for Finance to consider additional training to approvers on batching approvals. This would include setting expectations at various levels in the approval process as well as communicating them in written procedures.	Completed	<b>Finance-</b> Detailed instructions posted in SharePoint (Enterprise ERP Dashboard).
Munis Analyses	It is recommended for Finance to assess, periodically, the usage of bulk approving and the impacts on the purchasing workflow.	Underway	Finance has the documentation on the process and plans to implement Q1 2024. The process will be added to the accounting monthly/quarterly close.
Munis Analyses	It is recommended, with the incidence of some invoices not being entered against a purchase order or contract, that Finance consider whether it would be beneficial to provide departments a tool to reference their purchase orders.	Planned	<b>Finance-</b> The Board approved a new procurement position in June 2023 and the position is expected to be hired in Q1 2024. This will be evaluated after the position is filled.
Munis Analyses	It is recommended for Finance to work with departments to identify and consider setting up routine payments with a purchase order or contract.	Planned	<b>Finance-</b> The Board approved a new procurement position in June 2023 and the position is expected to be hired in Q1 2024. This will be evaluated after the position is filled.
Munis Analyses	It is recommended the County limit usage of its accountable plan payments to employees/volunteers and that other departmental payments should not be paid through the County's accountable plan.	Underway	Finance plans to implement Q1 2024. The process will be added to the accounting monthly/quarterly close.
Management of Pandemic Case Investigation and Contact Tracing	It is recommended for the County to develop a new invitation to bid to cover the newer needs of the County for temporary labor and address the handling of margin and concerns noted above.	Planned	<b>HR-</b> RFP for temporary and agency staffing pushed out for one year due to HR staffing.

Audit	Recommendation	Updated Status	Updated Comment
Management of Pandemic Case Investigation and Contact Tracing	It is recommended the current contract with the primary vendor for temporary labor be extended out 12-18 months until an invitation to bid can be developed and issued.	Underway	<b>HR-</b> Contract to be finalized in January 2024. Most terms have been confirmed, with only a few terms still under review for specialized work.
Management of Pandemic Case Investigation and Contact Tracing	It is recommended for the County to establish more effective leadership and management of the temporary labor contracts and how they are used by County departments. They may want to consider a policy or procedures to address the variety of human resource (HR) issues that come with using a temporary workforce. This would include whether an in-house labor pool could be developed and when departments should consider contracted labor.  Human Resources has indicated they will be taking over efforts to work on the temporary labor RFP/contracts.	<b>Planned</b>	HR will draft guidelines for oversight of temporary and agency workforce management.
Management of Pandemic Case Investigation and Contact Tracing	It is recommended for the County (and Health Services) consider what practices should be employed to provide feedback (formal and informal and to what extent) to contracted temporary staff working for the County.	Underway	HR will include guidance in the upcoming revised employee performance management project.
Management of Pandemic Case Investigation and Contact Tracing	It is recommended for Health Services and the County to consider using more metrics as they manage temporary and remote staffing workloads (for case investigation and contact tracing).	Underway	HR will include guidance in the upcoming revised employee performance management project and the guidelines for oversight of temporary and agency workforce management.

Audit	Recommendation	Updated Status	Updated Comment
<p>Initial Cybersecurity Assessment  (as of May 2023)</p>	<p>It is recommended for the County to implement a cybersecurity program that includes establishing a framework and continuous cycle of activity for assessing risk, developing and implementing effective security controls and procedures, and monitoring the effectiveness of those procedures as noted above.</p>	<p>Underway</p>	<p><b>IT:</b> A fresh approach to the cybersecurity program will be put in place under the guidance of new leadership in the IT department. In the meantime, we are striving to fulfill the CIS controls' IG2 requirements to reduce risks. To aid in this effort, a managed cybersecurity service company was brought on board in January 2023. In partnership with the vendor, an Incident Response Plan will be started in Q2. IT staff from multiple units are working in collaboration with cybersecurity vendors on a weekly basis to accurately identifying and responding to vulnerabilities. These meetings' participants have informally been referred to as the advisory committee. Quarterly vulnerability scanning is being conducted by the vendors in collaboration with the advisory committee. The hope is to have a framework in place that meets the business needs, provides metrics, process, and procedures in place by FY25. <b>Administration:</b> We will support the IT department's continued work to establish a cybersecurity program. Continued funding for this program was included in the FY24 budget . IT will continue to track this work through its performance measures, which should provide consistent progress updates both to the Board and to residents.</p>
<p>Initial Cybersecurity Assessment  (as of May 2023)</p>	<p>It is recommended, at least annually, the Board of County Commissioners review and approve the County's cybersecurity program.</p>	<p>Planned</p>	<p><b>IT:</b> IT will provide current state of the County's cybersecurity posture by summer 2023. A full cybersecurity program report will be provided by FY25. <b>Administration:</b> We agree with this recommendation and will support IT in facilitating this annual check in with the Board.</p>

Audit	Recommendation	Updated Status	Updated Comment
Initial Cybersecurity Assessment  (as of May 2023)	It is recommended for the County, led by the IT Department, continue improvements in addressing cyber defenses.	Underway	<p><b>IT:</b> During the budget planning for FY24, the new IT leadership did not request a full-time employee (FTE). Instead of hiring a dedicated FTE for security, the plan is to use the allocated funding for a managed cybersecurity services company. Although outsourcing has identified many gaps, it alone is not enough. By adding a dedicated resource, we can significantly improve our cybersecurity defenses both proactively and reactively.</p> <p><b>Administration:</b> Administration looks forward to future discussions with the IT Department about potential new FTE that may be needed to meet organizational needs.</p>
Sheriff's Office - Cash handling (as of Sept 2023)	It is recommended the Sheriff's Office strengthen the internal control system to better oversee all payments they receive and periodically assess their operating environment to assure the system is operating as intended.	Underway	<b>DCSO-</b> Recommendation is completed in several guidance areas; work remains in Records and Civil for Munis training.
Sheriff's Office - Cash handling (as of Sept 2023)	It is recommended the Sheriff's Office develop procedures to make more timely deposits.	Underway	<b>DCSO-</b> Recommendation is completed in several guidance areas; work remains in evidence money deposits and electronic transfers.
Sheriff's Office - Cash handling (as of Sept 2023)	It is recommended the Sheriff's Office implement additional control activities through policies and procedures.	Underway	<b>DCSO-</b> Recommendation is completed in several guidance areas; work remains in CODE accounting.
Vacation and Sick Leave (as of Oct 2023)	It is recommended Human Resources and Payroll establish secondary review processes for employee leave balance limit calculations and adjustments.	Planned	<b>Finance</b> - Given the Pay Period Alignment Project and the Tyler/Munis Upgrade Project, this item was deferred until June 2024.

Audit	Recommendation	Updated Status	Updated Comment
Vacation and Sick Leave (as of Oct 2023)	It is recommended the County develop a process to support supervisors in monitor employees' use of vacation leave in compliance with policy.	Underway	<b>HR-</b> The County has a policy covering expectations for employee's use of vacation leave. It is a supervisor's responsibility to hold their employees accountable to all policies, including this one. Human Resources will update the attendance expectations in the employee performance evaluation form to include this review. This will prompt supervisors to review all aspects of an employee's attendance and use of leave with respect to County policies. The performance evaluation update is still in process.
Vacation and Sick Leave (as of Oct 2023)	It is recommended the County revise leave policy HR-16 to be in conformance with State law.	Underway	<b>HR-</b> HR has drafted an Oregon Paid Sick Time (OPST) Policy which will be ready for consideration soon. Additionally, HR will update HR-16 to comply with the OPST law and will present for consideration in coordination with the OPST policy.
Vacation and Sick Leave (as of Oct 2023)	It is recommended the County update policy and CBA contract language to align with practice.	Underway	<b>HR-</b> HR will engage with unions, as each CBA is bargained, to align CBA language with practice. This policy is in draft and underway.
Vacation and Sick Leave (as of Oct 2023)	It is recommended for the County to consider adjustments to the leave cash out policies to further address constructive receipt.	Underway	<b>HR-</b> HR will engage with unions, as each CBA is bargained, to align CBA language with practice. This policy is in draft and underway.
Elected District Attorney Transition (as of Oct 2023)	It is recommended the Elected District Attorney document transitional information for their successor.	Underway	<b>DA-</b> We have successfully compiled an outline of transitional information and are presently in the process of collecting data and making real-time updates as new items arise.



## 6. Appendix B: Objective, Scope, and Methodology

### Objective and Scope



*“Audit objectives”  
define the goals of  
the audit.*

#### Objective:

The objective was to follow up on previously unresolved recommendations.

#### Scope and timing:

This 2023 Global follow-up included all reports issued in the last four years. Those reports with unresolved recommendations that had a follow-up report completed in approximately nine months were subject to a new request for information. Updates to the recommendations outlined in the audit reports presented in **Figure I** have been incorporated into this report and are detailed in **Appendix A**. There are fifty-four (54) recommendations included in this update over ten (10) audit reports.

Status was determined through information provided by offices and departments in December 2023. The original internal reports should be referenced for the full text of recommendations and associated discussion. All internal audit performance reports are published on the County website at

<https://www.deschutes.org/administration/page/internal-audit-reports>.

### Methodology

The follow-up report was developed from information provided by appropriate staff in the associated offices and departments. In cases where recommendations have not been implemented, comments were sought for the reasons why and the timing for addressing these. The follow-ups are, by nature, subjective. In determining the status of recommendations that were followed up, we relied on assertions provided by those involved and did not attempt to independently verify those assertions.

Since no substantive audit work was performed, Government Auditing Standards issued by the Comptroller General of the United States were not followed.

## 7. Appendix C: Audit Reports Issued

Audit Title	Original Report #	Report Issued	# of Original Recommendations	# of Recommendations Outstanding	% Resolved
<a href="#">Treasurer Transition</a>	19/20-1	Dec-19	22	0	100%
<a href="#">HR – Cash Handling</a>	19/20-4	Dec-19	14	1	93%
<a href="#">Juvenile - Cash Handling</a>	19/20-7	Jan-20	4	0	100%
<a href="#">Cellular Costs - Verizon</a>	17/18-5	Mar-20	9	4	56%
<a href="#">CDD - Cash Handling</a>	19/20-10	Jun-20	2	1	50%
<a href="#">Fair and Expo – Trending Costs</a>	19/20-12	Aug-20	16	0	100%
<a href="#">Munis purchasing topics Part I - Security and Workflows</a>	19/20-9	Jan-21	18	2	89%
<a href="#">Munis purchasing topics Part II - Vendor Master</a>	20/21-6	Mar-21	12	3	75%
<a href="#">Munis purchasing topics Part III – P-Cards</a>	20/21-8	May-21	7	4	43%
<a href="#">County Clerk Transition</a>	20/21-11	Jul-21	9	5	44%
<a href="#">2021 County Fair - Ticketing and selected areas</a>	21/22-1	Sep-21	17	3	82%
<a href="#">Munis purchasing topics Part IV - Analyses</a>	20/21-9	Nov-21	10	4	60%
<a href="#">Management of Pandemic Case Investigation and Contact Tracing</a>	21/22-5	Mar-22	5	5	0%

Audit Title	Original Report #	Report Issued	# of Original Recommendations	# of Recommendations Outstanding	% Resolved
<a href="#">Adult Parole and Probation - Cash Handling</a>	21/22-11	May-22	1	0	100%
<a href="#">Administrative Services &amp; Risk - Cash handling</a>	21/22-10	May-22	3	0	100%
<a href="#">Assessor's Office - Cash Handling</a>	21/22-13	Jun-22	10	0	100%
<a href="#">Initial Cybersecurity Assessment</a>	21/22-6	Jul-22	3	3	0%
<a href="#">Justice Court - Cash handling</a>	21/22-15	Sep-22	2	0	100%
<a href="#">Sheriff's Office - Cash handling</a>	21/22-16	Nov-22	3	3	0%
<a href="#">Vacation and Sick Leave</a>	21/22-17	Dec-22	10	5	50%
<a href="#">Elected District Attorney Transition</a>	22/23-4	Jan-23	5	1	80%
<a href="#">Treasurer Transition 2022</a>	21/22-12	Mar-23	7	0	100%
<a href="#">District Attorney's Office - Cash Handling</a>	23/24-4	Sep-23	1	0	100%
<b>Total</b>	<b>23</b>		<b>190</b>	<b>44</b>	<b>76.84%</b>

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Recommendations  
4

# Follow-up Report Personal Information Data Privacy

(Internal Audit report #22/23-2 issued February 2023)

**The Office of County Internal Audit:**  
Elizabeth Pape, CIA, CFE – County Internal Auditor  
Aaron Kay – Performance Auditor

**Audit committee:**  
Daryl Parrish, Chair - Public member  
Jodi Burch – Public member  
Joe Healy - Public member  
Kristin Toney – Public member  
Summer Sears – Public member  
Stan Turel - Public member  
Patti Adair, County Commissioner  
Charles Fadeley, Justice of the Peace  
Lee Randall, Facilities Director



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## 1. Introduction

### Audit Authority

The Deschutes County Audit Committee has suggested that follow-ups occur within nine months of the report. The Audit Committee would like to make sure departments satisfactorily address recommendations.

### Background on Department and Original Audit

This initial assessment of personal information data privacy was to demonstrate a commitment to and thoughtful protection of personal information. Personal information is data that distinguishes an individual, such as full legal name, driver's license, or social security number. Additional risk comes with additional pieces of personal data. Generally, one piece of personal information alone cannot be used to steal a person's identity. It's the various pieces put together that risks compromise of an individual's identity.

Overall, the County demonstrated a strong grasp of data privacy handling and only a couple of areas resulted in recommendations. Staff in departments/offices handling personal information exceed 99% of County staff. The County's departments/offices that deal with HIPAA or law enforcement were unilaterally found to have greater awareness and procedures.

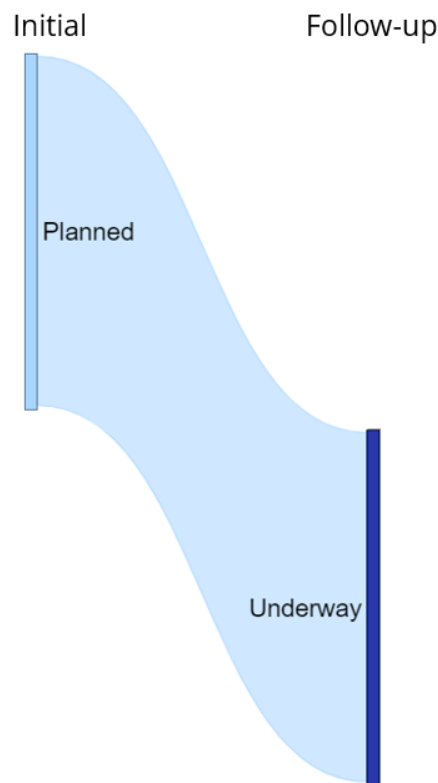
The audit identified the following areas for further improvement, including:

- additional administrative safeguards could help with personal information awareness;
- department/office utilization of technology with personal information could be strengthened;
- some departments/offices retain or collect personal information they do not need; and
- county policy does not reflect update to statute.

## 2. Follow-up Results

The follow-up included four outstanding recommendations agreed to by multiple County departments and offices. **Figure I** provides an overview of the resolution status of the recommendations. The details of the follow-up are included at the end of the report in **Appendix A**. In interpreting the status, Internal Audit may sometimes raise or lower the status provided by the department based on communication received from the department.

**Figure I -**  
How were recommendations resolved?



With this follow-up, none of the outstanding recommendations have been fully addressed. This outcome is not wholly unexpected, given the breadth of the recommendations spanning the entirety of County operations. Many County departments/offices have reported completing portions of the four recommendations, but until an updated policy is approved and a countywide program including a risk assessment process have been established, the status will be considered underway.

**3. Appendix A: Updated workplan (status as of December 2023)**

Recommendation	Status	Estimated Resolution	Updated Comment
<p>It is recommended for the County departments/offices to assign an employee over each department's/office's personal information security program who will also be responsible for establishing appropriate training and compliance with County policy.</p>	<p><b>Underway</b></p>	<p>September-24</p>	<p><b>Admin-</b> After GA-9 is updated and resources are identified, County Administration will begin coordinating with Department Heads to implement this recommendation.</p> <p><b>IT-</b> The IT department has assigned an employee who is responsible for ensuring that the data that IT collects for our business processes is compliant with regulations and training is provided to the IT department. Data that is stored on behalf of departments/offices within IT infrastructure and systems is the responsibility of the respective department/offices.</p> <p><b>911-</b> Our Administrative Manager/Technical Manager will jointly be responsible for this task. We maintain secure records with locking cabinets/offices, and our computers are locked when someone is not at their desk. Our technical and physical safeguards are managed. Between both our Administrative and Technical Manager they can identify internal/external risks and train employees as required in policy GA-9. If training is a requirement county-wide it would be great to have a universal training for employees. Outside of our locked personnel files we do not house store any PHI information elsewhere. Additionally, staff must be certified biannually in information security best practices as a requirement to access CJIS and LEDS. If/when the policy is updated we will review and make necessary adjustments pertaining to the policy.</p>



Recommendation	Status	Estimated Resolution	Updated Comment
<p>It is recommended for departments/offices to consider the risks and develop and/or deploy technology appropriate to the situation for communicating and sharing personal information.</p>	<p><b>Underway</b></p>	<p>June-24</p>	<p><b>Admin-</b> County Administration is currently working with IT to identify tools and resources to assist departments with implementation.</p> <p><b>IT-</b> We have successfully partnered with many departments on safeguards related to transferring personal information via Secure File Transfer Protocol (FTP) and have created documented processes that can be shared and adapted for use by other teams. What has not been created or communicated is where not to share PII data. Today, the County's shared drive is secure at the business unit level. IT is currently responsibly for defining security permissions for the department's top level shared drive based on HR's input to IT which includes people who have been hired or terminated. IT recommends that the departments maintain this level of security and perform auditing, if needed. Departments can work with IT to develop reporting so that managers can periodically monitor permissions of shared drives.</p> <p><b>911-</b> After discussion with amongst our Leadership Team it was determined that we do not have the need to send encrypted emails since we do not send PHI or other confidential information via email. However, we did train all the admin staff on how to turn encryption on in their email if we deem it necessary. In a circumstance where there is a question on if it needs to be turned on the employee will reach out to County Legal for direction.</p> <p><b>Finance-</b> Completed. Staff training occurred in February 2023 and access to files and servers was verified with IT to</p>

Recommendation	Status	Estimated Resolution	Updated Comment
			limited Finance personnel or those with necessary business needs.
It is recommended County departments/offices consider whether they are following policies and could reduce the amount of personal information they collect or retain and make changes to associated processes.	<b>Underway</b>	June-24	<b>Admin-</b> County Administration is currently working with IT to identify tools and resources to assist departments with implementation. <b>IT-</b> We agree with this recommendation and can support departments/offices with finding technical solutions, if necessary.
It is recommended the County update policy GA-9 to reflect the substantive changes from the revised Oregon Consumer Information Protection Act.	<b>Underway</b>	February-24	<b>Admin-</b> County Administration is currently updating GA-9.

## 4. Appendix B: Objective, Scope, and Methodology

### Objective and Scope



*“Audit objectives”  
define the goals of  
the audit.*

#### Objective:

The objective was to follow up on recommendations from the original audit.

#### Scope and timing:

The follow-up included four recommendations from the internal audit report for [Personal Information Data Privacy #22/23-2](#) issued in February 2023. The original internal audit report should be referenced for the full text of the recommendations and associated discussion. The follow-up reflects the status as of December 2023.

### Methodology

The follow-up report was developed from information provided by Whitney Hale, Deputy County Administrator, Tania Mahood, County Information Technology Director, Robert Tintle, County Chief Financial Officer, and Sara Crosswhite, 9-1-1 Director.

Follow-ups are, by nature, subjective. In determining the status of recommendations that were followed up, we relied on assertions provided by those involved and did not attempt to independently verify those assertions. The updates received were included in **Appendix A**.

Since no substantive audit work was performed, Government Auditing Standards issued by the Comptroller General of the United States were not followed.

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**Recommendations**  
**8**

# Overtime and Compensatory Time: Enhanced oversight will improve transparency.

**The Office of County Internal Audit:**

Elizabeth Pape, CIA, CFE – County Internal Auditor  
Aaron Kay – Performance Auditor

**Take survey by clicking here**

**Audit committee:**

Daryl Parrish, Chair - Public member  
Jodi Burch – Public member  
Joe Healy - Public member  
Kristin Toney – Public member  
Summer Sears – Public member  
Stan Turel - Public member  
Patti Adair, County Commissioner  
Charles Fadeley, Justice of the Peace  
Lee Randall, Facilities Director



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## Highlights:

### Why this audit was performed:

Due to time constraints during the Vacation and Sick Leave audit, a comprehensive review of compensatory time was deferred. Given its direct association with compensatory time, the decision to include overtime into the overall review was apparent.

### What was recommended:

The County should improve the transparency of overtime spending and compensation decisions.

The County's policy on overtime and compensatory time should be updated to reflect current practice.

The Finance Department should ensure the timekeeping system is kept up to date and secure.

## Overtime and Compensatory Time: Enhanced oversight will improve transparency.

### What was found:

Deschutes County overtime expenses surged over 30% in Fiscal Year 2023 outpacing increases in overall personnel costs. As the County increasingly depends on overtime to maintain the delivery of quality services, the need for a strong control foundation becomes more crucial. The review focused on systemic and policy-related controls for both overtime and compensatory time. Audit findings are summarized below:

**Overtime reporting.** The Board receives monthly financial reports updating them on the current state of major County funds. Emphasizing vacancy savings is common in personnel cost discussions; however, incorporating overtime expenses into the conversation would provide greater transparency and accountability.

**Overtime documentation practices.** For over a decade, employees who are typically exempt from overtime have been receiving overtime compensation. Centralizing the documentation supporting these decisions would optimize their accessibility.

**County policy.** The County policy on overtime and compensatory time includes a 180-day compensatory time mandate that is not enforced. Furthermore, including compensatory time in the calculation of regular hours in an employee's workweek creates opportunities for limited exploitation of the overtime system. Revisions are needed to clarify expectations for both management and employees.

**System management.** County timekeeping system controls and security measures can be improved to ensure intended functionality.

## 1. Introduction

### Audit Authority

The Deschutes County Audit Committee authorized the review of overtime and compensatory time in the Internal Audit Work Plan for 2022-2023. Audit objectives, scope, and methodology can be found in **Appendix A**.

## Background on Overtime and Compensatory Time

### What is overtime?

Overtime simply means the extra hours eligible employees work beyond their standard 40-hour workweek. During overtime, federal law requires employers to pay higher rates than they do for their regular hours. The County uses overtime when employees are needed to meet increased workloads, deadlines, emergencies, or other demands. One example would be the Road Department mobilizing resources to clear roads of snow and ice when winter weather unexpectedly hits. Those hours are often overtime above their standard workweek. Overtime is also often used to cover vacancy-related operational demands created through employee separations, vacations, or illness.

### What are the benefits of overtime and some of the risks?

Overtime can provide several benefits for an organization, including increased production and the ability to meet tight deadlines or unexpected spikes in workload. It allows the County to capitalize on employees' expertise and dedication beyond regular working hours, fostering a culture of commitment and flexibility. Moreover, overtime can be a cost-effective solution compared to hiring additional staff, especially for short-term projects. However, regular reliance on overtime carries inherent risks.

Extended work hours can lead to employee burnout, reduced job satisfaction, and a decline in overall well-being. This, in turn, may result in higher turnover rates and increased healthcare costs for the organization. Furthermore, prolonged periods of overtime



can negatively impact work-life balance, diminishing creativity and long-term productivity. Striking a balance between leveraging overtime strategically and safeguarding employee well-being is crucial for organizations aiming to optimize their workforce and maintain a healthy organizational culture.

### **How is overtime paid by the County?**

The Fair Labor Standards Act (Act) governs the use of overtime. Under the Act, employers may provide a higher rate of pay than simply 1.5 times base pay for overtime. Deschutes County uses a higher, blended overtime rate that includes the employee's base pay and various additional wages like longevity pay, professional certification stipends, or lead pay. The County last updated its policy regarding overtime in 2007 to comply with changes in State and Federal Laws. The County also negotiates the operation of overtime through collective bargaining between the County and various labor union representatives. Elected officials and County department directors must adhere to overtime contract provisions and relevant Human Resource policies.

### **What is compensatory time?**

Compensatory time, often referred to as "comp time," is a leave benefit offered to employees of a public agency in place of receiving overtime pay to be used at a future date. The Fair Labor Standards Act also governs comp time. Employees earn comp time at a rate of 1.5 times the number of overtime hours worked. For instance, if an employee works 10 hours of overtime, they accumulate 15 hours of time off as comp time leave. The conversion of overtime hours to comp time leave must be mutually agreed upon by both the employee and the office/department in which they work.

### **Who is eligible for overtime and comp time?**

The Fair Labor Standards Act classifies employees into two categories: Exempt and Non-Exempt. Exempt employees usually have salaried positions in executive, administrative, supervisory, or professional roles and don't receive overtime pay. Non-exempt

employees are typically paid hourly and are entitled to overtime pay when they work more than 40 hours in a workweek. There are exceptions within the Act for certain essential workers like police, firefighters, paramedics, and other first responders who are entitled to overtime for public safety regardless of category. The State of Oregon also has additional exceptions for corrections staff. The County Human Resources Department (HR) ensures that each job position is properly classified according to the Act's regulations.

### **How is overtime and comp time tracked?**

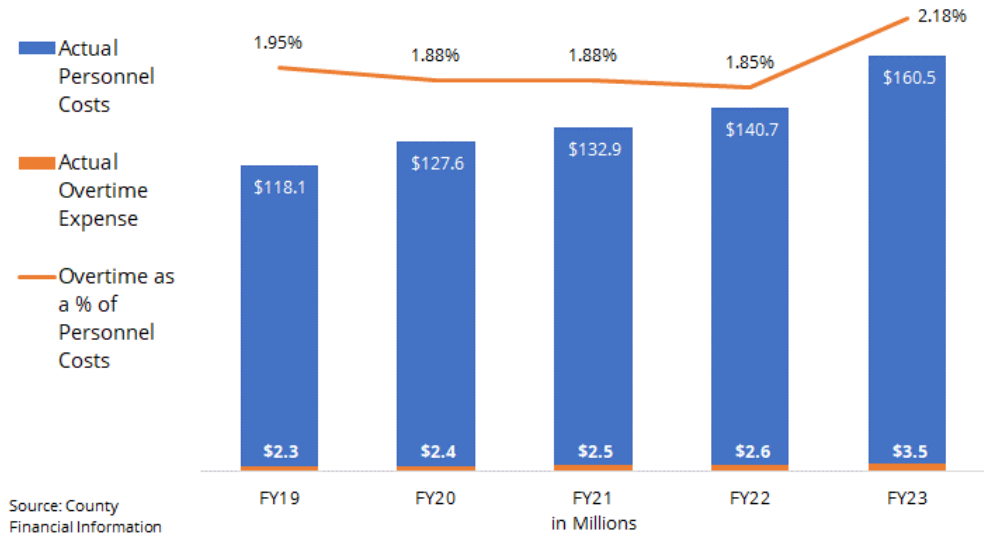
The County uses NOVAtime Time Management Online (NOVAtime) for its employee timekeeping and time management system. Employees are responsible for recording all hours worked, including any overtime, requesting conversion of overtime hours into comp time leave, and requesting comp time leave usage in the system. Department heads and supervisors are responsible for approving timesheets, comp time conversions, and comp time leave usage. Overtime expenses are recorded and monitored within County governmental funds through the County's financial system, Tyler ERP (previously known as MUNIS). Meanwhile, expenses related to compensatory time off are consolidated alongside expenditures from other employee leave options, such as Time Management Leave or Vacation Leave, in Tyler ERP.

## **Financial Background**

### Overtime Expenses

Overall personnel costs have risen each year as the County workforce expands, employees gain higher wage steps, and cost-of-living increases are negotiated and approved. Overtime expenses historically represent around 2% of overall personnel costs.

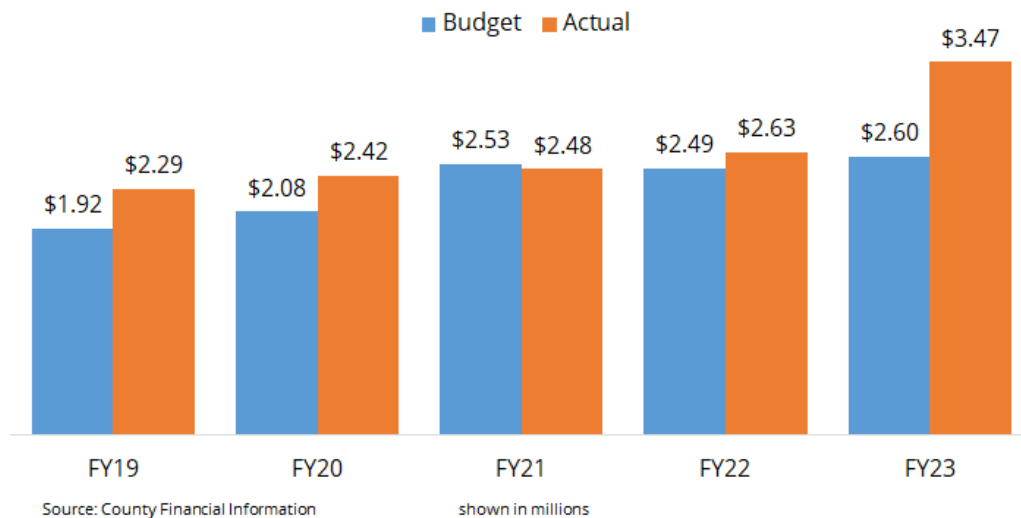
**Figure I**  
The growing cost of personnel and overtime for the County over the last five fiscal years. (FY19-23 Budget to Actual)



Overtime Budgeting

Overtime spending has eclipsed budgeted amounts in four of the last five fiscal years, usually by a narrow margin. Fiscal Year 2023 saw an estimated 32% increase in overtime expenses over the previous fiscal year. The Fiscal Year 2024 budget approval resulted in an increase in allocated overtime spending, now set at \$2.88 million.

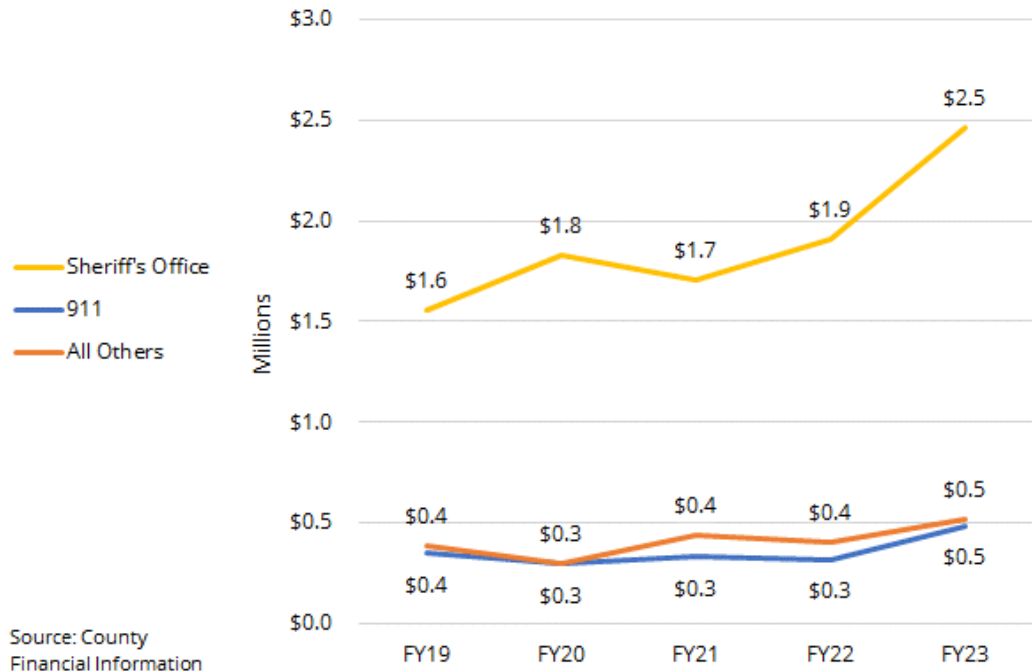
**Figure II**  
Fiscal Year 2023 had the largest discrepancy between budget and actual overtime expenses in the last five fiscal years. (FY19-23 Budget to Actual)



Departmental Spending

Within the estimated \$3.5 million spent on overtime in Fiscal Year 2023, the Sheriff’s Office had the highest overtime expense. The reasons for Sheriff's Office overtime hours differ among divisions.

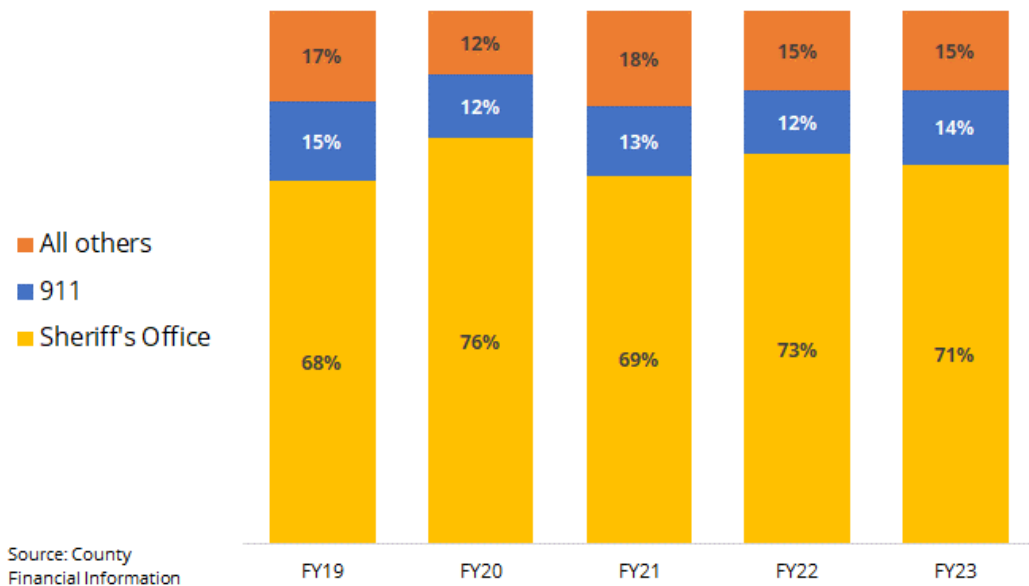
**Figure III**  
Over the last five fiscal years, the Sheriff's Office has the highest overtime expense for the County. (FY19-23 Actual)



For example, corrections deputies are more likely to work overtime for an entire shift covering for vacancies. Patrol deputies typically work overtime between 1 to 2 hours in duration, usually covering calls for service or emergency situations near the end of their regular shift.

In contrast to the upward trend seen in **Figure III**, when compared to the overall overtime expenses incurred by the County over the last five years, the Sheriff's Office's percentage of the expenses were lower in FY23 when compared to prior FY.

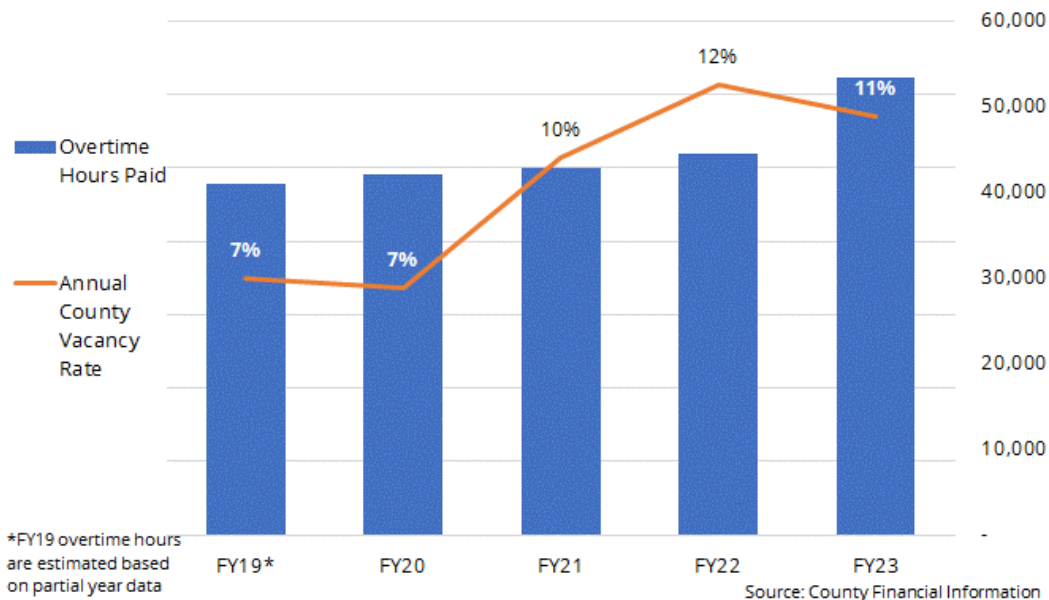
**Figure IV**  
As a percentage of the overall overtime expense for the County, the Sheriff's Office expenses are relatively flat. (FY19-23 Actual)



The Impact of Vacancies

As previously mentioned, overtime is often used to cover vacancies. Health Services, the Sheriff's Office, and 9-1-1 have all faced staffing shortages in recent years, while addressing an increase in service provision and emergency situations.

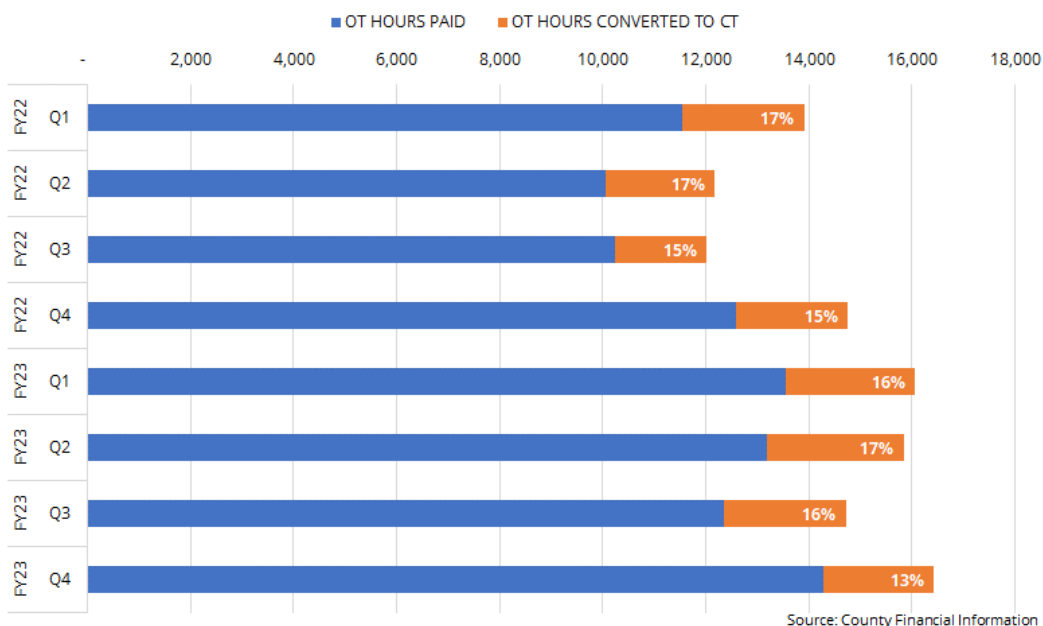
**Figure V**  
Higher vacancy rates seen over the last three fiscal years correlate into increased overtime hours.



Comp Time Costs

The County doesn't look at comp time costs in the same way as overtime expenses because comp time costs get combined with other types of employee leave, such as time management leave

**Figure VI**  
Employees converted overtime hours worked into comp time leave about 16% of the time over the last two fiscal years.

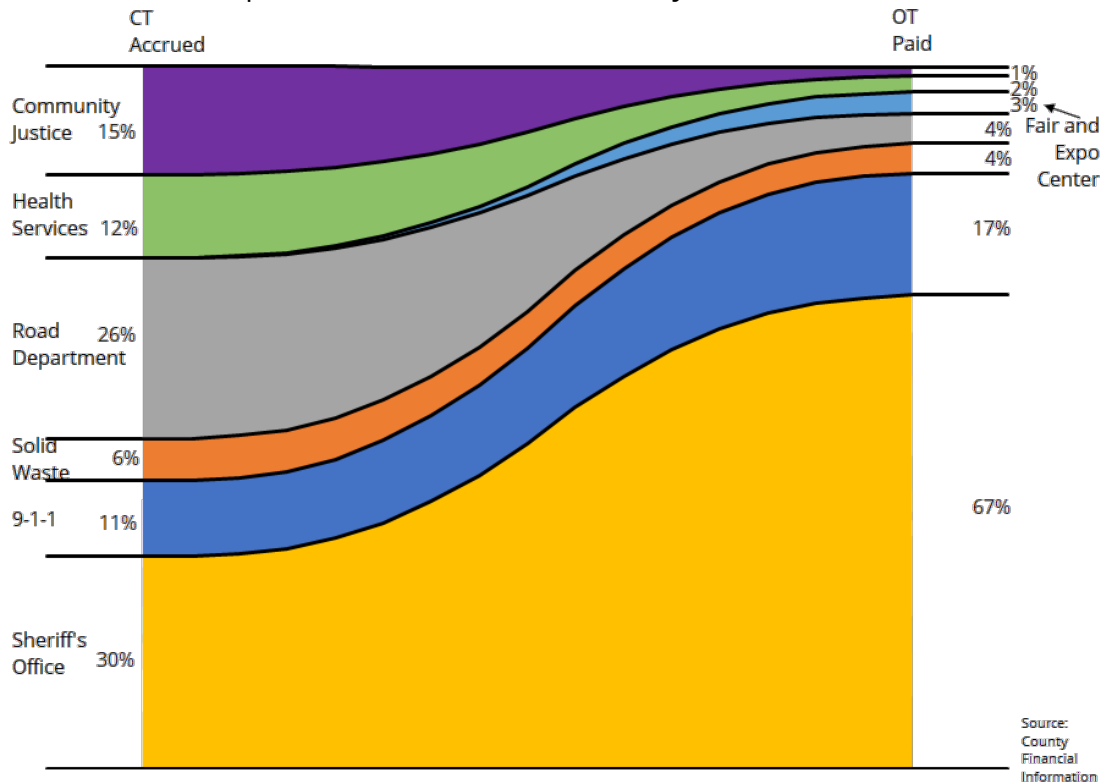


and vacation leave. The Fair Labor Standards Act imposes restrictions on comp time leave, placing maximum accrual limits that mitigate the risk of substantial liabilities, thereby making it less critical to actively monitor its costs. For Deschutes County, overtime hours worked are more apt to be compensated as overtime pay rather than converted into comp time leave.

A County office or department’s operation significantly influences the choice available to employees regarding compensation for overtime or conversion to comp time leave. For instance, at the Fair and Expo Center, overtime work occurs from events directly tied to revenues, making it practical for the department to opt for overtime compensation rather than incurring deferred comp time leave costs. In contrast, the Road Department experiences peak overtime activity during the summer and winter seasons, affording the flexibility to grant employees leave when service demand is relatively lower in the spring and fall. Some offices or departments, like Solid Waste, are able to strike a balance between overtime and comp time.

**Figure VII**

Distribution of overtime hours for the largest overtime departments indicating the preferences of each office/department for the last two fiscal years.



## 2. Findings

Government waste is frequently attributed to overtime spending by the media, and often with good reason. Cases of overtime falsification and gross overspending by government agencies have been reported outside of Deschutes County. Given the recent increase in overtime expenses and sustained double digit vacancy rate, it is important for the County to have robust controls around overtime and compensatory time to ensure the system is working as intended. The findings highlight the need for enhancing oversight and transparency across various control areas to bolster existing systems.

This audit specifically focuses on a County-wide evaluation of electronic timekeeping system controls and policy-level mechanisms related to overtime and compensatory time. It does not delve into individual employee compensation details, decisions made by employees or management, the appropriateness of specific instances of overtime worked, or the quality of duties performed during overtime hours. The findings and recommendations provided are centered solely on the systemic and policy-related aspects of overtime and comp time administration within the scope of the audit. Any considerations beyond this scope should be addressed through separate and specific inquiries.

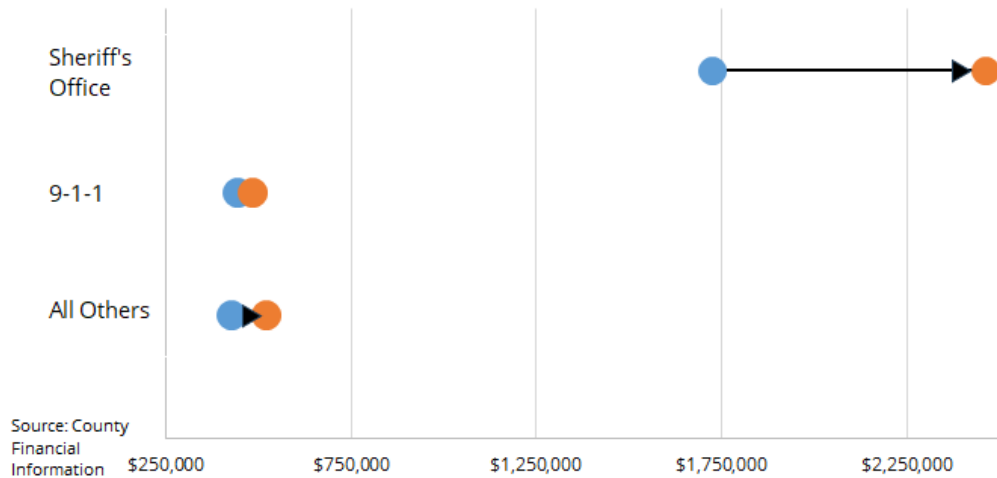
### Budgeting Overtime Expense

#### **Inadequate budgeting for overtime expenses is obscured within overall personnel costs.**

As seen in **Figure II**, Until Fiscal Year 2023, the County closely matched budgeted and actual overtime expenses. Fiscal Year 2023 was significantly different, with an estimated overspend of \$870,000. Given the significant influence the Sheriff's Office has toward the County's overtime budget coupled with the emergency nature of their responsibilities, it is no surprise that 84% of the discrepancy is attributable to the Sheriff's Office.

**Figure VIII**

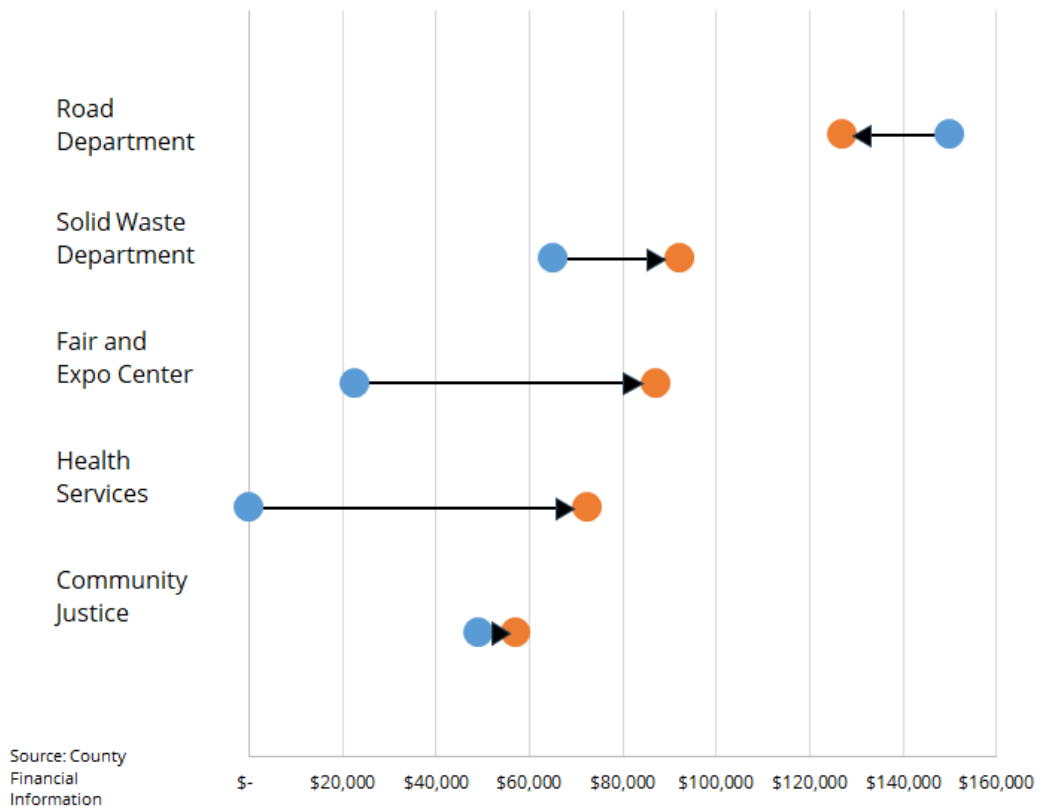
The Sheriff's Office overspent their budgeted overtime expenses by an estimated \$737,000. (FY23 Budget to Actual)



However, the Sheriff's Office is not alone in underestimating budgetary expenses. Among departments with overtime costs exceeding \$50,000 in Fiscal Year 2023, Solid Waste, Health Services, and the Fair and Expo Center combined to fall \$164,000 short in estimating their overtime expenses, while 9-1-1, Road Department, and Community Justice more precisely anticipated theirs.

**Figure IX**

Department overtime spending ranged from 15% underbudget to 288% overbudget. (FY23 Budget to Actual)



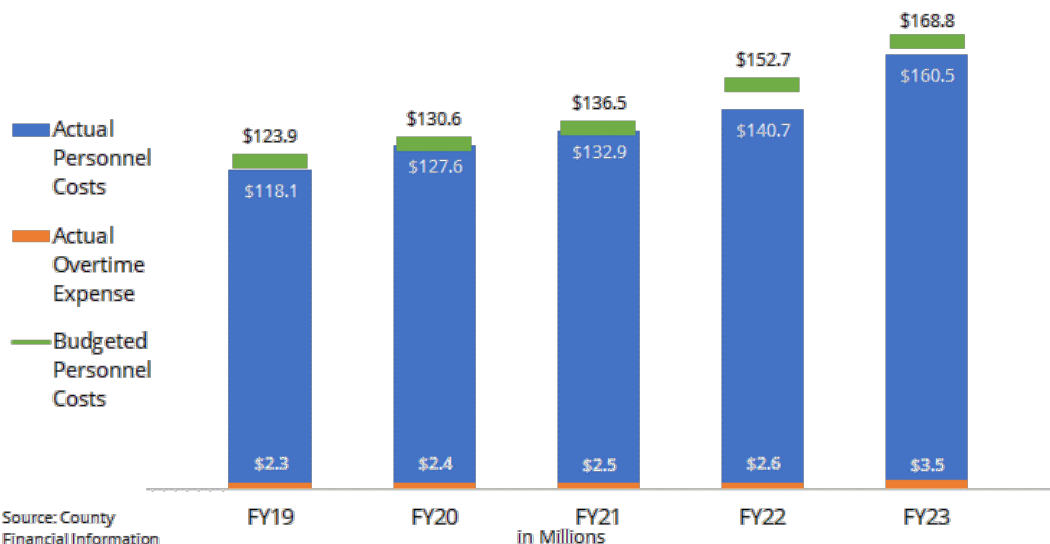


For Deschutes County, the annual budget cycle commences with the formulation of budget objectives and operating budget requests. In their operating budget requests, each office/department includes anticipated overtime expenses as part of their overall or rolled-up personnel costs. The Budget Office examines these rolled-up personnel costs, relying on historical averages and future cost assumptions, before presenting them to the Budget Committee for in-depth discussions.

Following the approval of the proposed budgets, the Board of County Commissioners receives monthly financial reports. These reports assess the actual spending of offices/departments in comparison to the budgeted amounts. The financial reports serve as a means to keep both policymakers and management informed about governmental fund performance, accountability, and potential savings. Both the budgeting process and expenditure monitoring serve as internal controls to ensure responsible and efficient spending by the County.

As previously mentioned, overtime expenses often stir controversy, with the media employing attention-grabbing terms such as "runaway spending" and "robbery" to characterize them. This framing can influence public opinion, fostering the perception that overtime is a manifestation of government waste. However, unforeseen overtime costs can often be mitigated through salary or vacancy savings. Considering the relatively small

**Figure I enhanced**  
 The County's personnel costs have stayed under budget despite the growing cost of personnel and overtime for the County over the last five fiscal years. (FY19-23 Budget to Actual)



percentage that overtime expenses constitute in the overall personnel costs, it is improbable for overtime alone to emerge as a primary factor contributing to financial instability for the County.

The Budget Office relies on office/department expertise when submitting budgeted numbers, but they can play a role in providing information the Board needs for providing oversight and accountability in overtime budgeting. The monthly financial reports present rolled-up personnel costs, potentially lacking the necessary detail for accurate transparency and oversight of overtime spending. Often these reports will include the amount of vacancy savings within projected personnel costs, but not mention overtime expense.

#### **Recommendation #1**

***The Finance Department monthly financial reports should include overtime expenses for major funds when the projected personnel services requirements exceed budgeted levels.***

### **Overtime paid to exempt employees**

#### **Insufficient documentation regarding premium pay decisions hinders transparency.**

Under the Fair Labor Standards Act, there are few exceptions to the overtime exempt classification. However, the County has been providing overtime opportunities to exempt employees in the 9-1-1 department for over a decade. County staff have not maintained documentation supporting these decisions in the County's personnel or payroll records; instead, it is kept within the records of the 9-1-1 department.

According to the Act, employers are required to keep such records secure and accessible, typically within a central record keeping office like County Human Resources or Payroll.

The availability of proper documentation for these overtime decisions potentially raises concerns about fairness and

preferential treatment. Moreover, keeping these records within the department limits accessibility for other County departments and employees.

Any records of the approval of additional compensation, even for temporary situations, should be treated in accordance with the Fair Labor Standards Act. It's important to note that the practice of exempt 9-1-1 employees earning overtime was initially negotiated in 2005 as a temporary solution to address persistent staffing issues. This was implemented as a stop-gap measure, incentivizing exempt employees to take on additional public safety dispatching shifts alongside their regular duties. The County is now considering extending additional compensation to exempt employees with expertise in information technology to address cybersecurity program needs in a timely manner rather than using temporary staffing or other tools to address this temporary increase in workload.

### ***Recommendation #2***

***The County should establish a centralized documentation repository for all payroll decisions that grant overtime compensation to exempt status employees.***

## **County overtime and comp time policy**

**The County's comp time expiration rule is confusing and unnecessary.**

County policy mandates that employees use comp time hours within 180 days after the overtime was earned for some employees, however this language in the policy has not been enforced. County policy and the various labor union agreements also limit overall comp time leave balances for each employee, ranging between 50-96 hours, which is enforced.

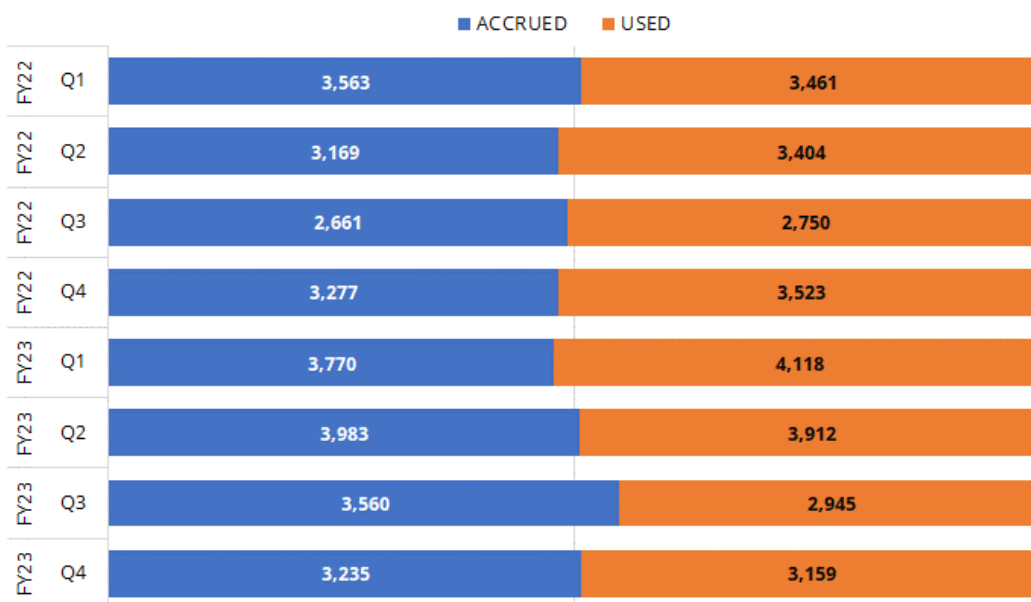
The Federal Government Accountability Office (GAO) urges management to periodically review policies for continued

relevance and effectiveness. The County policy on overtime compensation and compensatory time, HR-4, was last revised in 2007. The American Federation of State, County, and Municipal Employees' agreement refers to HR-4 as a governing document applying the same rule to all employees represented under that contract.

The County creates confusion when it does not follow its own policy. Not enforcing policies can also lead to an erosion of trust between the employer and employee.

Despite not enforcing the expiration time, County employees are using comp time as fast as they accrue it. Expiring time limits are one method in which organizations prevent leave balances from turning into a significant liability. However, leave balance limits also serve a similar purpose. The balance limits act as an incentive for employees to utilize their leave, allowing them to convert future overtime hours worked into time off. Once comp time leave banks reach capacity, the employee is left with no other option than to receive overtime pay for overtime hours worked. Consider the previous scenario involving a Road Department employee who worked the weekend plowing snow and ice. This employee, keen on maintaining a work-life balance, chooses to convert the overtime worked into time off for a fall hunting trip.

**Figure X**  
County employees are using comp time as fast as they accrue it.



Source: County Financial Information

By strategically replenishing their leave bank and using comp time for personal pursuits like hunting, employees create a balanced system while limiting the overall liability to the County.

**Recommendation #3**

***The County should determine if the 180-day mandate is still relevant and adjust practices/revise policy based upon the determination.***

To enhance the administration of comp leave, the County policy could benefit from further refinements. Currently, Lane County opts to issue a payout for all comp time leave balance hours when an employee transitions from a non-exempt to an exempt role. This payout serves to alleviate the burden on payroll by eliminating the need to track and issue payments from a leave category that is no longer eligible for accrual.

Additionally, Lane County extends payouts when an employee undergoes a departmental transfer. Comp time, originally approved as a liability by the department that authorized the overtime, becomes a challenge when an employee moves to a different department. The receiving department is then compelled to acknowledge leave hours they did not initially authorize.

These adjustments in practice would align with payouts of comp time hours for employees that are separating employment with the County.

**Recommendation #4**

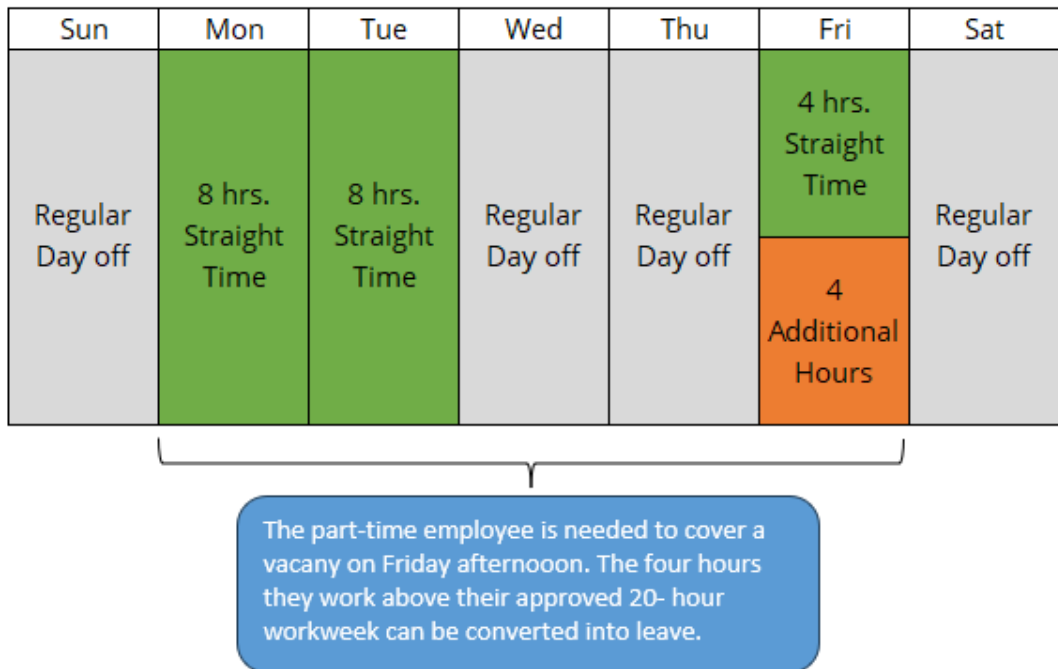
***The County should incorporate policies which include payouts for comp leave balances in cases of departmental transfer or promotion to exempt status.***

**Leave time granted to part-time employees does not align with the Fair Labor Standards Act definition of comp time.**

Part-time employees currently accrue leave at an hour-for-hour rate when exceeding their authorized weekly hours, and this leave is classified as comp time within the Novatime system, despite not being earned through overtime work. The County lacks a policy to support or regulate this practice.

Auditor created example of a part-time employee workweek.

**Figure XI**  
Example workweek for a part-time employee working more than their authorized weekly hours.



According to the Fair Labor Standards Act, comp time is defined as leave earned at a rate not less than one and one-half hours for each hour of employment for which overtime compensation is required.

The absence of clearly defined written policies leaves staff to navigate ambiguous leave benefits independently. It remains unclear whether this practice is uniformly extended to all part-time employees or solely where it has been long-standing. Furthermore, while consolidating various leave types into a single category may streamline payroll processes, identifying the source of hours and rate of accrual becomes increasingly challenging.

Some regular part-time employees under the 9-1-1 Employees Association agreement have guidelines governing their leave options, while others lack any guidance in this area. In discussions with payroll, recategorizing this type of leave would require tremendous hours of work and a reconfiguration of NOVAtime that would exceed the benefits of defining this leave as something other than comp time.

***Recommendation #5***

***The County should establish and document comprehensive leave options and procedures specifically tailored to part-time employees.***

### **NOVAtime System**

The audit report on [Vacation and Sick Leave](#) highlighted structural and operational issues within the NOVAtime system. These issues included negative employee leave balances, restricted reporting choices, the existence of test accounts in the live system, and discrepancies in employee records between NOVAtime and Tyler ERP. The [follow-up report](#) revealed that reporting options remained unchanged, and a resolution for the presence of test accounts had not been found. Additional control issues within NOVAtime were discovered during this audit.

**NOVAtime system controls do not consistently restrict employees from exceeding their accrued comp time leave balance in certain instances.**

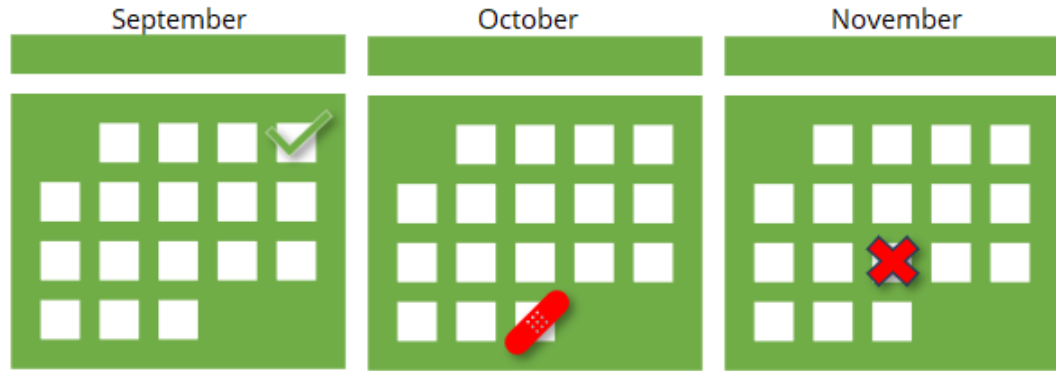
Ten employees used more comp time leave than they had banked over the past two fiscal years.

The County Leave Policy, HR-14, specifies that supervisors can only approve scheduled leave for hours currently in the employee's leave bank, and they are not allowed to approve leave contingent upon future accumulation or credit to the leave bank.

Allowing employees to use more leave than available is a risk to the County. The County is advancing leave to a person without guarantees that the time will be worked.

Auditor created example of a comp time leave request.

**Figure XII**  
Example of how a negative comp leave balance is created.



In this example the employee begins September with 10 hours of leave. In the first week of September, they request to use 8 hours in the third week of November. They mistakenly use 8 hours of comp time at the end of October for an illness. When the approved date in November comes around, the system takes the 8 hours of approved leave even though the employee only has 2 in the leave bank.

Timing plays a large factor in this issue. If the supervisor approves an employee's request to use comp time in the future knowing their current balance is sufficient to cover the request, but then the employee uses comp time prior to that future date the bank does not have enough to cover the approved request, leaving it negative once that date is reached.

NOVAtime does not have preventative controls that limit the employee's ability to use more comp time than they have available taking into consideration future approved requests. An attentive supervisor may catch the error, but that is not an effective control to prevent the advance.

**Recommendation #6**

***The Finance Department should develop stronger controls around negative comp time leave balances.***



**Generic user accounts compromise NOVAtime security.**

Some Human Resources staff were not assigned individual user accounts and were sharing generic supervisory level user logins to perform data entry and reviews required as part of their assigned duties.

**Figure XIII**  
Three users accessing the system using two shared generic logins.



The Government Accountability Office Federal Information System Controls Audit Manual urges organizations to ensure identification and authentication are unique for each user.

When users cannot be distinguished from one another, tracking changes to the system, and identifying responsible individuals in case of errors or malicious intent becomes increasingly challenging.

Generic user accounts were set up in 2017 and 2018 when the County transitioned to NOVAtime. The creation of generic user accounts was likely driven by cost considerations, given that each supervisor license incurs individual billing.

**Recommendation #7**

***The Finance Department should assign individual user accounts for each Human Resources staff member needing access to the NOVAtime system.***

**Data accuracy issues persist with the presence of former employee accounts in the County's timekeeping system.**

The NOVAtime system has 18 active supervisor level users who are no longer employed by the County, including five former department directors. While the passwords have been changed,

the user accounts and their corresponding permissions have not been revised.

The Government Accountability Office guidance on designing information security controls includes promptly updating access rights when employees change job functions or leave the entity.

Since the County's timekeeping system operates online and falls outside the purview of the County's information technology security system, the existing user accounts pose a potential risk for malicious activity. This risk is particularly pronounced for former departmental directors, who may retain elevated system privileges.

As previously reported in the Time Management Leave audit, there was a discrepancy in employee records between NOVAtime and Tyler ERP. The Finance Department developed a semi-annual review system but has yet to implement it. According to the Finance Department, the next scheduled system review is set for March 2024. That review schedule is expected to mitigate this issue in the future, but the immediate risk should be addressed.

***Recommendation #8***

***The Finance Department should remove supervisor-level access for all noted former employees.***

### **3. Observations**

The County's policy HR-4 and negotiated Collective Bargaining Agreements (CBAs) permit the inclusion of comp time hours in the calculation of regular hours for an employee's workweek. Currently, sick leave hours are the only explicitly excluded category from regular hours.

This provision creates opportunities for employees to exploit the system strategically. Two strategies were identified through analysis of NOVAtime data:

**Using comp time leave to accumulate more comp time than utilized.**

By strategically utilizing comp time leave at the start of the workweek, anticipating available overtime at the week's end, employees can accumulate more comp time leave than they use. In the below example, the employee uses comp time leave to gain one and a half times the comp time leave.

Auditor created example of an employee workweek.

**Figure XV**  
Example of an employee using comp time leave to gain more comp time leave than used.

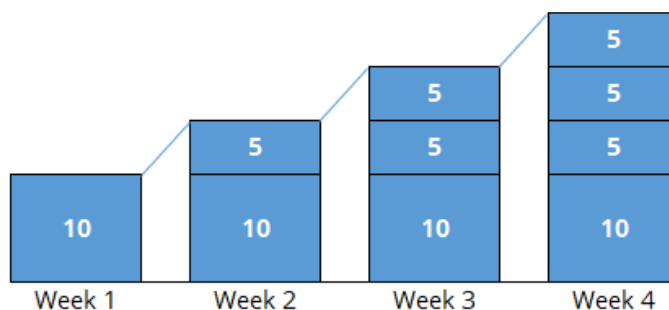
Sun	Mon	Tue	Wed	Thu	Fri	Sat
Regular Day off	10 hrs. Comp Time Leave	10 hrs. Straight Time	10 hrs. Straight Time	10 hrs. Straight Time	10 hrs. Overtime taken as comp time	Regular Day off

The employee uses 10 hours of comp time to start the week, works 3 regular shifts, then converts their overtime shift at the end of the week into comp time - essentially exchanging 10 hours of comp time leave at the beginning of the week for 15 hours of comp time leave at the end.

**Figure XVI**  
Potential to stack comp time leave hours quickly.

If this practice continued for one month, the employee would end the month with 250% more comp time leave than they used.

Auditor created example of an employee comp leave bank.



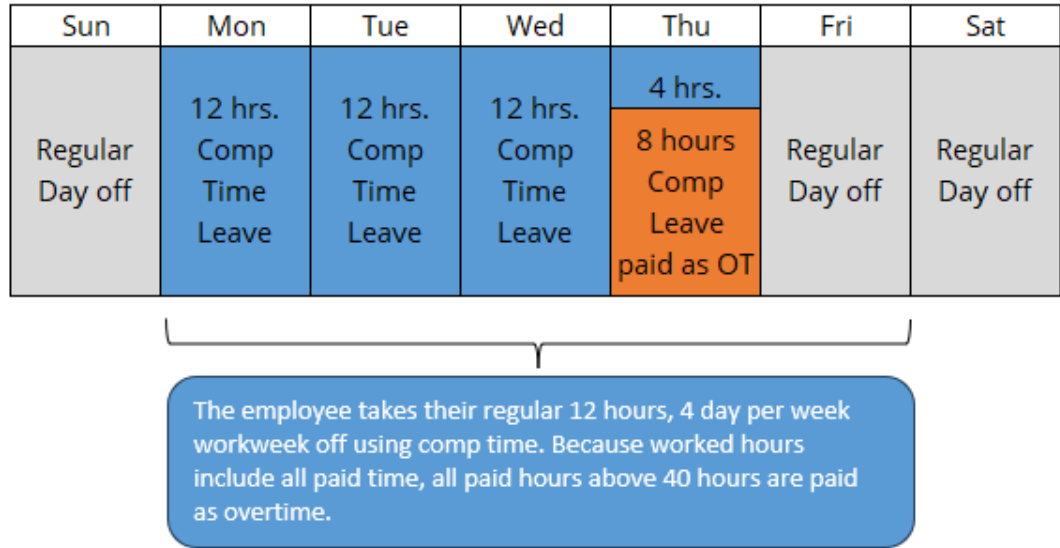
Comp leave hours were used in the same week they were accrued over 1,100 times in the last two fiscal years. It is important to note that employees are restricted by comp time leave limits based on their position. Eventually, their leave bank would reach capacity, and they would be compelled to take overtime pay. Supervisors could also identify and address this behavior by denying requests to use comp time at the beginning of the week.

**Using comp time leave to earn paid overtime.**

Some employees working a scheduled workweek exceeding 40 hours, such as four days of twelve-hour shifts, can receive overtime pay from comp leave hours. This results in earning leave hours at a 1.5x rate and being compensated at a premium overtime rate.

Auditor created example of an employee workweek.

**Figure XIV**  
Example of an employee using comp time leave to earn paid overtime.



The calculation methodology for regular hours is stipulated in each CBA. While the County's policy HR-4 is silent on compensatory time for non-represented employees, it is practically counted towards regular hours. Approximately 0.2% of the total overtime hours paid in the last two fiscal years were earned through this practice.

## 4. Management Responses

Finance Department, Robert Tintle, Chief Financial Officer



### FINANCE DEPARTMENT

Date: January 03, 2024  
To: Elizabeth Pape, County Internal Auditor  
From: Robert Tintle, Chief Financial Officer  
Re: Finance's Response to Audit Report #23/24-6 Overtime and Compensatory Time

Thank you for the internal audit and initial assessment on overtime and compensatory time. Finance appreciates your effort in this area as we work together to enhance oversight and transparency across various control areas to bolster existing systems.

Below are responses to the internal audit recommendations.

**1) Recommendation: The Finance Department monthly financial reports should include overtime expenses for major funds when the projected personnel services requirements exceed budgeted levels.**

- a) Management position concerning recommendation:  Concurs  Disagrees
- b) Comments: To provide greater transparency and accountability, when projected total personnel services costs exceed the budget, the Chief Financial Officer will include a breakout of overtime expenses when presenting the monthly financial report on major funds to the Board of County Commissioners.
- c) The new reporting will be implemented in January 2024, when applicable.

**2) Recommendation: The County should establish a centralized documentation repository for all payroll decisions that grant overtime compensation to exempt status employees.**

- a) Management position concerning recommendation:  Concurs  Disagrees

b) Comments: Finance defers the implementation of this recommendation to Human Resources. Once a centralized documentation repository is established, Finance/Payroll should have access to the policy files.

**3) Recommendation: The County should determine if the 180-day mandate is still relevant and adjust practices/revise policy based upon the determination.**

a) Management position concerning recommendation:  Concurs  Disagrees

b) Comments: Finance defers the implementation of this recommendation to Human Resources. Finance supports eliminating this policy as it is not practicable to enforce as stated.

c) If the 180-day mandate is maintained, implementation will increase the workload within Payroll and will add to the capacity constraints the section is already experiencing. Additional capacity will need to be addressed.

**4) Recommendation: The County should incorporate policies which include payouts for comp leave balances in cases of departmental transfer or promotion to exempt status.**

a) Management position concerning recommendation:  Concurs  Disagrees

b) Comments: Finance defers the implementation of this recommendation to Human Resources. Finance supports payouts for comp leave balances in cases of departmental transfer or promotion to exempt status.

**5) Recommendation: The County should establish and document comprehensive leave options and procedures specifically tailored to part-time employees.**

a) Management position concerning recommendation:  Concurs  Disagrees

b) Comments: Finance defers the implementation of this recommendation to Human Resources.

**6) Recommendation: The Finance Department should develop stronger controls around negative comp time leave balances.**

a) Management position concerning recommendation:  Concurs  Disagrees

b) Comments: Finance will develop a report to identify negative comp time leave balances and manually update timecards each pay period.

c) This recommendation was implemented in December 2023 and will continue monthly.

d) This has increased the hours required to complete the payroll process and added to the capacity constraints the section is already experiencing.

**7) Recommendation: The Finance Department should assign individual user accounts for each Human Resources staff member needing access to the NOVAtime system.**

- a) Management position concerning recommendation:  Concur  Disagree
- b) Comments: Finance has already assigned individual user accounts for each Human Resources staff member.
- c) The estimated date of completion is January 2024.

**8) Recommendation: The Finance Department should remove supervisor-level access for all noted former employees.**

- a) Management position concerning recommendation:  Concur  Disagree
- b) Comments: Finance has identified the former employee roles and has established a quarterly reconciliation of termed employees and supervisor roles.
- c) The estimated date of completion is January 2024.

**County Administration, Nick Lelack, County Administrator**



COUNTY ADMINISTRATOR NICK LE LACK

I generally concur with Finance's responses to the recommendations with the following comments:

**3) Recommendation: The County should determine if the 180-day mandate is still relevant and adjust practices/revise policy based upon the determination.**

I am concerned about the increase in liability over time (beyond 180 days) as noted in the Audit because as wages and overall personnel costs increase so too does the value (liability) of the unused comp time. With that said, as the Audit demonstrates, employees are using comp time at about the same rate as they are accruing it. It seems the 180 day requirement should remain in place and supervisors and department heads should be both informed about this policy (I expect many are not aware of it) and required to implement it.

**4) Recommendation: The County should incorporate policies which include payouts for comp leave balances in cases of departmental transfer or promotion to exempt status.**

Strongly support.

**5) Recommendation: The County should establish and document comprehensive leave options and procedures specifically tailored to part-time employees.**

I concur though I likely need a better understanding of when OT and CT are accrued if under 40 hours.

**8) Recommendation: The Finance Department should remove supervisor-level access for all noted former employees.**

Strongly support.

**Human Resources, Kathleen Hinman, Director**



HUMAN RESOURCES

Date: January 4, 2024  
To: Elizabeth Pape, County Internal Auditor  
From: Kathleen Hinman, Human Resources Director  
Re: Human Resources Response to Audit Report #23/24-6 Overtime and Compensatory Time

Thank you for the internal audit and for the opportunity to review and comment on your report, Overtime and Compensatory Time #23/24-6 (the Audit). Human Resources values your review on this important issue and the perspective it provides County Leadership as we work together to enhance oversight and transparency of this useful tool.

Below are responses to the internal audit recommendations.

**1) Recommendation: The Finance Department monthly financial reports should include overtime expenses for major funds when the projected personnel services requirements exceed budgeted levels.**

Human Resources concurs with this recommendation.



While overtime assignments may be used to offset the impact of vacancies, HR agrees that review of expenses should occur when the overall projected personnel services requirements exceed budgeted levels. Additionally, the County may benefit from review when overtime expenses exceed budgeted costs by a certain %.

**2) Recommendation: The County should establish a centralized documentation repository for all payroll decisions that grant overtime compensation to exempt status employees.**

Human Resources concurs with this recommendation.

HR will work with departments and offices to create a centralized list for instances outside of existing Collective Bargaining Agreements and County Policies when authority has been granted to provide overtime compensation, or premium compensation, to exempt status employees. This will be made available to payroll staff for their use in reviewing timesheets. The estimated date of completion is July 2024.

**3) Recommendation: The County should determine if the 180-day mandate is still relevant and adjust practices/revise policy based upon the determination.**

Human Resources concurs with this recommendation.

HR will work with the County's Policy Advisory Committee to review the current policy and determine if the 180-day mandate should be maintained. County leadership will be consulted, and the policy will be updated with any changes as needed. The estimated date of completion is July 2024.

**4) Recommendation: The County should incorporate policies which include payouts for comp leave balances in cases of departmental transfer or promotion to exempt status.**

Human Resources concurs with this recommendation.

HR will work with the County's Policy Advisory Committee to review the current policy and consider the recommendation. County leadership will be consulted, and the policy will be updated with any changes as needed. The estimated date of completion is July 2024.

**5) Recommendation: The County should establish and document comprehensive leave options and procedures specifically tailored to part-time employees.**

Human Resources concurs with this recommendation.

HR will work with the County's Policy Advisory Committee to review the current practices and any applicable policies and consider the recommendation. County leadership will be consulted, and the policy will be updated with any changes as needed. The estimated date of completion is July 2024.

**6) Recommendation: The Finance Department should develop stronger controls around negative comp time leave balances.**

Human Resources concurs with this recommendation.

HR defers to Finance/Payroll for this recommendation. It would be best if this function could be turned off in NOVAtime, or only allowed at the System Administrator level; and should be considered when next reviewing new timecard software.

**7) Recommendation: The Finance Department should assign individual user accounts for each Human Resources staff member needing access to the NOVAtime system.**

Human Resources concurs with this recommendation.

**8) Recommendation: The Finance Department should remove supervisor-level access for all noted former employees.**

Human Resources concurs with this recommendation.

**5. Appendix A: Analysis Information**

An in-depth analysis was conducted to assess whether the systemic and policy-related controls for overtime and comp time introduced any disparities among employees. The comprehensive examination did not yield any specific findings, observations, or identified opportunities for improvement. While no disparities were uncovered during this analysis, the information is presented to provide transparency and clarity, offering insight into the absence of notable differences in the application of systemic and policy-related controls for overtime and compensatory time across the employee base.

In the interest of safeguarding individual privacy and confidentiality, this report deliberately excludes specific demographic group breakdowns. The decision to withhold this information is made to prevent the potential identification of individuals within exceptionally small demographic subsets.

**Gender Identity**

For Deschutes County, women constitute a substantial portion of the workforce. At first glance, the data reveals a disparity in the female employees working paid overtime (OT) compared to their male counterparts. However, when the Sheriff’s Office (DCSO), a male-dominated field with high overtime, is excluded from the analysis, the disparities between genders diminish. However, a noteworthy observation is that comp time (CT) leave allocations appear to align more closely with the overall population percentage, even without excluding law enforcement.

	<b>Deschutes County Workforce</b>	<b>% of OT Hours Paid</b>	<b>% of OT Hours Paid w/o DCSO</b>	<b>% of CT Hours Accrued</b>
Women	56.89%	36.57%	54.93%	54.37%
Men	43.04%	63.43%	45.07%	45.63%

### Racial Identity

The County workforce primarily consists of white individuals, making up 89% of the total workforce. While the data indicates a potential disparity with non-white employees being underrepresented in overtime hours, the extent of this difference is not substantial enough to warrant additional efforts or interventions at this time.

	Deschutes County Workforce	% of OT Hours Paid	% of CT Hours Accrued
White	89%	92%	89%
Non-White	11%	8%	11%

### Age

The distribution of overtime and comp time utilization across different age groups within the workforce reveals distinct patterns. Notably, as employees age, there is a decline in both overtime earning and comp time accrual percentages, suggesting a correlation between age and not working more than 40 hours a week.

Age Range (years)	Workforce earning OT	% of OT Hours Paid	Workforce accruing CT	% of CT Hours Accrued
20-30	13%	10%	11%	9%
30-40	29%	28%	32%	31%
40-50	28%	30%	28%	30%
50-60	20%	23%	21%	26%
60-70	9%	8%	8%	3%
70-80	0%	0%	1%	1%

### Base Pay

Employees with base rates in the \$30-\$40/hr. range exhibit the highest engagement in additional work, constituting 41% of those

earning overtime and 48% accruing comp time. This group also has the highest percentage of overtime hours paid (41%) and comp time hours accrued (57%). As the base rate increases beyond 50 dollars, the percentage of employees earning overtime decreases, potentially indicating a saturation point in overtime engagement as base rates rise.

Base Rate in \$	Workforce earning OT	% of OT Hours Paid	Workforce accruing CT	% of CT Hours Accrued
10-20	1%	0%	1%	1%
20-30	29%	7%	28%	18%
30-40	41%	41%	48%	57%
40-50	21%	37%	22%	23%
50-60	5%	10%	2%	2%
60-70	2%	3%		
70-80	1%	2%		

**Length of Service**

Employees with 0-5 years of service represent the majority, comprising 50% of those earning overtime and 48% accruing comp time. However, there appears to be an underutilization of this group for paid overtime in proportion to their substantial representation. Instead, overtime hours are directed towards individuals with more tenure, hinting at a potential preference for the expertise that often accompanies greater experience.

Length of Service (years)	Workforce earning OT	% of OT Hours Paid	Workforce accruing CT	% of CT Hours Accrued
0-5	50%	29%	48%	44%
5-10	21%	26%	24%	23%
10-15	8%	12%	8%	11%
15-20	12%	20%	12%	14%
20-25	6%	10%	5%	7%
25-30	2%	3%	2%	2%

**CBA**

The employees covered under the Deschutes County Sheriff Employees Association (DCSEA) CBA stand out with 26% of the county workforce, representing nearly half of all overtime hours paid (48%) and a substantial portion of comp time hours accrued (20%). In contrast, the AFSCME CBA, representing 36% of the workforce, shows a lower percentage of overtime hours paid (8%) and a higher percentage of comp time hours accrued (30%) suggesting the preference for leave over additional pay for those employees.

CBA	Deschutes County Workforce	% of OT Hours Paid	% of CT Hours Accrued
911EU	7%	16%	9%
AFSCME	36%	8%	30%
DCSEA	26%	48%	20%
FOPPO	3%	0%	5%
IUOE	12%	8%	26%
NON-REPRESENTED	17%	20%	10%

**PERS Tier**

Employees within each category of the Public Employees Retirement System (PERS) align closely with the distribution of the workforce. With a slight uptick in overtime hours paid for Tier 1, employees who may be trying to maximize their retirement benefits and a preference to take the additional leave from comp time accrued for Oregon Public Sector Retirement Plan (OPSRP) employees.

PERS	Deschutes County Workforce	% of OT Hours Paid	% of CT Hours Accrued
Tier 1	4%	5%	2%
Tier 2	11%	19%	10%
OPSRP	85%	75%	88%

**Job Classification**

The job classifications with the highest ranks in each category are in alignment with the respective offices/departments where these roles are performed. Positions within the Sheriff's Office and 9-1-1 work the most overtime hours with overtime pay, whereas roles within the Road Department and Community Justice accumulate the most compensatory time and maintain the highest leave balances.

<b>Top 10- Avg OT hours paid with more than 10 employees in the job classification.</b>	<b>Top 10- Avg CT hours accrued with more than 10 employees in the job classification.</b>	<b>Top 10- Avg CT leave balances with more than 10 employees in the job classification.</b>
Public Safety Dispatcher II	PW Equipment Operator, Heavy	PW Equipment Operator, Heavy
Sergeant	Public Safety Dispatcher II	Public Safety Dispatcher II
Public Safety Dispatcher I	PW Equipment Operator, Light	PW Equipment Operator, Light
Deputy Sheriff	Public Safety Dispatcher I	Community Justice Specialist
Maintenance Specialist II	Parole & Probation Officer	Sergeant
Deputy Sheriff, Corrections	Maintenance Specialist II	Deputy Sheriff
Lieutenant	Community Justice Specialist	Deputy Sheriff, Corrections
PW Equipment Operator, Heavy	Code Compliance Specialist	Parole & Probation Officer
9-1-1 Call Taker	Equipment Mechanic	Landfill Site Attendant
Landfill Site Attendant	Landfill Site Attendant	Behavioral Health Spec I

### Departmental Breakdown

The Finance and Human Resources departments totals calculate to over 100% due to staff transitions from non-exempt to exempt status during Fiscal Years 2022/2023.

Office/ Department	# of FT/PT employees working during FY22/23	# of employees eligible for OT during period	% eligible for OT	# of employees with paid OT	# of employees with CT accrual	# of employees with both OT/CT	Total # of employees working OT	Total Hours of OT worked	% of eligible employees working overtime
911	67	53	79%	27	1	25	53	17,995	100%
Assessor's Office	42	37	88%	2	19	4	25	467	68%
Clerk's Office	14	10	71%	5	2	3	10	182	100%
Community Development	80	52	65%	38	1	10	49	2,070	94%
Community Justice	97	76	78%	9	14	35	58	3,440	76%
County Administration	27	12	44%	1	3	5	9	388	75%
District Attorney's Office	82	41	50%	9	7	18	34	1,045	83%
Facilities	32	26	81%	4	1	14	19	1,349	73%
Fair and Expo Center	12	8	67%	7	0	1	8	2,901	100%
Finance	22	8	36%	3	6	1	10	389	125%*
Health Services	503	211	42%	61	49	46	156	3,927	74%
Houselessness	2	1	50%	1	0	0	1	45	100%
Human Resources	10	4	40%	2	1	2	5	426	125%*
IT	21	1	5%	1	0	0	1	1	100%
Justice Court	5	3	60%	0	2	1	3	126	100%
Legal Dept	9	2	22%	0	1	1	2	21	100%
Road Department	68	57	84%	6	14	32	52	7,818	91%
Sheriff's Office	256	232	91%	118	6	103	227	68,013	98%
Solid Waste	46	40	87%	16	0	24	40	4,998	100%
Veterans Services	6	5	83%	1	0	3	4	313	80%
<b>TOTALS (AVGS)</b>	<b>1401</b>	<b>879</b>	<b>(63%)</b>	<b>311</b>	<b>127</b>	<b>328</b>	<b>766</b>	<b>115,910</b>	<b>(87%)</b>



## 6. Appendix B: Objective, Scope, and Methodology

The County Internal Auditor was created by the Deschutes County Code as an independent office conducting performance audits to provide information and recommendations for improvement.

The audit included limited procedures to understand the systems of internal control around overtime and comp time. No significant deficiencies were found in this audit. A significant deficiency is defined as an internal control deficiency that could adversely affect the entity's ability to achieve its objectives, safeguard assets, and provide comprehensive and accurate information in line with financial, compliance, or performance reporting goals. The findings noted were primarily compliance and efficiency matters.

Audit findings result from incidents of non-compliance with stated procedures and/or departures from prudent operation. The findings are, by nature, subjective. The audit disclosed certain policies, procedures and practices that could be improved. The audit was neither designed nor intended to be a detailed study of every relevant system, procedure, or transaction. Accordingly, the opportunities for improvement presented in the report may not be all-inclusive of areas where improvement may be needed and does not replace efforts needed to design an effective system of internal control.

Management has responsibility for the system of internal controls, including monitoring internal controls on an ongoing basis to ensure that any weaknesses or non-compliance are promptly identified and corrected. Internal controls provide reasonable but not absolute assurance that an organization's goals and objectives will be achieved.



*"Audit objectives" define the goals of the audit.*

### Objectives and Scope

Objectives included:

1. Analysis and assessment of employee overtime and comp time approvals and use to inform County policy and procedures.

- a. Whether it aligns with budgeted department costs
  - b. Whether it complies with policies and procedures
  - c. Whether there are disparities across employees
2. If applicable, identify opportunities for improving efficiency and effectiveness of processes.
  3. Be aware of any compliance issues with federal and state regulations and requirements, as may be applicable.

#### Scope and timing:

The audit occurred from September through November 2023. The focus of the review was on relevant personnel data and information maintained by County Information Technology, Finance, and Human Resources Departments as of September 2023. We reviewed historical information as needed to support the conclusions of the analysis. The scope did not include all aspects of internal controls employed and was limited to hours classified as overtime or compensatory time.

## Methodology



*Audit procedures are created to address the audit objectives.*

#### Audit procedures included:

- Reviewing County overtime and compensatory time policies; collective bargaining agreements (CBA); and Federal/State laws and rules.
- Interviewing selected departmental management and staff knowledgeable of the various processes to support the audit objectives.
- Evaluation of the reliability of data provided from the NOVAtime Time Management Online system. During the evaluation, the data reporting limitations of the system prevented any analysis of data prior to Fiscal Year 2021.
- Analyzing available data to support the audit objectives including:
  - Evaluation of overtime expenses and consideration of comp time liabilities in the annual budget process.

- Compliance with County policies and procedures and/or CBA requirements.
- Operation of overtime and compensatory time activity.
- Adjustments to compensatory time leave balances.
- Selected categories for the purpose of informing policy.
- Benchmarking the County to other like-size counties in Oregon.

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.

(2018 Revision of Government Auditing Standards, issued by the Comptroller General of the United States.)

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***Please take a survey on this report by clicking this link:***

<https://forms.office.com/g/yGvJ8FEAVc>

***Or use this QR Code:***



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<http://bit.ly/DCInternalAudit>.



**Recommendations**  
**4**

# Follow-up Report

## Finance/Tax – Controls over receipts

(Internal audit report #22/23-8 issued April 2023)

**The Office of County Internal Audit:**

Elizabeth Pape, CIA, CFE – County Internal Auditor  
Aaron Kay – Performance Auditor

**Audit committee:**

Daryl Parrish, Chair - Public member  
Jodi Burch – Public member  
Joe Healy - Public member  
Kristin Toney - Public member  
Summer Sears – Public member  
Stan Turel - Public member  
Patti Adair, County Commissioner  
Charles Fadeley, Justice of the Peace  
Lee Randall, Facilities Director



To request this information in an alternate format, please call (541) 330-4674 or send email to [internal.audit@Deschutes.org](mailto:internal.audit@Deschutes.org)

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## 1. Introduction

### Audit Authority

The Deschutes County Audit Committee has suggested that follow-ups occur within nine months of the report. The Audit Committee would like to make sure departments satisfactorily address recommendations.

### Background on Department and Original Audit

This was a periodic review of fiscal controls for the Finance/Tax Department in place during February 2023. The Finance/Tax Department manages all financial activities of the County including annual budget coordination, financial planning, internal and external financial reporting, general accounting, payroll, capital asset records, distribution of property taxes to all taxing districts, cash management and investments, dog licensing and administration, collection and administration of the transient room tax, and administration of the County's long-term debt.

Overall, the Finance/Tax department performed well in providing fiscal control over receipts. Recommendations were developed to assist the Finance/Tax department comply with County policy or prudent business practices for receipts.

The areas identified in the original audit for further improvement included:

- accountability for the movement of funds between people;
- efficiency for daily bank reconciliations;
- audits of transient room taxpayers; and
- management review of adjustments to the property tax system.

## 2. Follow-up Results

The follow-up included four outstanding recommendations agreed to by the department. **Figure I** provides an overview of the resolution status of the recommendations.

**Figure I –**  
How were recommendations implemented?



The details of the follow-up are included at the end of the report in **Appendix A**. In interpreting the status, Internal Audit may sometimes raise or lower the status provided by the department based on communication received from the department.

With this follow-up, seventy-five percent (75%) of the outstanding recommendations have been fully addressed, as confirmed in the provided responses. The remaining recommendation, concerning the resumption of audits for transient room taxpayers, is actively being addressed. The department has completed a request for proposals, and the contract is currently under review.



**3. Appendix A: Updated workplan (status as of February 2024)**

Recommendation	Status	Date Resolved	Updated Comment
It is recommended the Finance/Tax department develop and document controls over cash handoffs.	<b>Completed</b>	Apr 2023	The <i>Cash Receipting Process &amp; Procedure</i> documentation has been updated to include witness verification of cash counts compared to each technician’s report.
It is recommended the Finance/Tax department explore elimination of the bank account providing duplicate services.	<b>Completed</b>	Oct 2023	The Tax Refund account has been closed with the County’s bank.
It is recommended the Finance/Tax department resume audits of transient room taxpayers.	<b>Underway</b>	Feb 2024	We have completed the request for proposals for audit services for the Transient Room Tax. We have just chosen the top firm and are in the process of getting the Personal Services Contract completed to route to Legal before sending on to the firm. Audits will begin in April 2024.
It is recommended the Finance/Tax department implement and document periodic management review of property tax adjustment reports.	<b>Completed</b>	Aug 2023	Monthly report reviews have been added to the tax adjustment procedures. The Chief Financial Officer is reviewing property tax adjustment reports monthly.

## 4. Appendix B: Objective, Scope, and Methodology

### Objective and Scope



*“Audit objectives”  
define the goals of  
the audit.*

Objective:

The objective was to follow up on recommendations from the original audit.

Scope and timing:

The follow-up included four recommendations from the internal audit report for [Finance/Tax – Controls over receipts](#) issued in April 2023. The original internal audit report should be referenced for the full text of the recommendations and associated discussion. The follow-up reflects the status as of February 2024.

### Methodology

The follow-up report was developed from information provided by Judi Hasse, Deputy Tax Collector. Follow-ups are, by nature, subjective. In determining the status of recommendations that were followed up, we relied on assertions provided by those involved and did not attempt to independently verify those assertions. The updates received were included in **Appendix A**.

Since no substantive audit work was performed, Government Auditing Standards issued by the Comptroller General of the United States were not followed.

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<http://bit.ly/DCInternalAudit>.

## The Office of County Internal Audit

# Completed Follow Ups

23/24-1 - 2023 Global Report

(62 recommendations over 4 years)

23/24-13- Personal Information Data Privacy

(22/23-2 issued February 2023)

23/24-15- Finance/Tax controls over receipts

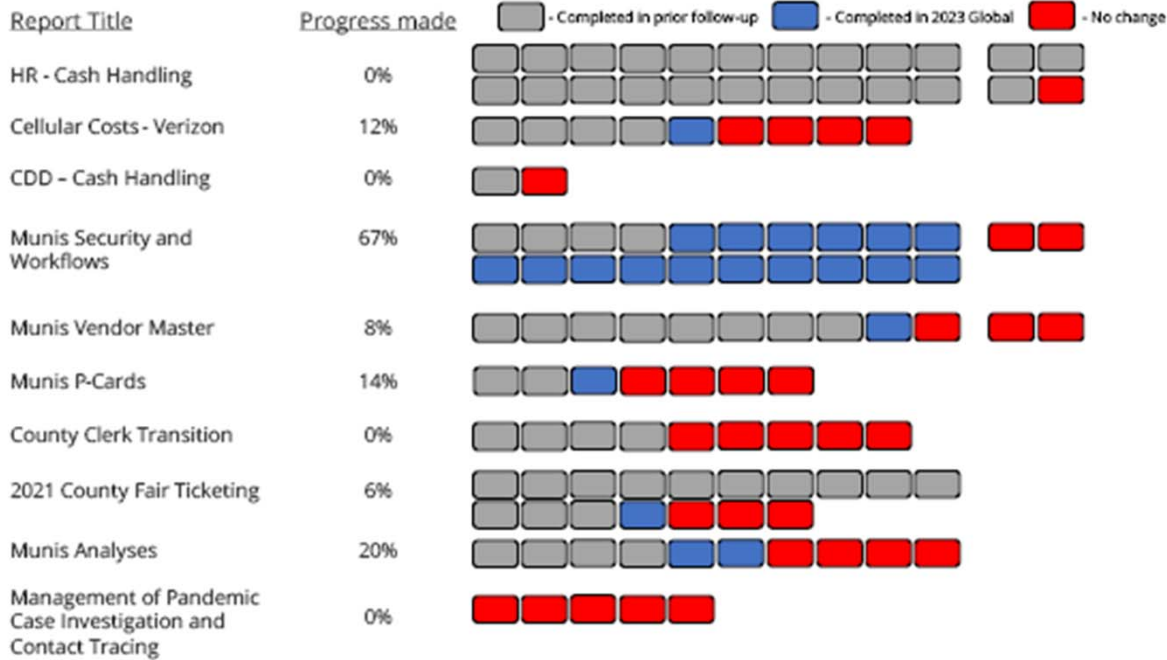
(22/23-8 issued April 2023)



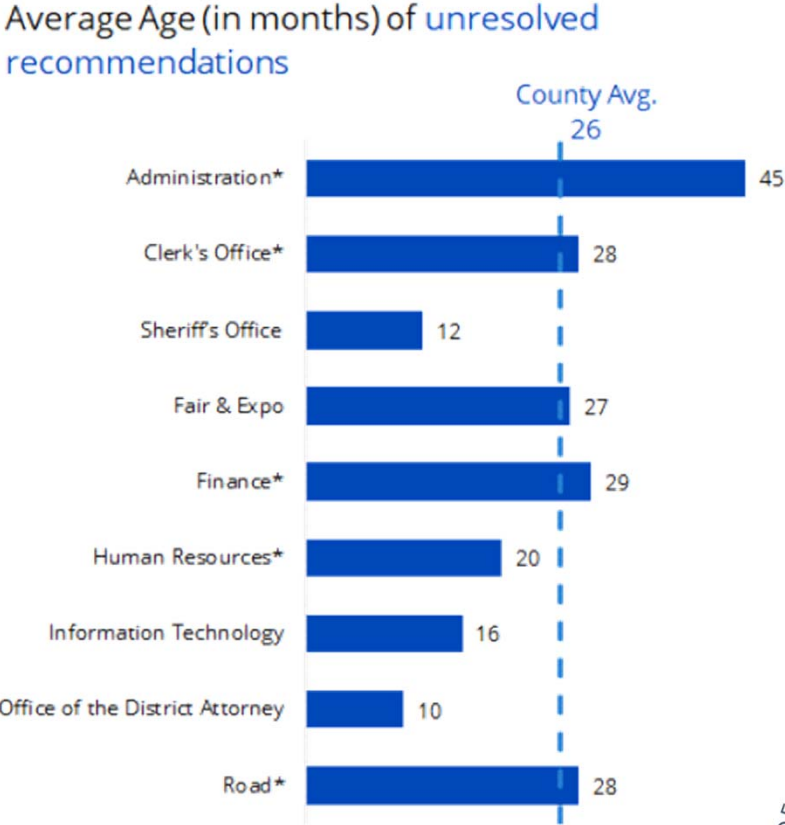
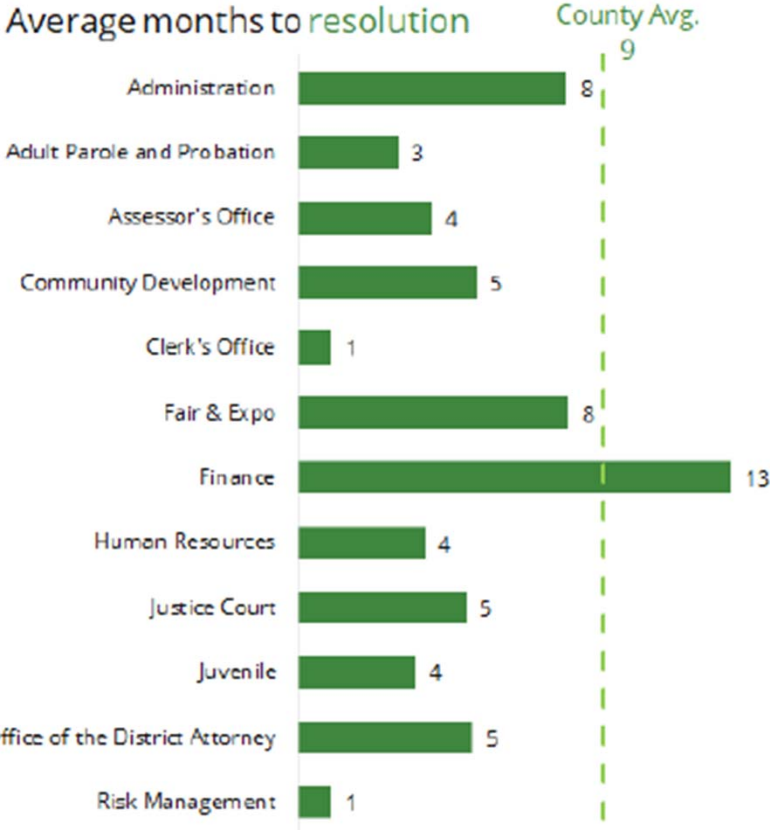
AUDIT COMMITTEE | MARCH 8, 2024

# 2023 Global Report - Progress

**Figure I** – Percent of resolved recommendation progress between the last follow-up and the 2023 Global Follow-up. Some audit reports saw **no progress** in the percentage of recommendations resolved.



# 2023 Global Report - Duration



## 2023 Global Report – Statistics



23 – Reports issued



190 – Recommendations made



128 – Resolved prior to 2023 Global



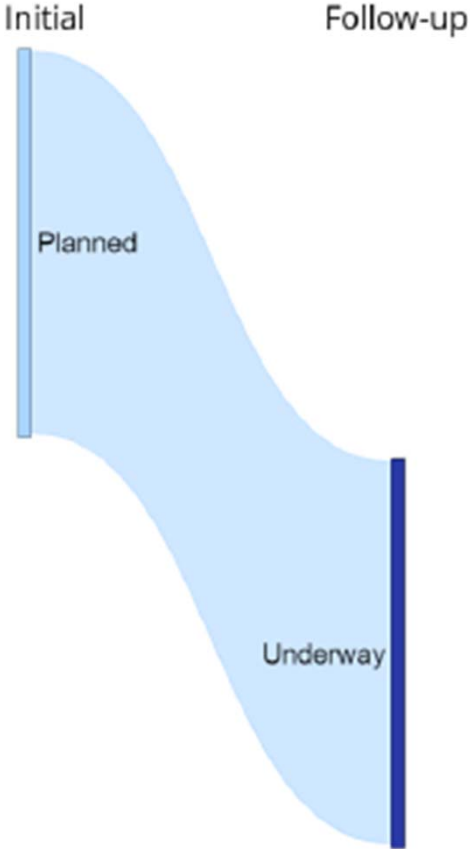
44 – remain unresolved



76.84% - 4-year resolution rate



# 23/24-12 Personal Information Data Privacy (22/23-2)



# 23/24-15 Finance/Tax Controls over receipts





# Questions?

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# Thank you





## INTERNAL AUDIT STATUS REPORT November 2023 through January 2024

Highlights for the period include:

**Audit work:**

- Equity of wages and benefits – in process
- Overtime and Compensatory Time – report issued
- Fair and Expo Cash Handling – report issued
- Internally developed software – in process
- Clerk’s Office integrated - in process

**Not-audit work:** None

**Follow-up work:** Follow-up work included 2023 Global Report, Personal Information Data Privacy, and Finance/Tax controls over receipts

**Administrative:**

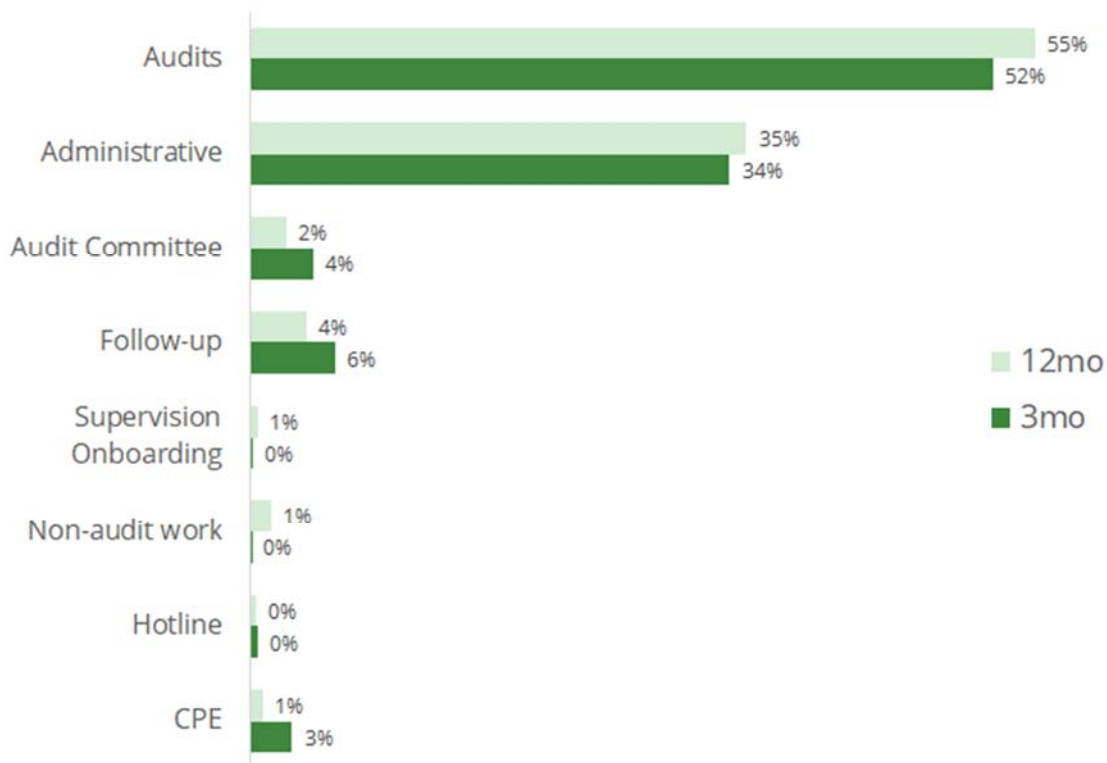
- County meetings and miscellaneous
- Internal process improvements
- Policies and procedures revision

**Supervision:** minimal

**CPE:** Year-end

**Audit committee:** Audit committee meeting, support, and recruitment

**Hotline:** minimal administration of reports



*NOTE: Time management leave of 18 hours not included over the 3 months.*



## Deschutes County Audit Committee Meeting

Friday, March 8, 2024 - Noon to 3:00 PM

63360 Britta Street NW, Building #2—Deschutes Room

**Type of Meeting:** Audit Committee Meeting  
**Facilitator:** Elizabeth Pape

### Committee Members

#### Six Public Members

- Daryl Parrish, Retired - City Manager of Covina, CA **{CHAIR}**
- Jodi Burch, CPA, Grove, Mueller & Swank, P.C.
- Joe Healy, Controller - Sunriver Owners Assoc.
- Kristin Toney, Administrative Services Director Bend Parks and Recreation
- Summer Sears, Summer Sears CPA, LLC
- Stan Turel, President Columbia Pacific Tax Service LLC

#### Three County Management Members

- Patti Adair, County Commissioner
- Charles Fadeley, Justice of the Peace Justice Court
- Lee Randall, Facilities Director

#### **{Quorum of five}**

#### Also Invited

- Nick Lelack, County Administrator
- Erik Kropp, Deputy County Administrator
- Whitney Hale, Deputy County Administrator
- Bill Kuhn, Treasurer
- Kathleen Hinman, Human Resources Director
- Robert Tintle, Chief Financial Officer
- Jana Cain, Controller
- Aaron Kay, Performance auditor
- Angie Powers, Administrative assistant

### Guests

- Geoff Hinds, Fair and Expo Center Director
- Deevey Holcomb, Community Justice Director

**Special note: Next Meeting**  
**June 14, 2024**  
*{See other meeting dates below- please put on your calendar!}*

### Calendar - Future Audit Committee Meeting

Meetings are from Noon to 3pm. We generally meet in the Allen Room (or DeArmond Rm), at the Deschutes Services Center (County/State building). Locations may vary, so please watch for notifications. **Please put these dates on your calendars and let me know if you have any conflicts.**

*(General rule: Last month in the Quarter, second Friday of the month, noon -3pm)*

- **June 14, 2024 - Friday (noon-3pm) Hybrid**
- **September 13, 2024 - Friday (noon-3pm) Hybrid**
- **December 13, 2024 - Friday (noon-3pm) Hybrid**
- **March 14, 2024 - Friday (noon-3pm) Hybrid**

### **Committee Appointments and Expiration Dates 4-6 Public; 3 County**

Name	Type	Original Appt.	Appt. Expiration date
Jodi Burch	Public	10/9/19	6/30/25
Joe Healy	Public	9/7/22	6/30/24
Daryl Parrish	Public	9/7/16	6/30/24
Kristin Toney	Public	1/2024	6/30/25
Summer Sears	Public	10/9/19	6/30/25
Stan Turel	Public	5/22/19	6/30/24
Patti Adair	County	1/2019	12/2024
Charles Fadeley	County	9/1/21	6/30/25
Lee Randall	County	9/1/21	6/30/24

*(Committee composition 4-6 Public, 3 County) (7-9 total)*

## Status of Communication / Reports

Communication / Report	Status
County code review – Audit committee and County Internal Auditor	<b>{Open for 6/2024 review}</b> Reviewed 6/2022 – and changes performed
Audit Committee survey	<b>{Next survey 2026}</b> Last survey 2023
Continuing education activity	<b>Ongoing presentations</b>
New audit committee member orientation	Orientation for new member. Four positions expire 6/24
Deeper understanding of County operations. Meetings at departments.	Community Justice 3/2024 Information Technology Tour 9/2022 Elections discussion 9/2020
Annual report to Board of County Commissioners	12/8/23 meeting
Reports of possible material violations of laws or alleged breaches of fiduciary duties are discovered.	None noted
County updates on changes	None noted
Significant audit issues or changes	No updates
Understanding County internal controls	Internal controls review through 9/2022
Review and ensure significant external audit recommendations are addressed.	None for FY23 Annual Comprehensive Financial Report
External audit recommended financial entries have been posted.	None for FY23 Annual Comprehensive Financial Report
Review and ensure significant Internal audit recommendations are addressed.	See ongoing follow-ups.
Reviews management representation letters.	Last done 9-2020
Assesses any independence issues with External auditors from non-audit work.	Agreement to perform policy reviews No non-audit work performed
Adjustments to financials from the external audit process are reviewed by audit committee.	None received for FY23 Annual Comprehensive Financial Report
Audit committee is consulted if management seeks a second opinion on accounting or audit matter	None in FY through 3/2024
Review of internal audit plan and budget	Budget discussion 3/2024 Bi-Annual Work plan 6/2023 (through 6/2025)

Communication / Report	Status
Process to assess effectiveness and value of internal audit.	Performance measures – Overall survey rating 91% FY23
Peer review performed (every 3 years. Internal audit reporting relationships reviewed)	<b>{Next Peer review est. 9/2024}</b> Peer review leader 10/2022 Peer review completed 10/2021
Establishes and manages the process for the selection, appointment, oversight, evaluation, retention and preapproval of services of the external auditors. Oversees fees.	Contract and support completed 6-2022 (contract good for 5 years before option)
Succession planning for audit committee	Board driven.
Whistleblower Hotline report (biannual?)	<b>Next report 7/2024</b> First report 7/2022