



**Office of the
Independent Auditor**

**Policies and Procedures
Engagement Manual**

AUGUST 2023

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CHAPTER 1- INTRODUCTION

100 PURPOSE AND SCOPE

This Policies and Procedures Engagement Manual documents the auditing policies, professional standards, guidelines, and procedures for planning, performing, and reporting on engagements conducted by the Office of the Independent Performance Auditor (OIPA). This manual is applicable to all engagements whether they are conducted under professional standards (i.e., auditing or attestation) or not. The OIPA created these procedures to ensure that its auditors conduct engagements in a professional manner using consistent and efficient procedures.

The Policies and Procedures Engagement Manual should serve as an orientation and training document for new audit staff, as it describes standardized procedures and evaluation techniques auditors should use to perform different engagement types (e.g. audits, attestations, surveys and reviews, etc.) conducted by the OIPA. The OIPA has made a comprehensive effort to incorporate current audit standards and procedures in this manual. However, the manual cannot address all auditing situations. Auditors should use their professional judgment and consult with OIPA's Independent Performance Auditor (IPA) to expand on the procedures outlined in this manual.

All audit staff members should become familiar with the Policies and Procedures Engagement Manual's contents and use it as a guide in carrying out their engagements. The IPA should ensure that its audit staff adheres to the manual's instructions and should use the manual to explain and clarify policies, procedures, and standards.

The Policies and Procedures Engagement Manual serves as evidence that as an organization we are following the *Government Auditing Standards, 2018 Revision*, United States Government Accountability Office (GAO) (paragraph 5.26) which describes the following:

The audit organization's policies and procedures may address consistency in the quality of engagement performance. This is often accomplished through written or electronic manuals, software tools or other forms of standardized documentation, and industry-specific or subject matter-specific guidance materials. Matters addressed may include the following:

- a. maintaining current policies and procedures;
- b. briefing the engagement team to provide an understanding of the engagement objectives and professional standards;
- c. complying with applicable engagement standards;
- d. planning the engagement, supervision, staff training, and mentoring;
- e. reviewing the work performed, the significant judgments made, and the type of report being issued;
- f. documenting the work performed and the timing and extent of review;
- g. reviewing the independence and qualifications of any specialists and the scope and quality of their work;
- h. resolving difficult or contentious issues or disagreements among team members, including specialists;
- i. obtaining and addressing comments from the audited entity on draft reports; and
- j. reporting findings and conclusions supported by the evidence obtained and in accordance with professional standards and applicable legal and regulatory requirements.

105 RESPONSIBILITY AND AUTHORITY

The OIPA is responsible for conducting audits and reviews on SANDAG's departments and other relative entities that SANDAG funds or has oversight responsibility for at the request of the board, audit committee, or management. The OIPA's authority and responsibilities are stated in the all engagements performed and are found in Board Policy No. 39, Government Code (GC), Statutes, Ordinances and other laws and/or requirements.

105.05 Audit Authority

The OIPA performs audits under various statutory authority of Government Code Sections, SANDAG Board Policies, best practices, or as a result of a special review. Prior to the acceptance of an engagement, auditors will determine the applicable audit authority and criteria to ensure a reasonable understanding, independence and other qualifications. Auditors will ensure that the review is conducted applying the appropriate audit authority and criteria identified.

110 MANUAL REVISIONS

The OIPA's IPA has the responsibility for maintaining and revising the Policies and Procedures Engagement Manual. For revisions to the manual in conjunction with field engagement procedural changes or changes in professional standards, or for clarification purposes contact the OIPA's IPA.

115 MANUAL ORGANIZATION

The Policies and Procedures Engagement Manual consist of seven chapters. The Policies and Procedures Engagement Manual begins with an introductory chapter that describes the responsibilities and authority of the OIPA to perform various engagement services. Chapter 2 discusses the applicable standards under which audit and attestation engagements are performed. Chapter 3 Engagement Life Cycle outlines the procedures to initiate an engagement and describes the general planning, field work and reporting requirements for audits, attestation, and other engagements. Chapter 4 Surveys and Reviews specifies the documentation and reporting requirements for these engagement types which do not cite professional standards in the report or letter. Chapter 5 Evidence outlines the requirements for evidence, documentation, supervision and review for all engagements. Chapter 6 outlines internal control procedures and Chapter 7 concludes the manual with the OIPA's Quality Control policies.

120 REFERENCES

This manual is a compilation of professional standards and guidance taken from various sources. The sources are as follows:

- *Government Auditing Standards, 2018 Revision*, United States Government Accountability Office (GAO)
- *Codification of Statements on Auditing Standards* American Institute of Certified Public Accountants (AICPA)
- *Codification of Statements on Standards for Attestation Engagements*, AICPA
- *State and Local Governments*, AICPA
- The IIA's *International Standards for the Professional Practice of Internal Auditing (Standards)*
- *Guide to Audits of Local Governments*, Practitioner's Publishing Company (PPC)
- *Codification of Governmental Accounting and Financial Reporting Standards*, Government Accounting Standards Board (GASB)
- *California Business and Professional Code*

125 TYPES OF AUDITS AND OTHER SERVICES

The OIPA conducts several different types of engagements encompassing a variety of engagement objectives. The types of engagements the OIPA performs may be broadly categorized as follows.

125.05 Financial Audits

The Government Accountability Office's (GAO) *Government Auditing Standards 2018* (paragraph 1.17(a)) describes financial audits as follows.

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.

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;
- (2) issuing letters (commonly referred to as comfort letters) for underwriters and certain other requesting parties;
- (3) auditing applicable compliance and internal control requirements relating to one or more government programs; and
- (4) conducting an audit of internal control over financial reporting that is integrated with an audit of financial statements (integrated audit).

Refer to the Government Accountability Office's (GAO) *Government Auditing Standards 2018* for planning, fieldwork and reporting requirements.

125.10 Performance Audits

The GAO's *Government Auditing Standards 2018* (paragraph 1.21) describes performance audits as follows.

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.

Performance audit objectives vary widely and include assessment of program effectiveness, economy, efficiency and equability; 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:

- 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.

Refer to the GAO's *Government Auditing Standards 2018* for planning, fieldwork and reporting requirements.

125.15 Attestation Engagements

The GAO's *Government Auditing Standards 2018* (paragraph 1.18) describes attestation engagements as follows.

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.

Attestation engagements are performed under the American Institute of Certified Public Accountants' (AICPA) Statements on Standards for Attestation Engagements (SSAE), as well as the related AICPA *Codification of Statements on Standards for Attestation Engagements*. *Government Auditing Standards* prescribe general standards and additional fieldwork and reporting standards for attestation engagements beyond those provided by AICPA.

Attestation engagements involve varying levels of assurance and each level of assurance has different reporting elements.

Refer to the GAO's *Government Auditing Standards 2018* for planning, fieldwork and reporting requirements.

125.20 Single Audit Act

The Single Audit Act Amendments of 1996 (Single Audit Act) require state and local governmental units that receive certain amounts of federal financial assistance to obtain an independent single audit of all federal funds received under various federal programs. Such an audit replaces separate audits of individual grants to which the entities would otherwise have been subject under federal requirements.

The Office of Management and Budget (OMB) provides auditors with guidelines and standards for accounting, budgeting, financial management, grants, and contracts. This guidance is communicated in the form of OMB Super Circular. Specifically, the sections that were previously identified as OMB A-133, *Audits of States, Local Governments and Other Non-profit Organizations*, provides specific guidelines for conducting single audit engagements. OMB A-133 stipulates that the single audit be conducted in accordance with *Government Auditing Standards*.

The audit objectives under the Single Audit Act are to:

1. Determine whether the financial statements of the auditee are presented fairly in material aspects in conformity with generally accepted accounting principles. The auditor should also determine whether the Schedule of Expenditures of Federal Awards is presented fairly in all material respects in relation to the auditee's financial statements taken as a whole.
2. Perform procedures to obtain an understanding of internal control over federal programs sufficient to plan the audit to support a low assessed level of control risk for major programs.
3. Determine whether the auditee has complied with laws, regulations, and the provisions of contracts or grant agreements that may have a direct and material effect on each of its major programs.

125.25 Non-Audit Services

In addition to audit engagements, auditing organizations may also provide non-audit services that are not covered by governmental auditing standards. Non-Audit services generally differ from financial audits, attestation engagements, and performance audits in that auditors may perform tasks requested by management that directly support the entity's operations.

Non-Audit services may provide a requesting party with information or data without providing verification, analysis, or evaluation of the information or data. Therefore, the work does not usually provide a basis for conclusions, recommendations, or opinions on the information or data. Non-Audit services may or may not result in the issuance of a report.

Audit organizations that provide non-audit services must make a determination on whether providing such services and attest engagements for the same entity potentially creates threats to independence.

Auditors should refer the GAO's *Government Auditing Standards 2018* (paragraph 3.64 through 3.106) Provision for Nonaudit Services to Audited Entities.

Auditors should refer to [Section 215.30 Independence](#) for guidance in this area.

125.30 Reviews and Surveys—Engagements Not Conducted Under Government Auditing Standards

Reviews

A review is limited in the application of procedures and scope and provides for a limited auditor assurance regarding the subject matter under review. The subject matter may involve financial transactions and data, operational processes, or informational systems. Under a review, the auditor would apply analytical procedures, perform limited tests of financial data and transactions, and conduct inquiries (e.g. interviews). The results would be documented in work papers and published in a report or letter.

Surveys

Surveys are used as a method for collecting quantitative information about a subject matter. Surveys require limited or no fieldwork in compiling the information. In some instances, surveys can lead to a review or audit. The results may not result in a report or letter.

Refer to [Surveys and Reviews Chapter 4](#) for planning, fieldwork and reporting requirements.

CHAPTER 2- PROFESSIONAL STANDARDS AND ETHICS

200 INTRODUCTION

Professional standards guide auditors in conducting financial, performance, and attestation engagements. Auditors should command a working knowledge of these standards. Auditors are also guided by professional ethics that provide guidance on professional conduct. Auditors should apply both professional standards and ethics during the course of conducting all engagements.

Auditors and audit organizations should follow the standards required by law, regulation, agreement, or contract. However, auditors and audit organizations should, at a minimum, follow *Government Auditing Standards* in conducting audits and attestation engagements of government entities, programs, activities, and functions, and of government assistance administered by contractors, nonprofit entities, and other nongovernmental entities.

205 GENERALLY ACCEPTED ACCOUNTING PRINCIPLES

Generally accepted accounting principles (GAAP) encompass the conventions, rules, and procedures that define accepted accounting practice at a particular time. General acceptance of a principle usually occurs when an authoritative body recognizes a need for an accounting convention and insists upon adherence to the conventions by the accounting profession and users of financial statements. While GAAP are usually based upon accounting and reporting methods prescribed by authoritative bodies, a particular accounting practice not addressed by an authoritative pronouncement can be considered an appropriate application of GAAP if it is prevalent in the industry.

The Governmental Accounting Standards Board (GASB) establishes accounting standards for the presentation of financial activities and transactions of state and local governmental entities; the Financial Accounting Standards Board (FASB) establishes the standards for all other entities. Created as an arm of the Financial Accounting Foundation in April 1984, GASB is the successor organization to the National Council on Governmental Accounting (NCGA) and accepts NCGA or FASB pronouncements as GAAP until superseded by a GASB pronouncement.

210 AUDITING STANDARDS

Auditing standards are a means of measurement established by professional authority. They are designed to ensure that auditors, during the course of conducting engagements, maintain competence, integrity, objectivity, and independence in planning, conducting, and reporting their work. Auditing standards are described in the GAO's Generally Accepted Government Auditing Standards (GAGAS), the International Standards for the Professional Practice of Internal Auditing (Standards), the AICPA's Generally Accepted Auditing Standards (GAAS), and/or the AICPA's Statements on Standards for Attestation Engagements (SSAE). Users of government audits and attestation engagements that are performed in accordance with these standards should have confidence that the work is objective and credible.

210.05 Generally Accepted Government Auditing Standards

In 1972, the GAO published the *Standards for Audits of Government Organizations, Programs, Activities and Functions*. The GAO reissued this publication as *Government Auditing Standards, 1994 Revision*, with amendments issued in May and July 1999. This publication is often referred to as the "Yellow Book."

Due in part to the public's demand for more government accountability, the GAO issued *Government Auditing Standards, 2003 Revision*. The 2003 revision to the Yellow Book expanded the definition of the types of audits and applicable standards, extended the requirements of Amendment No. 1, and strengthened and clarified language throughout the standards.

The GAO adopted and incorporated most current and future AICPA Statements on Auditing Standards for fieldwork and reporting in its fieldwork and reporting standards for financial and attestation engagements.

The Yellow Book expands the AICPA standards and provides additional standards.

On February 1, 2007, the Comptroller General of the United States issued the 2007 revision of *Government Auditing Standards*, which supersedes the 2003 revision. On July 27, 2007, the Comptroller General of the United States issued the 2007 revision of *Government Auditing Standards*, which supersedes the 2003 revision and updates the January 2007 revision. The July 2007 version contains the January 2007 revision to the standards and updates the quality control and peer review sections in Chapter 3.

In December 2011 Revision of *Government Auditing Standards* represented a more modernized version of the standards, considering changes in other auditing standards, including international standards. This revision supersedes the 2007 revision.

The 2018 revision of *Government Auditing Standards* is effective for financial audits, attestation engagements, and reviews of financial statements for periods ending on or after June 30, 2020, and for performance audits beginning on or after July 1, 2019. Early implementation is not permitted. The 2018 revision of *Government Auditing Standards* supersedes the 2011 revision.

An electronic version of this document can be accessed on GAO's 2018 Yellow Book web page at <http://www.gao.gov/yellowbook>.

210.10 Generally Accepted Auditing Standards

Generally Accepted Auditing Standards (GAAS), originated by the AICPA in 1947, encompass the broadest application of the auditing standards available. GAAS apply to audits performed to express an opinion on:

- The fairness with which an entity's financial statements present its financial position;
- The results of operations and cash flows and changes in financial position in conformity with GAAP; and
- Other types of audits, if they are relevant.

210.15 Statements on Auditing Standards

Statements on Auditing Standards (SASs) are issued by the Auditing Standards Board, a senior technical body of the AICPA, as interpretations of GAAS. SASs represent the most authoritative references available to auditors. SASs are often referred to as auditing standards, but they should not be identified as GAAS. However, auditors should justify any departure from the statements. Many of the SASs are relevant to the work performed by the OIPA SAS No. 1 is a codification of 54 AICPA Statements on Auditing Procedures, the predecessor to Statements on Auditing Standards. Subsequent SASs are new pronouncements issued by the Auditing Standards Board whenever an auditing problem arises that is sufficiently important to warrant an official interpretation by the AICPA. The SASs are incorporated into the AICPA professional standards publication by topic.

210.20 Attestation Standards

Attestation engagements should be performed according to the AICPA's attestation standards, as well as to the related AICPA Statements on Standards for Attestation Engagements (SSAEs). GAGAS prescribe, for attestation engagements, general standards and additional fieldwork and reporting standards beyond those provided by the AICPA. These standards have been incorporated and referenced in the *Government Auditing Standards 2018*.

210.25 International Standards for Professional Practice of Internal Auditing (Standards), and Other Accounting and Auditing Guidelines

Internal auditing is conducted in diverse legal and cultural environments; within organizations that vary in purpose, size, complexity, and structure; and by persons within or outside the organization. While differences may affect the practice of internal auditing in each environment, conformance with The IIA's *International*

Standards for the Professional Practice of Internal Auditing (Standards) is essential in meeting the responsibilities of internal auditors and the internal audit activity. *Standards* are principle-focused and provide a framework for performing and promoting internal auditing. It is necessary to consider both the statements and their interpretations to understand and apply the *Standards* correctly. The *Standards* employ terms that have been given specific meanings as noted in the Glossary, which is also part of the *Standards*.

Many less authoritative references are available in online. These references are to be used when the auditor needs more specific guidelines on appropriate accounting practices and/or how to comply with the standards and guidelines for auditing or accounting given the circumstance.

215 PROFESSIONAL ETHICS

The auditor(s) must be able to carry out his/her professional responsibilities in an ethical and professional manner. The following sections outline these ethical and professional standards.

215.05 Guidelines for Professional Conduct

Officials of audited entities that are entrusted with handling public resources and auditors of government programs fulfill essential roles and responsibilities in ensuring that public resources are used efficiently, economically, effectively, and legally. Audit organizations have the important responsibility of ensuring that auditors can meet their responsibilities. This unique role involves using sound management practices and providing professional audits and attestation engagements.

215.10 Auditors' Responsibilities

In carrying out their professional responsibilities, staff members must serve the public interest by maintaining the highest degree of integrity, objectivity, and independence. The public interest is defined as the collective well-being of the community of people and entities the auditors serve. The principles stated above are fundamental to the responsibilities of auditors.

215.15 Public Interest

Auditors should behave in a way that will serve the public interest, honor the public trust, and uphold their professionalism. A distinguishing mark of a profession is its acceptance of its responsibility to the public. This responsibility is critical when auditing in the government environment. Professional auditing standards embody the concept of accountability, which is fundamental to serving the public interest.

Auditors must make decisions that are consistent with the public interest in the program or activity under audit. In discharging their professional responsibilities, auditors may encounter conflicting pressures from management of the audited entity, various levels of government, and/or others who rely on the objectivity and independence of the auditors. In resolving those conflicts, auditors are responsible for acting with integrity, guided by the precept that individuals' and organizations' interests are best served when auditors fulfill their responsibilities to the public.

215.20 Integrity

To maintain and broaden public confidence, auditors must perform all professional responsibilities with the highest degree of integrity. Auditors must be professional, objective, fact-based, nonpartisan, and non-ideological in their relationships with audited entities and users of the auditors' reports. In the conduct of their work, auditors should be—within the constraints of the audited entity's confidentiality laws, rules, or policies—honest and candid with the audited entity and users of the auditor's work. Auditors must be prudent in the use of information they acquire in the course of their duties. They should not use such information for personal gain or in any manner that would be detrimental to the legitimate and ethical objectives of the audited entity.

Auditors should never subordinate service and the public trust for personal gain, and advantage. Integrity can accommodate the inadvertent error and the honest difference of opinion; it cannot accommodate deceit or subordination of principle. Integrity requires the auditor to observe both the form and the spirit of technical and ethical standards. Circumvention of those standards constitutes subordination of judgment. Integrity also requires the auditor to observe the principles of objectivity and independence.

Accordingly, auditors must not solicit or accept, directly or indirectly, any gift, gratuity, favor, entertainment, loan, or any other item of monetary value from a person or entity that the auditor knows or has reason to believe is seeking to receive preferential treatment or favoritism.

215.25 Objectivity and Professional Judgment

Auditors must be objective and free of conflicts of interest in discharging their professional responsibilities. Auditors are also responsible for being independent in fact and appearance when providing audit and attestation services. Objectivity is a state of mind that requires the auditor to be impartial, honest, and free from conflicts of interest. Independence precludes relationships that may in fact or appearance impair an auditor's objectivity in performing the audit or attestation engagement. The maintenance of objectivity and independence requires an auditor to continually assess relationships with the audited entities in relation to the auditor's responsibility to the public.

Auditors are responsible for using professional judgment when establishing scope and methodologies for their work, determining the tests and procedures to be performed, conducting the work, and reporting the results. Professional judgment includes exercising reasonable care and professional skepticism. Reasonable care includes acting diligently in accordance with applicable professional standards and ethical principles. Professional skepticism is an attitude that includes a questioning mind and a critical assessment of evidence. Professional skepticism includes a mindset in which auditors do not assume that management is dishonest or that management is honest beyond question. Auditors must maintain objectivity when performing their tasks, in order to make decisions that are consistent with the broader public interest in the program or activity under review. When reporting on the results of his or her work, the auditor is responsible for disclosing all material or significant facts known to him or her which, if not disclosed, could mislead knowledgeable users, misrepresent the results, or conceal improper or unlawful practices.

215.30 Independence

In all matters relating to audit work, the audit organization and the individual auditor must be independent. *Government Auditing Standards* require that all audit staff members and management have a responsibility to maintain independence so that opinions, conclusions, judgments, and recommendations will be impartial and will be viewed as impartial by knowledgeable third parties.

With the issuance of the *Government Auditing Standards, 2018 Revision (paragraph 5.08 and 5.09)* directs the auditor to establish policies and procedures on independence and requires that at least annually the auditor will obtain written affirmation of compliance from all auditors required to be independent. The IPA will accomplish this requirement on each engagement performed and document the compliance in each set of workpapers.

With the issuance of the *Government Auditing Standards, 2018 Revision*, the GAO adopted a conceptual framework of evaluating the relationship between the auditor (and audit organization) and the entity to be audited. Under this evaluation, a determination would be made by the auditor and the audit organization if such a relationship posed an unacceptable risk to the auditor's or audit organization's independence. The key to this evaluation is to assess the extent to which a threat to the auditor's/audit organization's independence exists, and whether such threat(s) would compromise the auditor's professional judgment. And if such a threat(s) existed, this assessment would include a determination whether such a threat could be effectively mitigated or eliminated by the use of safeguards.

Under this approach, the auditor and audit organization should take steps to prevent circumstances that threaten independence from compromising the professional judgment required in the performance of an attest engagement.

The approach involves the following steps and considerations:

1. Identifying and evaluating threats to independence individually or in the aggregate. The evaluation would take into consideration the type of threat and their potential effects,
2. Determining whether the identified threats are at an acceptable level or have been eliminated or sufficiently mitigated by safeguards. A threat is determined to be at an acceptable level if 1) It does not compromise the auditor's ability to conduct the engagement and influence his/her professional judgment, and 2) Would not be perceived by a reasonable and informed third party or parties that the auditor's integrity, objectivity, or professional skepticism has been compromised.
3. Apply safeguards as necessary to eliminate the threats or reduce them to an acceptable level.
4. If no safeguards are available to eliminate an unacceptable threat or reduce it to an acceptable level, independence would be considered impaired.
5. Declining to perform a perspective engagement or terminating an audit in progress if threats to independence are significant and cannot be eliminated or mitigated by safeguards.
6. Circumstances may exist in which statutory or constitutional requirements prevent the auditor and audit organization from declining to take on an engagement or terminate an engagement in progress. In such circumstances, the auditor is required to document the nature of the threat that could not be eliminated or mitigated by safeguards in the audit documentation. Additionally, The Generally Accepted Governmental Auditing Standards (GAGAS) compliance statement in the engagement's report must be modified to disclose the applicable standards not followed, the reasons why the standards were not followed, and how not following the standards affected or potentially affect the engagement. Refer to *Government Auditing Standards, 2018 Revision*, paragraph 3.25 for guidance in this area.

Threats to Independence

The following are broad categories of potential situations that may create a threat to independence. This is a limited list, as it is impossible to identify every situation that has the potential to create a threat.

- Self-interest: A potential benefit derived for the auditor resulting from a direct or indirect financial relationship with the entity or entity's officials or management.
- Self-review: The auditor reviewing, as part of attest engagement, evidence that resulted from a non-audit service performed by the auditor or other auditors within the audit organization.
- Bias: The auditor will take a position based on ideology or other conviction that is not objective.
- Familiarity: The auditor maintains a close or long-lasting relationship with the entity's management and personnel (immediate and close family member).
- Undue influence: Attempts made by the entity's management or other interested parties to coerce or use excessive influence upon the auditor. This could involve entity's interference in acceptance or rejection of audit team members due to a dispute, unreasonable time constraints placed upon the auditor to complete the engagement, or the offering of a significant gift to the auditor.
- Management participation: The auditor takes on the role or performing management functions on the behalf of the entity.
- Structural: The audit organization's placement within the state or federal government structure where such placement would impact the audit organization's ability to perform work and report results objectively.

Safeguards

Safeguards are controls implemented by the audit organization that eliminate or reduce the threats to independence. Safeguards range from partial to complete prohibitions of specific acts to procedures that counteract the potential influence of the threat. Multiple safeguards may be applied to potential threats depending on the circumstances.

1. Safeguards implemented by the audit organization

- Policies and procedures that are designed to implement and monitor quality control in attest engagements.
- Internal policies and procedures that facilitate the identification of threats to independence.
- Consulting on engagement issues with a knowledgeable third body, separate and distinct from the audit organization.
- The involvement of another audit organization to perform part of the attest engagement.
- Rotation of senior management and staff who are part of the attest engagement.
- Having a professional staff member who was not a member of the audit team to review the work performed.
- The removal of an individual from the audit team when the individual's financial interests or relationships pose a threat to independence.

2. Safeguards implemented by the entity's systems and procedures*

- An entity requirement that someone other than management ratify or approve appointments of an audit organization to perform the audit.
- Internal procedures that ensure objective choices in appointing the audit organizations to conduct engagement and non-audit services.

*Auditors should not entirely rely on such systems or procedures.

The Independence Representations form has been created to document and identifying threats to independence. This form is located on the OIPA share drive.

Non-Audit Services

Under *Government Auditing Standards, 2018 Revision*, audit organizations must make a determination on whether providing non-audit services and attest engagements for the same entity potentially creates threats to independence. This determination is made using the independence conceptual framework outlined in the standards which should be conducted prior to undertaking the non-audit service.

Auditors should refer the GAO's *Government Auditing Standards 2018* (paragraph 3.64 through 3.106) Provision for Nonaudit Services to Audited Entities.

215.35 Audit Organization Responsibilities

An audit organization also has responsibility for ensuring that:

- It maintains independence and objectivity in all phases of the assignment;

- It uses professional judgment, including exercising reasonable care and professional skepticism, in planning and performing the work and in reporting the results;
- Personnel who are professionally competent and collectively have the necessary skills and knowledge perform the work; and
- An independent peer performs a periodic review, resulting in an opinion issued as to whether the audit organization's system of quality control is designed to provide reasonable assurance of conformance with professional standards.

While management is responsible for addressing audit and attestation engagement findings and recommendations and tracking their resolution, audit organizations are responsible for establishing policies and procedures for follow-up to determine whether the audited entity has considered and addressed previous significant findings and recommendations.

If, after the final report is issued, the audit organization determines that it is not independent and has not complied with *Government Auditing Standards*, the audit organization is required to determine the impact of such circumstances on the audit. If such circumstances are considered significant, the audit organization is required to notify the auditee's management, those charged with governance, regulatory agencies, and requestors of the engagement of the independence impairment and impact on the engagement.

215.40 Use of a Specialist or Other Audit Organizations Work

When using the work of a specialist, auditors must consider the specialist to be a member of the audit team and, accordingly, assess the specialist's ability to perform the work and report results impartially. Auditors should use the independence standards outlined in *Government Auditing Standards 2018* (Chapter 3) to assess the specialist's independence. Additionally, the auditor should consider the following:

- The objectives and scope of the specialist's work;
- The specialist's relationship to the client;
- The methods or assumptions used by the specialist;
- The methods or assumptions used as compared with those used in the preceding period;
- The appropriateness of using the specialist's work for the intended purpose; and
- The form and content of the specialist's findings.

If the specialist has an impairment to independence, auditors should not use the work of that specialist.

Auditors planning to use the consulting services of internal (inside the organization) and external (outside the organization) specialists should determine whether such specialists are qualified in their fields of expertise. Such internal and external specialists are not required to comply with governmental auditing standards continuing professional education requirements. However, if the use of the internal and external specialists involves the direct participation in the directing, performing of audit procedures or reporting on an audit or attestation engagement, the specialists are required to comply with continuing professional education requirements. *Government Auditing Standards 2018* (paragraph 4.12 through 4.15).

Other Audit Organizations Work - Auditors relying on the work of another audit organization (agency) should request a copy of the agency's latest peer review report and any other written communication.

215.45 Competence

Audit staff members and management must observe the profession's technical and ethical standards, strive continually to improve competence and the quality of services, and discharge their professional responsibilities to the best of their abilities.

Competence requires from the auditor a commitment to learning and professional improvement that must continue throughout his or her professional career. In all services rendered and responsibilities executed, the auditor must undertake to achieve a level of competence that will assure that the quality of service meets the high levels of professionalism required by these Policies and Procedures Engagement Manual guidelines.

The staff assigned to perform the audit must collectively possess adequate professional competence needed to address the audit objectives and perform the work in accordance with GAGAS. Before beginning work on the audit, the staff should also collectively possess the technical knowledge, skills, and experience to be competent for the type of work being performed.

Competence represents the auditor's attainment and maintenance of an understanding and knowledge that enables him or her to render services with ease. A competent auditor knows his or her limitations and knows when to seek referrals or consultation. Each staff member is responsible for assessing his/her own competence and evaluating whether his or her education, experience, and judgment are adequate for the task to be performed.

This standard also means that the auditor is responsible for monitoring and obtaining his or her own continuing professional education in order to maintain his or her level of competence for performing the work of an auditor. Professional standards require that auditors responsible for planning or directing an audit, conducting substantial portions of the fieldwork, or reporting on the audit should complete, every two years, 80 hours of continuing professional education that contributes to their professional proficiency. An auditor should complete at least 20 of these 80 hours in any one year.

At least 24 of the 80 hours should relate to the government environment or government auditing.

220 CONTINUING PROFESSIONAL EDUCATION

To facilitate meeting the audit standards regarding continuing professional education and this manual's ethics requirement, explained under "Due Care," the auditor should refer to the AICPA, IIA, and Government Code as applicable to ensure that continued education requirements are being applied to the most current requirements.

225 STANDARDS UPDATE AND RESPONSIBILITIES

The OIPA IPA is responsible for disseminating relevant information to staff through memoranda and periodic training sessions.

The professional standards referenced throughout this document can be easily located online in various professional auditing guides, circulars, manuals and technical guides.

CHAPTER 3—ENGAGEMENT LIFE CYCLE

300 INTRODUCTION

This chapter provides an overview of the OIPA engagement life cycle. This chapter outlines initiating the engagement, general planning, fieldwork, reporting, and report processing procedures for engagements such as financial audits, performance audits, and attestation engagements resulting in a report or letter that will cite compliance with *Government Auditing Standards* and, if applicable other professional standards. This chapter also applies to engagements that will result in a report that will cite compliance with professional standards other than *Government Auditing Standards*. Auditors should also refer to the applicable professional standards to ensure that they meet the requirements for planning, fieldwork, and reporting procedures for the specific engagement type.

All engagements performed by the OIPA must be adequately reviewed and approved by the IPA or IA management (i.e. Internal Auditor and/or Independent Performance Auditor) throughout the engagement life cycle.

It is the policy of the OIPA is to determine whether to accept and/ or continue with a client. The engagement must be evaluated by OIPA management in order to make such a determination.

Refer to [Quality Control Chapter 7](#) for additional requirements for accepting and/or continuing with clients and engagements.

305 INITIATING THE ENGAGEMENT

Auditors perform certain engagements on a recurring basis. The auditor should refer to the documentation from the prior engagements as a starting point when planning the current engagement. However, the auditor must consider any changes within the entity's organization that may affect the planning for the current engagement, as well as the effect of new auditing or accounting pronouncements or other professional standards.

The engagement type is based on the level of assurance required for the engagement and the reporting objectives. Engagement type is categorized by the set of standards the engagement will follow.

Engagements are most often performed in response to requirements set forth in laws, regulations, or other regulatory requirements or in response to a request from an oversight body. These requirements often set forth the reporting objectives. In cases where the reporting objectives are not specified, the auditor should consider the users' needs and the auditor's own knowledge, skills, experience, and professional judgment when determining the appropriate set of standards to follow.

Withdrawal from Engagements

After the commencement of an engagement, situations or conditions may occur that may warrant a withdrawal from the engagement. Usually, the decision to withdraw is made during the course of the engagement. Professional auditing standards provide guidance as to conditions that may require withdrawal from the engagement.

310 GENERAL PLANNING REQUIREMENTS

Auditors must adequately plan and document all of their engagements in accordance with the OIPA's general planning requirements. See Supplement 3A – Engagement Process – Planning Table. For those engagements that follow prescribed standards, auditors must meet additional, specific planning requirements. Auditors should use the following general planning requirements for engagements performed under *Government Auditing Standards Revision 2018*: Financial Audits, Performance Audits, and Attestation Engagements and meet all applicable professional standards.

OIPA Policies and Procedures Engagement Manual

Following are the steps involved in planning financial audits, performance audits, and attestation engagements resulting in a report or letter that will cite compliance with *Government Auditing Standards 2018* and, if applicable other professional standards. The steps also apply to engagements that will result in a report that will cite compliance with professional standards other than *Government Auditing Standards*.

Note: The terms *engagement team* and *auditor(s)* are used interchangeably in this section and the following sections in this chapter.

1. The IPA identifies the type of engagement and assigns the engagement.

The IPA identifies the type of engagement and communicates what the general objectives are for that engagement. Refer to [Introduction Chapter 1](#) regarding the different types of engagements.

The IPA will assign the engagement to staff or the IPA herself who have the appropriate level of technical expertise and proficiency required for the engagement requirements. More than one auditor may be assigned to an engagement, depending on its complexity. A more experienced staff member may be assigned to an engagement to act as lead and provide on-the-job training and guidance to less experienced engagement staff.

Once the engagement team is notified of the assignment, the lead should gather the background information necessary to prepare for the engagement. The auditor will prepare a time budget with specific target dates to take into account any internally or externally imposed deadlines for completion of planning, fieldwork, and reporting. The auditor should consult with his or her IPA on these specific deadlines.

The lead will schedule an entrance conference with the entity and prepare the planning documents.

Based on the preliminary review performed and discussions with the audit IPA, the lead will prepare an Assignment Information form. This form officially documents the initiation of the engagement and includes the following basic assignment information:

- Engagement Identification
- Contract Information
- Engagement Description
- Staff Information
- Engagement Period Information
- Status
- Target Date Information
- Budgeted Hours
- Approvals

The Assignment Information form is located on the OIPA share drive.

2. Confirmation of independence.

The auditor must consider not only his or her independence with respect to the engagement in question, but also the effect that this engagement will have on other engagements the OIPA performs regarding the entity. For example, a non-audit engagement generally impairs the auditor's independence related to attest engagements performed on the same entity.

Refer to [Professional Standards and Ethics Chapter 2](#) for additional requirements on auditor's independence.

Each team member must confirm his or her independence by signing an Independence Representations form. This form is located on the OIPA's share drive.

For non-audit services, an Independence Representation Form is required. This form is located on the OIPA share drive. Refer to GAGAS 2018 Non-Audit Services Chapter for further guidance.

3. The engagement team gains an understanding of the entity and program.

Auditors should be familiar with the program by reviewing information, including criteria, policies and procedures, and internal controls.

The auditor should obtain an understanding of internal controls relevant to the engagement to the extent required for the type of engagement being performed and the professional standards being followed. Refer to the specific chapters within GAGAS 2018 for further guidance.

The auditor should conduct a preliminary risk assessment of internal controls, or fraud and/or abuse; identify potential and/or the highest risk areas requiring testing during fieldwork; and identify evidence needed to support potential findings. If internal controls are not considered as part of the engagement the auditor assigned must document the reason why internal controls are not considered.

In planning the engagement, the team should assess the risk of fraud and/or abuse. In every engagement, the team members should discuss, relative to the engagement objectives, the factors that may provide incentives or pressures for the entity's management or employees to commit fraud. The team should also discuss the entity's opportunity to commit fraud. Auditors should consider obtaining information from officials and employees from the entity, internal auditors, or external oversight agencies or departments. When factors have been identified that indicate that fraud may have occurred or is likely to have occurred, the engagement team should design procedures to provide a reasonable basis for detecting such fraud.

The engagement team shall use the Fraud Brainstorming form to document their discussion and assessment of potential fraud. This form is located on the OIPA share drive.

Auditors should perform analytical procedures during the planning phase of every engagement. The extent of the auditor's use of analytical procedures is based on the specific standards applicable to the engagement and on professional judgment. Refer to [Evidence Chapter 5](#) for guidance on analytical procedures.

4. The engagement team develops the engagement procedures

After the auditor gains an understanding of internal controls and assesses risks, he or she must develop engagement procedures for the engagement program.

The engagement program sets forth in detail a listing of specific steps and procedures necessary to achieve the engagement objectives; the program must also consider the nature, extent, and timing of work to be performed. Generally Accepted Auditing Standards (GAAS) and *Government Auditing Standards* both address the need for written engagement programs to sufficiently document planning; establish a basis for assigning work to staff; provide guidance for staff performing work; document procedures performed; and provide evidence that sufficient, appropriate evidential matter was obtained. In addition, the program functions in concert with the Planning Memorandum as a tool for planning, directing, coordinating, and monitoring the engagement.

Engagement programs are tentative and subject to revision based on new information that arises or changes in the nature, timing and extent of the engagement. Auditors may need to modify engagement procedures during the course of the engagement and document the changes in the original plan. As a result, the engagement program is not complete until the end of the engagement, when it will reflect the procedures the auditors actually performed. The final version is evidence of the auditor's planning and exercise of due professional care in performing the engagement.

5. The engagement team prepares an engagement (start) letter.

The engagement letter is a written communication that ensures that the entity agrees with the auditor about the scope, objectives, terms, and conditions of the engagement. In addition, the engagement letter should communicate to the entity what applicable professional standards, contracts, and/or regulations will apply during the course of the engagement. This letter is addressed to the entity and it is distributed to the head of the entity, entity's committee, board of directors, and those individuals or organizations charged with governance (oversight) responsibilities. The letter should also document the scheduled entrance conference date.

The primary purpose of such a letter is to minimize any possible misunderstanding concerning the scope and the terms of the engagement.

The engagement team/auditor should establish an understanding with the entity regarding the services to be performed for each engagement and should document that understanding in an engagement letter. The letter should document:

- Engagement objectives
- Management responsibilities (if applicable)
- Auditor's responsibilities or specific requirements
- Limitations of the engagement (if applicable)
- *Government Auditing Standards* and/or other applicable professional standards that will be applied to the engagement

Refer to *GAGAS 2018* and the specific engagement type for additional engagement letter requirements and the illustrations of engagement letters. Apply the SANDAG Engagement Letter which is available on the IPA's share drive.

6. The engagement team prepares the engagement planning memorandum.

A written planning memorandum is required for all engagements performed by the OIPA. The planning memorandum should include the information necessary to support the estimated staffing requirements and related costs and identify target completion dates for the basic phases of the engagement.

The planning memorandum includes (a) scope and objectives; (b) background information, including discussion of pertinent laws and regulations; (c) strategy and major phases of the engagement work; (d) resources (number of staff and hours), milestones/target dates, and staff assignments; and (e) management approval. Staff should also refer to applicable professional standards when preparing the planning memorandum to ensure that all planning requirements are met.

(a) Scope and Objectives

The scope and objectives section detail the purpose and the parameters of the engagement in terms of statements or programs to be examined and the extent of the procedures to be applied. The specific information the auditor should document in the scope section includes reporting objectives, performance or measurement criteria, statutes or regulations, applicable engagement standards, a description of the intended report or reports, a listing of report users (the entity, government officials, the media, interest groups, individual citizens), a description of the significance and needs of potential report users, and the period under review.

(b) Background Information

The background information section includes general information about the entity and the engagement. Auditors must obtain this information in order to demonstrate a sufficient understanding of the entity and the particular industry or circumstance necessary to perform the engagement.

Information typically discussed in this section includes: the entity name or other business names used; subsidiaries, component units, or other related entities; the form of government/business; the entity's organizational structure; the names of administrators, management, or other key personnel; entity's location; applicable laws or statutes; program, fund, account, or other activities that will be subject to review; and other relevant information.

(c) Strategy and Major Phases

The strategy section summarizes the pertinent areas of engagement coverage and the methods the engagement team will use to complete the engagement, based on the information obtained during preliminary work. Items considered and documented in this section should include, at a minimum, the following:

- Estimated materiality level (e.g., planning materiality);
- Strengths/weaknesses in the entity's system of internal controls (i.e. control detection and inherent risks);
- Sampling methodology;
- Steps to be performed, or reference to the engagement program and/or program modifications;
- Consideration of the entity's computer systems, including the extent to which the entity uses the computer in each significant accounting application, the complexity of computer operations, the organizational structure of computing activities, the availability of data, and the use of computer-assisted audit techniques (CAATs);
- Extent of reliance placed on the entity's computer systems and documentation validating the reliability of computer-based data. Refer to [Internal Controls Chapter 6](#);
- Consideration of the entity's use of outside entities for processing pertinent accounting or management information
- Anticipated problem areas, including follow-up on prior engagement findings, related party transactions, potential fraud and/or abuse, errors and irregularities, illegal acts, noncompliance, and going concern issues;
- Anticipated reliance on the work of outside auditors or specialists (including the qualifications and independence);
- Staffing considerations (i.e. assign sufficient staff with adequate collective professional competence to perform the engagement);
- Travel considerations;
- Establishment of an understanding with the entity;
- Entrance and exit conferences;
- Any investigations or legal proceedings initiated or in process impact on the current engagement;
- Departures from auditing or professional standards requirements due to law, regulation, scope limitations, restrictions to access to records, or other issues impacting the engagement; and
- Assessment of expected significance of evidence. (e.g. performance audits and attestation engagements)

This list is not all-encompassing; items will vary, depending on the program.

(d) Resources

The resources section includes the total budgeted hours for the engagement. The estimated hours are based on the budgeted hours per the Assignment Information form approved by the IPA. The hours in the plan should include any revisions required as a result of preliminary work performed. If the auditor makes such revisions, he or she should prepare and submit for approval a revised Assignment Information form. In those instances where the hours are being increased by more than 10%, the auditor must prepare and submit for approval a request for increased hours in accordance with instructions contained on the form.

The engagement team uses the time budget for scheduling the engagement, assigning specific tasks to staff, establishing budgets and deadlines for each significant task, documenting actual hours and completion dates, and assuring that the audit is performed efficiently. The time budget and engagement calendar establish milestones to be met in terms of hours and dates and provides a basis for evaluating staff performance.

In some circumstances, the engagement team might include external consultants or specialists hired for specific purpose(s). The auditors must identify these individuals, if any, in this section.

(e) Management Approval

The IPA must sign and date all plans. If the engagement requires the services of external consultants or specialists, the IPA must ensure that the consultants or specialists understand what to do and what the OIPA expects them to accomplish. Auditors must require the consultants or specialists to read, initial, and date all relevant planning and other working papers. Furthermore, the IPA must also approve the staff working on the engagement to ensure that the team members have the adequate professional competence, technical knowledge, skills, and experience necessary to address the engagement objectives and perform the work in accordance with professional standards.

An illustration of an engagement planning memorandum is at the end of this chapter. See [Supplement 3F](#)

315 GENERAL FIELDWORK REQUIREMENTS

Fieldwork is the process of gathering evidence, then analyzing and evaluating that evidence. The purpose of fieldwork is to accumulate sufficient and appropriate evidence to reach a conclusion concerning the engagement objectives and auditors' expectations, and to support the auditor's conclusions, findings, and/or recommendations. Refer to [Evidence Chapter 5](#) for evidence and documentation requirements.

The Following are the steps involved in the fieldwork for financial audits, performance audits, and attestation engagements resulting in a report or letter that will cite compliance with *Government Auditing Standards 2018* and, if applicable other professional standards. The steps also apply to engagements that will result in a report that will cite compliance with professional standards other than *Government Auditing Standards*.

1. The engagement team conducts an entrance conference and gains an understanding of the program and internal controls.

Auditors should communicate to the various parties involved in the engagement information about the specific nature of the engagement and should explain general information concerning the planning and conduct of the engagement. Such parties may include the head of the entity, the entity's committee, or the board of directors or other equivalent individual or entity that possesses a sufficient level of authority and responsibility for the program or activity under the engagement.

This conference is usually scheduled by a member of the engagement team through a contact with an official of the entity. This communication is followed by an engagement letter confirming with the official the engagement objectives, time frame, and documentation needs. The entrance conference is generally conducted during the first day of fieldwork.

Entrance Conference Agenda

In conducting the entrance conference, the engagement team should have an outline or agenda that highlights specific topics of the engagement. The agenda should, at a minimum, include the following specific items:

- The auditing authority to conduct the engagement
- *Government Auditing Standards* and/or other professional standards that will be applied to the engagement
- Engagement objectives
- Scope and methodology
- Protocols and engagement process to be followed
- Discussion of engagement findings and conclusions at the exit conference
- Documentation of the entrance conference attendees

An example of an entrance conference agenda is provided at the end of this chapter. See [Supplement 3G – Entrance Conference Agenda](#).

2. If relying on internal controls, the engagement team performs tests of controls and reassesses engagement risk or risk of material misstatements.

Refer to [Internal Controls Chapter 6](#) for additional requirements.

3. The engagement team reassesses risk.

Whether the auditor relies on internal controls or not, the auditor should reassess engagement risks:

- Results of test of controls (if applicable) does or does not support the planned auditor's reliance on controls; or
- Increased risks of fraud or materiality subsequent to the initial assessment; and/or
- Materiality exceeds what is tolerable for the materiality levels.

4. The engagement team finalizes the engagement planning memorandum and/or program.

The auditor should finalize the engagement planning memorandum and/or program by providing a conclusion on internal controls, identifying any modifications to the scope and objectives, and describing the planned methodology based on the results of the risk assessments.

The engagement team in the field often is the first to encounter unforeseen events or discover unexpected problems. The IPA should maintain contact with each auditor on the team to stay informed about engagement progress, potential findings, and any unexpected information. By conducting a timely review of working papers, the IPA may also discover information that will affect the planned engagement objectives and procedures.

Auditors are permitted to make minor adjustments to the engagement program without obtaining their IPA's approval. However, they must document in the engagement program included in the working papers any such engagement program changes, along with the reason for the change. If the auditors conclude that a significant change to the engagement procedures—including any expansion of engagement testing—is necessary, they must prepare an addendum to the engagement planning memorandum and submit the addendum to the IPA. The IPA must sign and date the addendum before implementing the changes.

Auditors may find it necessary to rely on the work of legal counsel in (1) determining those laws and regulations that are significant to the engagement objectives; (2) designing tests of compliance with laws and regulations; and (3) evaluating the results of those tests. Auditors also may find it necessary to rely

on the work of legal counsel when engagement objectives require testing compliance with provisions of contracts or grant agreements. Depending on the circumstances of the engagement, auditors may find it necessary to obtain information on compliance matters from others, such as the officials of other government entities that provided assistance to the entity or the applicable law enforcement authority.

5. The engagement team performs engagement procedures and discusses any findings with the entity.

Auditors apply procedures during fieldwork, perform analyses and develop conclusions and findings. If the auditors determine that the procedures in the program are not needed, or additional procedures should be added, they should obtain IPA approval.

The engagement team should discuss the findings with the entity's representative during the course of the engagement.

The auditors should document their performance of substantive tests of the entity's evidence and/or confirmations. Refer to [Evidence Chapter 5](#) for additional requirements for evidence and documentation.

Preparation of Engagement Point Sheets

During the engagement, many working papers are gathered that contain information about one or more phases of an assignment. These include copies of regulations and procedures, correspondence, records of interviews, and an assortment of schedules. Although this information may be interesting, useful, and pertinent, it is of little value unless analyzed, logically organized and collated, and interrelated. Engagement point sheets help with this process. Engagement point sheets summarize the engagement findings, discussions with the entity, the conclusions reached, and the auditor's recommendations. Engagement point sheets must be prepared in a clear, concise, and convincing manner.

When properly conceived and tailored to the particular circumstances of an assignment, engagement point sheets accomplish the following:

- Serve as a basis for reaching conclusions from the results of the engagement work.
- Become the focal point in the working papers for any particular work segment. The engagement point sheets present the underlying rationale and original thinking that leads to positions taken in reports or letters.
- Provide valuable training for staff members in developing analytical and writing skills.

An Engagement Point Sheet (EPS) form is located on the OIPA of Internal Audit's share drive. Refer to [Evidence Chapter 5 – Section 520.30](#) for the components of a point sheet.

6. The auditor conducts an exit conference.

An exit conference is a meeting between the officials representing the entity, the engagement team, and the IPA (if necessary). Depending on the issues being discussed, the exit conference may include representatives from outside organizations, officials with oversight responsibilities and those charged with governance. Auditors should conduct the conference at the conclusion of fieldwork and after the audit supervisor or IPA has reviewed the engagement documentation.

It is during this conference that a full discussion of the engagement issues and conclusions should take place between the officials representing the entity and the auditor (or engagement team). Generally, the auditor(s) has been communicating with the officials regarding engagement issues that have arisen during the course of the engagement. Any engagement issues that have not been resolved or entity disagreements with the positions taken by the auditor or engagement team should be discussed at this meeting. The auditor should clearly explain his/her observations, criteria used, cause, effect (monetary or non-monetary), overall conclusions, and recommendations. In some circumstances, a pre-draft report may be used as a discussion document during the conference. The officials from the entity should be allowed to express their views on each finding or conclusion being discussed at the conference. These

discussions should be documented.

Exit Conference Agenda

The auditor should use an exit conference agenda to document the exit conference. The auditor should prepare an outline or agenda prior to the meeting. The agenda should outline items such as:

- *Government Auditing Standards* and/or other professional standards that were applied to the engagement
- The engagement objectives and scope of work performed
- Results, findings, conclusions, and recommendations
- Pre-draft report or letter (if provided at the conference)
- Request for management responses (entity may reserve the right to respond to findings at a later date)
- Timeline for the draft report or letter issuance (if applicable)
- Appeal process (if any)
- Questions, concerns, or any requests from the entity.

An example of an exit conference agenda is provided as a supplement at the end of this chapter. See [Supplement 3I for an Exit Conference Agenda](#).

7. The engagement team completes and assembles work papers and draft report or letter packet.

The work papers should be assembled, cross-referenced, and ready for management review. The work papers should support the planning, fieldwork, and reporting of the analysis, methods, conclusions, findings, and/or recommendations.

8. The engagement team submits work papers and draft report or letter packet to the IPA for review and approval.

9. The IPA performs and completes a review of the engagement prior to the issuance of the engagement report or letter (or no more than 60 days after).

The IPA's review must be documented on the IPA's Review Checklist form is located on the OIPA of Internal Audit's share drive.

If revisions are needed, the auditor makes the necessary revisions and resubmits the work papers and draft report or letter to the IPA for review and approval.

10. The IPA performs a final review of the draft report or letterpacket.

Refer to [Evidence Chapter 5 Section 510.05](#) for review of engagement documentation requirements.

If revisions are needed, the IPA revises the report and the auditors modifies the work papers to address review comments.

320 ADDITIONAL FIELDWORK REQUIREMENTS

Following are additional requirements related to the engagement during fieldwork. The engagement team/auditors should assess the engagement progress and provide periodic status reports to management.

Requests for Increased Hours

The audit supervisor is responsible for ensuring that the number of hours charged to a particular engagement does not exceed the number of hours originally budgeted by more than 10% (as reflected in the planning memorandum and the Assignment Information form).

The IPA and/or the staff assigned to the engagement may encounter an unforeseen event or situation that may require those additional hours to be budgeted to the engagement. If the additional hours needed for the engagement exceeds 10% of the original budget, then a completed Request for Increased Hours form must be approved by the IPA. The OIPA's policy requires that the Request for Increased Hours form be submitted to the IPA before the hours charged to the engagement exceeds 75% of the original budget. The Request for Increased Hours form is located on the OIPA of Internal Audit's share drive.

Periodic Status Reports

The engagement team must communicate the progress of the engagement to their IPA on a periodic basis. This should be accomplished through progress meetings between engagement team members and the IPA. It is a good communication practice for the auditors to periodically document the progress of the engagement using a status report. The status report documents:

- Discussion between team members and IPA regarding potential findings and conclusions;
- Summary of a significant engagement issues that may impact the engagement program, time estimates, or staff assignments;
- Discussion of the current status of the engagement regarding work already performed and remaining time to complete major segments of the engagement; and
- Discussion between staff and IPA about eliminating unnecessary procedures, shortening or combining other procedures, developing alternative procedures, or expanding the scope of the engagement.

These techniques should always include some measure of feedback from members of the engagement team and IPA. Significant changes in the engagement should include additional documentation to support the auditor's change in methodology and scope.

The timing and form of the status reports should be communicated by the engagement team to the IPA. It is a good practice to require biweekly or monthly status reports for engagements lasting over several months. A periodic status report form is located at the end of this chapter. See [Supplement 3H](#) for Status Report form.

Time Control

At the beginning of the engagement, the supervisor should prepare a breakdown of the number of budgeted hours allocated to each member of the engagement team. The breakdown should follow the same format (or in greater detail) as outlined in the budgeted hours section of the planning memorandum. Each member of the engagement team should then track his or her hours accordingly and provide the IPA with updates as requested. At the end of the engagement, the supervisor should ensure that the actual hours spent on the engagement are updated in the corresponding section of the planning memorandum.

Closing, Suspending, or Canceling an Engagement before Completion

The auditor must complete an Assignment Status Change form if it becomes necessary to either close, suspend, or cancel an engagement. The auditor should state his or her reasons for the action on the form, which should also contain all appropriate approving signatures. The auditor must document the form in the working papers. If communication and coordination with the entity have commenced, the auditor should communicate the action being taken and the reasons surrounding it to the entity or to any other officials, as required. The auditor must document the communication in the working papers.

The Assignment Status Change form is located on the OIPA of Internal Audit's share drive.

Post-Engagement Planning

An important part of the engagement planning process is the critique which occurs after the engagement is substantially complete. This critique serves as advance preparation for the next engagement of the agency or program. If, during the engagement, auditors identify significant issues that warrant further work, but the issues are not directly related to the engagement objectives or the auditors do not have the time or resources to expand the engagement to pursue them, they should refer the issues to the auditors within the audit organization who are responsible for planning future engagement work. When appropriate, auditors should also disclose the issues in the report and the reasons why the issues need further study.

If it is unlikely that the engagement will be conducted again in the future, the critique and post-engagement planning procedures may not be necessary. However, the auditor should develop procedures for the follow-up review and inform the IPA of any ideas for future engagement. Based on the auditor's experience on the completed engagement, he or she may be able to recommend areas for expansion, modification, reduction, addition or deletion in the engagement program. The auditor should finalize the engagement program used during the current engagement as the suggested engagement program for the next engagement. Post-engagement planning is most effective when the auditor makes notes of possible modifications during the engagement.

In addition, the IPA should review the performance of each assigned staff member after every engagement in order to provide timely feedback. The IPA should discuss with the auditor the quality and quantity of work and the adherence to budgets and timelines.

325 GENERAL REPORTING REQUIREMENTS

Financial audits performed in a government environment primarily include audits of financial statements and are prescribed under AICPA and *Government Auditing Standards*. The AICPA Statements on Auditing Standards (SASs) also govern and provide guidance for other types of financial audits that may be performed in a government environment, such as compliance auditing, special reports, audits of service organizations, reviews of interim financial information, and letters to underwriters and certain other requesting parties. These other services may be performed in conjunction with an audit of financial statements. *Government Auditing Standards* incorporates the AICPA standards and requires additional reporting standards for audits of financial statements.

Reporting standards under *Government Auditing Standards* prescribe the form and content for performance audits. The importance of reporting results cannot be over-emphasized. Audit reports communicate audit results to officials at various levels of government, make the audit results less susceptible to misunderstanding, and facilitate follow-up for the purpose of determining whether the audited entity has taken appropriate corrective actions. Performance audit reports vary depending on the reporting entity and objectives. Reporting entities can include government organizations, programs, activities, or functions.

The AICPA Statements on Standards for Attestation Engagements (SSAE) prescribe the standards for different levels of reporting based on the type of assurance the auditors are providing.

Reporting requirements for audits conducted under Circular OMB Super Circular, the Single Audit Act. Audits conducted under the Single Audit Act are required to follow reporting standards promulgated by the AICPA, *Government Auditing Standards*, and OMB Super Circular reporting requirements.

Auditor's Report

The auditor's report or letter is a formal document used to communicate the engagement results. The report or letter must be written accurately, objectively, convincingly, clearly, and concisely.

Auditors must consider various forms of reporting when addressing different types of reporting entities and scope requirements.

Management Representation Letter

Management representation letters are required for financial audits and attestation engagements. They are optional for performance audits. The representation letter should be dated as of the date of the final report or letter.

During an engagement, management makes many representations, both oral and written, to the auditor in response to specific inquiries or through the financial statements. Such representations from management are part of the engagement evidence the independent auditor obtains, but they are not a substitute for the application of those engagement procedures necessary to afford a reasonable basis for an opinion regarding the financial statements under audit. Written representations from management ordinarily confirm representations explicitly or implicitly given to the auditor, indicate and document the continuing appropriateness of such representations, and reduce the possibility of misunderstanding concerning the matters that are the subject of the representations. An appropriate way of documenting these representations is through a management representation letter.

Management representation letters should:

- Be typed by the entity on its own letterhead.
- Be addressed to the IPA of the OIPA.
- Be dated as of the date of the auditor's report or letter (or anticipated date of the final report or letter).
- Identify in the introductory paragraph the engagement period, financial statements, accounts, claims, or reports being audited.
- Be signed by member(s) of the entity's management who have overall responsibility for financial and operating matters and are knowledgeable about the matters covered by the representations.

The written representations to be obtained should be based on the nature and basis or presentation of the circumstances of the engagement and the nature and basis of presentation of the financial statements being audited. Management need not state all of the representations in the representation letter. However, if matters exist that should be disclosed to the auditor, management should indicate these matters by listing them following therepresentation.

PROGRAM NAME
[Project name]
ENGAGEMENT PLANNING MEMORANDUM ¹
ENGAGEMENT PERIOD: _____ THROUGH _____
ID No. XXX-XXX-XXX

TO: _____, Audit IPA

FROM: _____, AIC

ENTITY: _____

PROGRAM NAME: _____

ENGAGEMENT PERIOD: _____ through _____

ENGAGEMENT ID: XXX-XXX-XXX

SECTION I SCOPE AND OBJECTIVES, AND BACKGROUND INFORMATION

This section includes an identification of the scope of the engagement, objectives, authority and general information:

- Scope and Objectives – details the purpose of the engagement and defines the parameters of the engagement. The specific information to be documented in the scope section includes reporting objectives, performance or measurement criteria, statutes or regulations, applicable standards, etc. Furthermore, it is important to mention what type of engagement this is and what authorities it is performed in accordance with (e.g. *Government Auditing Standards*)
- Background Information – general information about the entity, laws and regulations. Information typically discussed in this section include: entity or other business names used, subsidiaries, or other related entities, etc.

¹ This is an example of an engagement planning memorandum and can be modified to conform to any engagement program.

SECTION II ENGAGEMENT STRATEGY

This section summarizes the pertinent areas of the engagement and the strategy or methods to be used to complete the engagement, based on the information obtained during preliminary work. Items considered and documented in this section should include, at a minimum, the following:

- Preliminary review – prior engagement reports or letters and the corresponding work papers; follow-up or prior findings. If problem areas were noted, that should be documented.
- Estimated materiality level
- Risk assessment of internal controls (e.g. control, detection, and inherent risks)
- Sampling methodology
- Considerations of fraud and/or abuse
- Risk assessment - fraud brainstorming
- Risk assessment – expected significance of evidence (i.e. performance audits and attestations)
- Consideration of the entity’s computer systems
- Outside use of auditors or specialist
- Establish an understanding with the entity (e.g. engagement letter)
- Entrance and exit conferences
- Establish distribution of report or letter

This list is not all-encompassing; items will vary, depending on the program.

SECTION III TIME BUDGET

This section includes the total budgeted and actual hours for the engagement breakdown in different segments which will vary by the program.

SECTION IV ENGAGEMENT CALENDAR

This section includes the estimated completion date for the different areas which will vary by the program.

SECTION V MANAGEMENT APPROVAL

This section is the approval of the engagement. The suggested OIPA language for the engagement planning memorandum (EPM) is below:

The staff members assigned to this engagement collectively have the adequate professional competence, technical knowledge, skills and experience necessary to address the engagement objectives and perform the work in accordance with GAGAS and/or other professional standards.

OIPA Policies and Procedures Engagement Manual

I approve the EPM and the professional competence and technical knowledge of the staff on this engagement. Any significant changes will be documented in an addendum

Auditor

Date

Independent Performance Auditor

Date

ENTRANCE CONFERENCE AGENDA – ENGAGEMENT EXAMPLE 1

Entity Name Program Type
Entrance Conference Agenda
Engagement Period XX-XXX-XXX

Date: _____
Time: _____ a.m.
Location: _____

AUTHORITY

The Yolo County’s Internal Audit OIPA authority to perform the audit is provided by *Government Code (GC) Section XXXX and XXXX*. GC Section **xxxx** states that...

OBJECTIVE

The general objective of the audit is to determine whether the costs ... for the pe r i od o f FY 2007- 08, FY 2008-09, and FY 2009-10 are in compliance program requirements.

SCOPE AND METHODOLOGY

- Engagement will be performed in accordance with Generally Accepted Government Auditing Standards
- Trace the costs claimed to supporting documentation to determine whether the costs were incurred for the program
- Confirm that the costs were not funded by another source
- Review the costs claimed to determine whether the costs were unreasonable and/or excessive

FIELDWORK

- Working hours at the district’s office?
- Work space?
- Who receives document requests?
- Auditor may request additional documentation throughout the audit process.
- Estimate length of fieldwork – Exact time frame cannot be determined at this time. It is dependent on factors such as the nature of documentation provided.

EXIT CONFERENCE/FINDINGS

We will brief the county of any findings as they occur. In addition, we will conduct an exit conference to discuss any findings in a formal forum.

- Engagement report process:
 1. Draft report process
 2. Auditee response and deadline for response
 3. Final report issued

QUESTIONS AND ANSWERS

Persons Attending Entrance Conference

Name	Position	Organization

¹ This is an example of an entrance conference agenda that can be modified to conform to any engagement program.

STATUS REPORT ¹

Date: As of

Audit IPA:

Engagement Identification Number:

Period covered under engagement:

Staff	Budgeted Hours	Actual Hours (to date)	Unexpected Hours	Percentage of Auditor Hours Used

Date engagement assigned:

Estimated findings:

Summary of significant engagement issues:

Current status of engagement:

Problems encountered to date (if none, state "None"):

Anticipated completion date:

Signature: _____

Date: _____

¹ This is an example of a status report that can be modified to conform to the engagement program.

EXIT CONFERENCE AGENDA - AUDIT ENGAGEMENT EXAMPLE ¹

Name of the Auditee
 Engagement Period
 Identification Number

Date of Conference		
Time of Conference		
Location		
In attendance	Name	Organization
	(Use attached sheet if necessary)	

Discussion Outline:

I. Discussion of the engagement objectives and scope of work and the report process

- Restatement of the engagement objectives and procedures performed
- Engagement was performed in accordance with Generally Accepted Government Auditing Standards
- Any limitations or constraints on auditor’s application of procedures (if applicable)
- Explanation of the report process (i.e. draft and final reports)

II. Results of field work

- Findings and conclusions resulting from the application of procedures. The auditor should provide in sufficient detail the auditor’s observations, the criteria applied to support the auditor’s conclusions and the cause and effect for each finding.
- Recommendations and corrective actions that should be implemented by the auditee.
- Solicitation of the auditee’s response to the auditor’s findings and recommendations. Auditee may reserve the right to respond to the findings at a later date.

III. Timeline for the draft and final report issuance

- Estimated time for the auditee to respond in writing or provide additional documentation after the issuance of the audit report.
- Estimated time for the issuance or release of the draft and final report.

IV. Appeal process (if any)

- Identify any administrative remedies (appeals) that are available to the auditee after the final report is issued.

V. Questions and Comments

CHAPTER 4—SURVEYS AND REVIEWS

400 INTRODUCTION

This chapter describes standardized procedures and evaluation techniques auditors should use during the course of their surveys and reviews engagements which are not conducted under *Government Auditing Standards*. The chapter covers the three engagement phases—planning, fieldwork, and reporting—and describes processes, documentation, and reporting requirements. The OIPA created these policies and guidelines to ensure that audit staff members conduct surveys and reviews engagements in a professional manner using consistent and efficient engagement procedures.

This chapter should serve as an orientation and training document for new audit staff. The OIPA has made a comprehensive effort to incorporate policies and procedures in this chapter. However, this chapter cannot address all surveys and reviews situations. Auditors should use their professional judgment and consult with their supervisor to expand on the procedures outlined in this chapter.

400.05 Surveys and Reviews Definitions

Surveys

Surveys are used as a method for collecting quantitative and qualitative information about a subject matter. Surveys are usually completed during short time duration and require limited or no field work in compiling the information. Surveys may incorporate questionnaires, physical observations conducted by the auditor, and research. Information gathered during the survey process can be integrated into a subsequent audit or attestation strategy for developing tests and procedures for gathering additional evidence. Survey results are documented into work papers and are generally published in a letter format. The survey letter would **not** include a statement that the engagement was conducted in accordance with *Government Auditing Standards*.

Reviews

Reviews are limited in the application of procedures and scope and provides for a limited auditor assurance regarding the subject matter under review. The subject matter may involve financial transactions and data, operational or informational processes. Under a review, the auditor would apply analytical procedures, perform limited tests of financial data and transactions, and conduct inquiries (e.g. interviews). The results should be documented in work papers and published in a report or letter. The review report or letter would **not** include a statement that the engagement was conducted in accordance with *Government Auditing Standards*.

Review engagements types cited in attestation standard described under GAAS or GAGAS are not included in the above definition. Staff should refer to GAGAS for guidance.

405 SURVEYS AND REVIEWS REQUIREMENTS

The OIPA of Internal Audits (OIPA) requires all engagements conducted by audit staff to adhere to work paper and reporting requirements. Additionally, the OIPA has adopted elements of the general auditing standards outlined in both the AICPA and *Government Auditing Standards* to provide guidance for auditors. This approach provides for uniformity in addressing auditor's, engagement planning, gaining an understanding of the entity under review, objectivity and independence, and the need to obtain sufficient and appropriate evidence to provide a basis for the report or letter. In addition to the OIPA's policy, the auditor should consider the requirements specified in interagency agreements, federal and state regulations, or legislation.

The engagement team may need to consider performing the engagement under AICPA and/ or GAO standards if the scope of work provides for a higher level of auditor assurance. Engagements that require the auditor to express an opinion, report on internal controls or similar objectives should consider performing the engagement under professional auditing standards. In such cases, the engagement team should refer to *GAGAS 2018* for guidance.

410 PLANNING FOR THE ENGAGEMENT

As part of the planning process, the auditor should consider the extent and timing of work to be performed to accomplish the engagement's objectives. The engagement plan will take into account any preliminary information regarding the entity obtained by the auditor, required strategies to be performed, as well as other factors that will provide the basis of the overall plan.

410.05 Assignment Information Form

The audit IPA will determine the engagement type and assign staff based on their technical expertise and proficiency. Once the auditor or the engagement team is notified of the assignment, the auditor will be appointed by the IPA. The auditor, or auditor-in-charge (AIC), will be responsible for gathering and preparing the preliminary planning documents that are required for every engagement.

The AIC will complete an assignment information form can be located on the OIPA share drive. This form officially documents the official start of the review or survey engagement. Information included in the form and completed by the auditor includes the following:

- Engagement Identification
- Contract Information
- Engagement Description
- Staff Information
- Engagement Period Information
- Status
- Target Date Information
- Budgeted Hours

- Approvals

Once the document is processed by the IPA, an engagement number will be assigned to the engagement. The auditor will use this number to identify his or her engagement documentation and report or letter.

410.10 Engagement Planning Memorandum (EPM)

The engagement planning memorandum is the primary document that outlines the auditor's planning strategy in accomplishing the engagement's objectives. All auditors performing a review and survey engagements should use the EPM to document the engagement's team strategy. The EPM should include the following planning considerations:

Scope and Objectives

The scope and objectives detail the parameters and purpose of the engagement. The scope should include the reporting objectives and the intended report, performance or criteria, statutes or regulations, and the period under review.

Background Information

This is the information obtained by the auditor during the preliminary review of the entity. The background information would include the entity's name, subsidiaries, and other related entities. This section would also include the names of the entity's management, organizational administrators, or relevant key personnel. Relevant laws and statutes that will be subject to review would be included.

The section should summarize the relevant areas of the engagement scope, and strategies, methods that will be used during the engagement. This section should disclose strategies that are consistent with the survey and review objectives and normally would not include strategies applied in more comprehensive efforts such as audit and attestation engagements. Strategies considered should include the following, at a minimum:

- Strengths and weaknesses in the entity's controls obtained through the interview or the questionnaire process
- Sampling methodology
- Consideration of the entity's use of outside entities for processing pertinent accounting or management functions
- Staffing considerations and use of internal specialists
- Steps to be performed or referenced to engagement program
- The auditor's intended use of entrance and exit conferences
- Steps in gaining an understanding of the entity's operation and business practices
- Materiality levels for further testing or reporting (as applicable)

Engagement Resources

This section outlines the time budget parameters that the auditor plans to employ in the application of the survey or review procedures. The basis for the time budget is the EPM's planning strategies, audit staff assigned, reporting deadlines, and auditor's estimates for time of completion for the field work phases of the engagement. The engagement should outline:

- The specific procedures under the planning, fieldwork, and reporting phases (as applicable)
- Audit staff assigned to the specific procedures
- Time allocated for completing the specific procedures
- Specific time and date milestones established by the engagement's management

Engagement Approval

For all survey and review engagements, the auditor must obtain appropriate approvals from the engagement supervisor or the IPA and have a planned strategy for accomplishing the engagement's objectives. The IPA's signatures on the EPM authorize the use of auditing staff, date milestones, billing amounts, and time allocated to the engagement.

Note that the auditor assigned to the engagement and IPA may make modifications to the EPM when unforeseen circumstances occur that would materially impact the engagement's team initial planning strategy. In these circumstances, the planning strategy may involve the reduction of time or effort or an expansion of applied tests and procedures and, consequently, the use of additional audit staff and time.

In either case, the circumstances should be disclosed in the EPM and a justification should be documented for either the reduction or expansion of the engagement's planned scope and time. This modification should be disclosed in an addendum to the EPM and include the approving signature of the IPA, as well as date signed.

410.15 Engagement Program

The engagement program is the specific procedures the auditor will apply to meet the objectives. The program should be in line with the auditor's planning strategy outlined in the EPM. As procedures are completed, the auditor will reference the specific procedure to the completed workpaper.

If circumstances dictate a change in the original planning strategy and additional procedures are deemed necessary to meet the objectives, the program should be modified to reflect these changes.

In addition to the specified procedures, the program will document the engagement's objectives, background, and criteria.

410.20 Gaining an Understanding of the Entity

The auditor should obtain background information on the entity. The background information will help the auditor plan for the engagement. The information will generally include, is not limited to:

- Department, district, vendor, or business name
- Locations and addresses
- Organizational chart
- Names of administrators or key officials and telephone numbers
- Specific program requirements
- Applicable regulations or statutes
- Specific accounting fund or account

Generally, an evaluation of internal controls is not required for survey or review engagements. However, gaining an understanding of the entity's control environment may provide information that will facilitate the auditor's performance of specific tests.

410.25 Engagement (Start) Letter

For review engagement types, the auditor should prepare an engagement letter using a standardized template document. The engagement letter will be addressed to the appropriate official of the entity. The auditor will need to prepare an original engagement letter, rather than using a template if the assignment is the initial work conducted on the subject matter or entity.

Survey engagements may or may not use an engagement letter, depending on how the survey work is to be conducted. An engagement letter should be prepared if the survey work will involve interactive procedures that include interviews of public officials, or an entity's personnel, or the inspection of the public organization's or company's documents. If the survey involves no interaction with a public official, organization, or private entity, and incorporates analysis previously developed from internally generated information, no engagement letter is necessary.

410.30 Independence Representation

Each member of the review and survey engagement should consider the possibility of any threats that would pose limitations on his or her ability to exercise professional judgment. These threats could encompass any financial interest, bias, or familiarity with the entity that could compromise the auditor's objectivity in completing the engagement. The Independence Representation Form is required must be signed by all members of the engagement team for both reviews and surveys. The Independence Representations form is located on the OIPA's share drive.

415 FIELD WORK REQUIREMENTS

Fieldwork is the process of gathering, analyzing, and evaluating evidence. The primary purpose of fieldwork is to accumulate sufficient and appropriate evidence to reach a conclusion concerning the auditor's objectives and provide support for the auditor's findings, conclusions, or opinions, and recommendations. Refer to [Evidence Chapter 5](#) for guidance on evidential matter and documentation requirements.

415.05 Entrance Conference

For all engagements, auditors are required to conduct an entrance conference with officials of the entity under review. The entrance conference allows the auditor to explain in greater detail the objectives, methodology, and reporting requirements of the engagement. This conference is a follow up to the engagement (start) letter sent prior to the entrance conference.

The discussion items should include, but are not limited to, the following:

- Engagement objectives and methodology
- Identification of the agency's or entity's key officials and contacts
- Specific engagement documentation requirements
- Engagement protocols for requesting documentation and scheduling interviews
- Estimated time duration of fieldwork
- Draft and final report process, including the submission of a formal response
- Administrative remedies available after the final report has been issued
- Report and work papers subject to the California Public Records Act

Auditors should document the discussion items at the entrance conference, the date of the conference, and participants in attendance. Refer to the [Engagement Life Cycle Chapter 3](#) for further guidance on the entrance conferences.

415.10 Perform Engagement Procedures

The fieldwork for surveys and review engagements will involve the application of specific procedures designed to accomplish the engagement's objectives, obtaining sufficient and appropriate evidence, and preparing engagement documentation.

415.15 Engagement Risk

The auditor will not perform a formal assessment of engagement risk for surveys and reviews. However, the auditor should be cognizant that the conclusions, findings, and results are based on the reliability and sufficiency of the information obtained to support them. Accordingly, the auditor should perform an evaluation of the information he or she used to determine its reliability and sufficiency.

The auditor should conduct a fraud brainstorming discussion with members of the engagement team. The discussion will help the team assess the risk that fraudulent activities may have been committed by the entity's management or personnel. The auditors should document this discussion using the Fraud Brainstorming Discussion form located is located on the OIPA share drive.

415.20 Preparation of Engagement Point Sheets

All unresolved issues and findings are documented using the engagement point sheet. The point sheet comprises the components to develop the auditor's findings and is the foundation for writing the engagement report. A separate point sheet should be developed for each finding or observation, with each finding component completed. All point sheets should be reviewed by the supervisor and IPA prior to any exit conference meetings with the entity's officials.

An Engagement Point Sheet (EPS) is located on the OIPA share drive.

415.25 Exit Conference

The exit conference allows the auditor to explain to the entity's key officials the specific procedures that were applied and the subsequent results of these procedures. The exit conference should be used to discuss either positive or negative results. Negative results are usually in line with the auditor's determination that the agency or entity was not in compliance with regulations or contract provisions, the auditor identified ineligible cost reimbursements, or there were weaknesses in processes or systems, as well as other issues. The entity's key officials should be given an opportunity to respond directly to the auditor's results.

In addition, the exit conference allows the auditor to discuss other aspects of the engagement: the draft or final report processes, the entity's rights to respond to the draft report, and any administrative remedies (appeals) available to the entity.

The audit staff, including the AIC and IPA (if necessary), should attend the exit conference. The level of management participation will depend on the complexity of the engagement and the issues to be discussed.

Generally, the auditor(s) should have been communicating observations and preliminary findings with the entity's officials during the course of the engagement. These discussions should be documented in the engagement point sheets for any unresolved issues. Furthermore, before an exit conference is conducted, the IPA should have reviewed and approved the issues or observations developed by the engagement team.

420 SURVEYS AND REVIEWS DOCUMENTATION

Engagement documentation must contain (unless specified otherwise), at a minimum, the following:

1. Documentation Index

All engagement documentation—whether hard copy or electric work paper—must include an index that identifies the engagement's documentation components. The purpose of the index is to help the auditor, IPA, or reviewer easily access specific work papers of interest.

The index structure should follow the OIPA's methodology of structuring the work paper set. Usually, this involves three primary sections.

- Review Report/Letter
- Preliminary (Planning)
- Field work

The number system assigned to the index is a matter of auditor preference.

1. Assignment Information Sheet

Refer to [Section 410.05](#).

2. Engagement (Start) Letter

Refer to [Section 410.25](#).

3. Independence Representations
Refer to [Section 410.30](#).
4. Engagement Planning Memorandum
Refer to [Section 410.10](#).
5. Engagement Program
Hard copy work papers require the inclusion of a hard copy program. Refer to [Section 410.15](#).
6. Gaining an Understanding of the Entity
Refer to [Section 410.20](#).
7. Engagement Risk
Refer to [Section 415.15](#).
8. Entrance Conference Write-up
Refer to [Section 415.05](#).
9. Supporting Work Papers
Auditor's detailed work papers documenting analysis, application of procedures, exhibits, sample documents etc. Refer to [Evidence Chapter 5](#) for evidence and documentation requirements.
10. Point Sheets
Refer to [Section 415.20](#).
11. Exit Conference
Refer to [Section 415.25](#).
12. Reports (Draft and Final)
Referenced copy (referenced to supporting work papers) of draft and final reports Refer to [Section 430](#).
13. Management Review of Documentation Refer to [Section 425](#).

Refer to the [Supplement 4A Surveys and Reviews Documentation Table](#) for specific documentation requirements.

420.05 Format Individual Work Papers

Individual work papers should follow the OIPA's guidelines specified in Evidence Chapter 9:

Section Description	Reference Section
Headings	520.05
Index Number and Page Number	520.10
Preparer and Reviewer Identification and Dating	520.15
Cross-Referencing	520.20
Tick marks and Legend	520.25

425 MANAGEMENT REVIEW OF DOCUMENTATION

The lead auditor or IPA should perform and complete a review of the engagement documentation and report. The purpose of the review is to determine that 1) all procedures identified in the engagement program have been completed by the auditor, 2) results and conclusions are appropriate for the work performed, and 3) the results are properly supported by the engagement documentation. Please refer to [Evidence Chapter 5 Section 530.15](#) for guidance on reviewing and documenting the review.

As part of the review process, the reviewer should provide written review comments (or coaching notes) and have the auditor follow-up with corrections or explanations to clear the review notes. The review notes can be removed from the workpapers after satisfactory follow-up by the auditor.

The reviewer should document the review by using the Supervisor’s Review Checklist – Reviews and Surveys that is located on the OIPA’s share drive.

The IPA should perform a secondary review of the engagement documentation and report. The purpose of the review is to 1) determine that the auditors complied with the procedures identified in the engagement program, 2) provide a secondary review of the documentation and report, and 3) determine that the overall results of the procedures performed are appropriate. The IPA should prepare review comments (or coaching notes) from his or her review and the comments should be removed from the workpapers after the comments have been resolved.

The IPA should document the review by using the IPA’s Review Checklist that is located on the OIPA’s share drive.

430 REPORTING OF RESULTS

All engagements are required to communicate the observations, conclusions, and findings to the audited entity. Auditors performing review and survey engagements should use the reporting formats described below.

Review Engagement Reports should include the reporting contents similar to the Performance Audit report described in *GAGAS 2018 Performance Audits Chapter*. Refer to the specific section number identified for each component for further details.

Reporting Component	Description
IPA’s Summary	This summary (if applicable) is a digest of the engagement’s results for the executive office. The executive office may approve the release of the report, ask questions regarding the engagement, or recommend changes to the report.
Title Cover Page	Title page identifies the entity name, report title, and period under review.
Transmittal Letter	The transmittal letter is used in conjunction with a final report. The transmittal identifies the entity name under review and briefly describes the report’s content.
Table of Contents	This section follows the title cover page and precedes the review report’s text. The table of contents is an outline of the major components of the report.
Summary	The summary should include the name of the entity under review, the program reviewed, and the period under review. The summary briefly summarizes the findings and conclusions of the report.

Objectives, Scope and Methodology	This section identifies the engagement objectives- why the engagement was conducted, what the report is to accomplish and why the subject matter is important. The scope provides a description of the subject matter or time period covered by the engagement. The scope should also describe any significant limitations or procedures not performed by the auditor. The report should also disclose the authority to conduct the review. A Review report will not describe the scope of the auditor’s work on internal controls or communications of any deficiencies in internal controls, and it will not include a scope paragraph indicating that the engagement was conducted under Government Auditing Standards.
Conclusion	The conclusion recaps the report’s findings.
Views of Responsible Officials	<p>This section should report the views of officials of the entity under review concerning the report’s findings, conclusions, and recommendations, and should include planned corrective action. The views of responsible officials are incorporated in the final report. This written response should be included in the report.</p> <p>If the entity under review did not submit a written response to the report, this section should note that the auditor requested a response, but none was received.</p> <p>If a draft report was not issued, this section should note that the report’s findings and conclusions were discussed with entity’s officials (including the names and titles) and the date the discussion took place. The official’s response should include his/her position on the engagement’s findings and conclusions.</p>
Distribution and Restricted Use of Reports	<p>This section should contain a separate paragraph indicating that the report:</p> <ul style="list-style-type: none"> ● Is intended solely for the information and use of the specified parties; ● Is restricted to the named specified parties; and ● Is not intended to be used by anyone other than the specified parties. <p>The report should disclose whether information contained in the report is privileged or confidential and whether information has been omitted for sensitivity or confidentiality concerns.</p> <p>The report should disclose that copies of the report are made available to the public upon request.</p>
Report Signature	The report should be signed by the IPA (or designee) and should include the date of the report below the IPA’s signature.
Review Results and Schedules	This section includes tables or schedules that summarize the engagement results. The tables or schedules should be referenced to the Findings section of the report.
Review Results Findings and Recommendations	This section reports on the engagement results using the engagement point sheet elements that were used to develop the finding. The finding should include sufficient and relevant information that will provide the reader with an adequate understanding and fair presentation of the auditor’s results.

430.05 Special Reports

In addition to its auditing function, the OIPA may be given authority to perform reviews over fiscal controls over various public funding types that includes providing oversight over departments, or major program that are funded whole or part by SANDAG. This oversight includes several functions performed by audit staff; such as providing audit guidelines for independent CPAs hired to perform the annual audit, and compiling audit results and corrective actions from CPA audit reports or other reviews. An important element of this oversight is to communicate the results compiled by the audit staff and issue a report to the appropriate level of Management or the Board.

These special reports contain the elements identified below. However, the elements and contents of these types of reports may be dictated by regulatory requirements, the type of data being presented, or other circumstances.

Reporting Component	Description
Executive Summary	This summary (if applicable) is a digest of the engagement’s results for the Executive Office. The executive office may approve the release of the report, ask questions regarding the engagement, or recommend changes to the report.
Title/Cover Page	Title page identifies the entity name, report title, and period under review.
Table of Contents	This section follows the title cover page and precedes the review report’s text. The table of contents is an outline of the major components of the report.
Introduction	The Introduction section provides an overview and background for the engagement.
Results	The Results section reports the actual results by category.
Appendices	The appendices are detailed schedules or exhibits located at the end of the report.

430.10 Letters

The use of a letter format is dependent on the reporting objectives, the engagement scope, and the intended users of the results. The engagement’s objectives and scope should be limited to specific issues that must be communicated to a specific user.

Reporting Component	Description
Executive Summary	This summary (if applicable) is a digest of the engagement’s results for the executive office. The executive office may approve the release of the report; ask questions regarding the engagement or recommend changes to the report.
Letter	The letter is addressed to the official of the entity using OIPA’s letterhead and current date. The letter communicates the review or survey results and should be signed by the IPA.
Enclosures	Enclosures would include schedules, tables, and other financial information.

435 DRAFT AND FINAL REPORTS FOR REVIEWS

Written communication of the auditor’s findings, conclusions, and recommendations should follow the OIPA’s protocol of issuing a draft (preliminary report) and final report to the entity under review. However, contracts entered into by the OIPA may specify that only a formal final report be issued and include instructions on the distribution of that report. Audit staff and management should adhere to any specific reporting and distribution requirements dictated by contractual obligations.

A draft report is a preliminary report of the auditor’s findings, conclusions, and recommendations as communicated to the entity. The draft is issued subsequent to the field exit conference conducted between

the auditor and the entity under review. The auditor should have communicated to the entity's officials the OIPA's policy for reporting results through the draft and final report process.

The OIPA's policy on issuance of reports requires that the entity's officials have an opportunity to respond to the auditor's preliminary findings and provide a written response regarding the report's factual accuracy. This opportunity to respond is limited to a time period dictated by the IPA.

Final reports are to be issued after the draft report has been issued, a formal written response has been submitted, and any additional information provided by the entity has been reviewed and taken into consideration.

Letters do not follow the same reporting protocol as reports. Letters are issued to address specific issues and may or may not invite written responses from the entity's officials. Letters generally do not follow a draft-to-final-report process.

SUPPLEMENT 4A

Surveys and Reviews Documentation Table

Document/Form Required?	Reviews	Surveys
Assignment Information Sheet	Yes	Yes
Engagement (Start) Letter	Yes	Yes
Entrance Conference	Yes	No *
Independence Representation	Yes	Yes
Planning Memorandum	Yes	Yes
Point Sheet	Yes	Yes
Risk Assessment – Overall Assessment of Evidence Checklist	Yes	No
Risk Assessment – Fraud Brainstorming Discussion	Yes	No
Exit Conference	Yes	No *
Supervisor/IPA Work Paper Review Checklist	Yes	Yes
Report	Yes	No
Letter	Yes	Yes

*Not required if the survey does not involve an interaction with an entity's official.

CHAPTER 5—EVIDENCE

500 INTRODUCTION

This chapter provides the OIPA requirements for evidence, documentation, supervision, and review for all engagements. Staff members should also refer to the professional standards and or other regulatory requirements

The OIPA has transitioned into the use of standardized work templates when possible for documenting audit work and reports. Auditors and engagement team members should refer to the OIPA's protocol and training resources as necessary for their engagements.

500.05 References

The following references have been used as technical guides for this chapter:

- *Government Auditing Standards 2018* (Financial, Attestation, and Performance)
- *AICPA Codification of Statements on Auditing Standards*
- *California Business and Professional Code Section 5071*
- *AICPA Audit Sampling – Audit Guide*

505 EVIDENCE

For all engagements the OIPA performs, team members must obtain sufficient and appropriate evidence to support the opinions, conclusions, and/or findings contained in the report or letter.

The nature of the evidence the auditor obtains varies from engagement to engagement and depends on the engagement objectives and the type of engagement (financial audit, attestation engagement, performance audit, or other). Auditors must use professional judgment in determining the nature and extent of evidence necessary to meet the OIPA's requirements as outlined in this Policies and Procedures Engagement Manual and the requirements of the professional standards applicable to the engagement.

505.05 Appropriateness of Evidence

Appropriateness is a measure of the relevance, validity, and reliability of evidence used by the auditor to support his or her findings and conclusions. Additionally, appropriateness is a function of the auditor's professional judgment, as the auditor will apply procedures in interpreting, analyzing, and summarizing evidence. Appropriateness should be of particular importance to the auditor in obtaining evidence.

Evidence is relevant as long as there is a logical relationship with the procedure being applied to it, and any conclusions drawn from the evidence make sense. Validity refers to the extent to which evidence is based on sound reasoning or accurate information. Lastly, reliability refers to the consistency of results when it can be measured, tested, verified, and supported by other sources.

505.10 Types of Evidence

Government Auditing Standards emphasize the importance of audit evidence in supporting the auditor's findings and conclusions. The importance of the evidence is measured by how persuasive and reliable it is. Engagement evidence can be categorized into the following types. Depending on how it is obtained, some types of evidence can be more reliable than other types.

- Documentary evidence is documentation that is directly obtained from the audited entity, i.e. letters, contracts, accounting records, spreadsheets, information extracted from information systems, and other similar documents. Auditors should either confirm or directly test these documents in order to determine their reliability, accuracy, and completeness.

- Testimonial evidence is information obtained through interviews, inquiries, or questionnaires. Testimonial evidence should not be the sole source of support for the auditor's findings and conclusions. Individuals providing this information may be biased, which may result in non-factual representations or limited and incomplete information that may lead the auditor to an inaccurate conclusion. The auditor should prepare a summary of oral comments and provide a copy to the entity to verify that comments contained therein are accurately stated.
- Physical evidence is evidence obtained through the auditor's direct physical examination, observation, computation, and inspection. Physical evidence may include photographs taken by the auditor, eyewitness accounts of events, and the auditor's analysis based on computations. The physical evidence may also include statistical analyses. Physical evidence is more reliable when it can be corroborated by other documents and consists of original documents and not facsimiles.

505.15 Sufficiency of Evidence

Sufficiency is a measure of the quantity of evidence used for addressing the audit objectives and supporting findings and conclusions. Sufficiency also depends on the appropriateness of the evidence. The auditor must exercise considerable judgment when determining whether he or she has achieved sufficiency. However, auditing standards recognize that auditors rely on evidence that is persuasive rather than convincing and that auditors typically work within economic limits. In assessing the sufficiency of evidence, auditors should determine whether enough evidence has been obtained to persuade a knowledgeable person that the findings are reasonable. As a guiding rule, a rational relationship should exist between the cost of obtaining evidence and the usefulness of the information obtained.

The auditor's objective is to accumulate sufficient evidence to reduce audit risk to a relatively low level for any type of engagement (financial, performance, or attestation) and support the level of assurance implied in the audit report. The auditor should select and apply procedures that assess audit risk (inherent, control, and detection risk) to support this appropriate low audit risk level.

505.20 Documenting Overall Assessment of Evidence

Government Auditing Standards requires the auditor to perform and document an overall assessment of evidence obtained by the auditor during the course of the engagement. The overall assessment evaluates the sufficiency and appropriateness of the evidence obtained by the auditor in supporting the opinion, findings or conclusions of the engagement report.

505.25 Restrictions on Applying Procedures

An auditor may face restrictions during the audit process that will prevent him or her from applying procedures required under professional auditing standards. These restrictions may result from laws or regulations, the audited entity's management or personnel-imposed scope limitations (i.e. deny access to records), or other issues impacting the engagement. Engagement documentation should include a description of the restriction (and any departure from professional auditing standards), material impact on the engagement, and the application of alternative procedures (if appropriate). Any material departure from professional auditing standards should be disclosed in the engagement report or letter.

505.30 Tests and Procedures

The auditor will use a two-pronged approach in determining the extent, timing, and nature of auditing procedures. The auditor will:

1. Develop specific objectives for each relevant assertion; and
2. Evaluate each relevant assertion as it relates to account balances, class of transaction, or report presentation and disclosure.

Once the objectives have been developed and an evaluation of the relevant assertions has been performed, the auditor should decide on the types of tests to perform.

Risk Assessment Procedures

These procedures are performed to gain an understanding of the entity and its environment and to evaluate internal controls. The assessment is undertaken to determine the risk of material misstatements (intentional omission or error) at the financial statement level and relevant assertion level. Alternatively, risk assessment procedures are conducted to determine the risk that the auditor's findings and conclusions are incomplete or incorrect due to a material misstatement or intentional omission. *Risk assessment procedures are conducted for every engagement.*

Tests of Controls

These procedures are performed to evaluate the effectiveness of internal controls in detecting material misstatements from errors or omissions. Tests of controls should be performed when the auditor's expectations that internal controls are effective and there is a planned reliance on such controls. Test of controls should be conducted if conducting substantive tests would not provide sufficient and appropriate audit evidence.

Substantive Tests

These procedures are detailed tests of account balances, classes of transactions, and disclosures. The purpose of the procedures is to test the relevant assertion. *Substantive procedures should be conducted in every engagement.*

510 ENGAGEMENT DOCUMENTATION

The OIPA requires that all engagements it performs that result in any type of attest report or letter contain documentation that:

- Provides sufficient detail as to the work performed;
- Provides detail as to how audit evidence was obtained and its source; and
- Supports the significant judgments and conclusions reached.

All engagement types must follow, at a minimum, the general requirements listed in section 510.05 of this chapter. In addition, auditors must comply with any other professional standards and/or other requirements (laws or regulations) that are applicable to the engagement.

The purpose of documentation is to:

- Provide principal support for the audit report, including evidence that applicable standards (GAAS, GAGAS, IIA, Attestation) were followed;
- Aid auditors in the conduct and supervision of the engagement; and
- Allow for quality control review.

510.05 Engagement Documentation General Requirements

The following requirements apply to all engagements performed within the OIPA. Staff members should also refer to the specific professional standards or regulatory requirements applicable to their engagements.

1. Documentation must show that the auditor has observed standards applicable to the engagement. If the auditor determines that certain standards do not apply, and/or the auditor does not follow certain standards, he or she must include in the documentation the reasons why he or she did not follow the applicable standards and the known effect on the engagement.

2. Documentation should be sufficient to enable an experienced auditor with no prior experience regarding the engagement to ascertain from the engagement documentation the evidence that supports the significant judgments and conclusions.

To meet this requirement, the documentation should be:

- Able to stand alone in providing support for the engagement report or letter issued. Support includes all criteria items, such as applicable laws, regulations, and other rules, excerpts or copies of significant or relevant contracts or agreements; and any other item necessary to support the work performed;
- Fully cross-referenced to the engagement report or letter. Cross-referencing includes financial statement amounts and notes, findings, scope, objectives, criteria, and background information. The supporting working papers referenced must actually agree or reconcile to the audit report. Also, the cross-reference must include the number of the page on which the supporting items can be found (not just working paper section number);
- Adequately detailed so as to provide a clear understanding of its purpose and source and the conclusions the auditor reached; and
- Sufficiently intelligible, clear, and neat.

All documentation including, but not limited to, the auditor's prepared summaries and schedules, accounting records, and other documentation must support the auditor's opinion, findings, or conclusions disclosed in the audit or attestation draft and final report or letter.

Additional documentation may be added to the documentation file, but the auditor must not delete or discard documentation after it has been assembled in the documentation file and has been reviewed by the supervisor and/or IPA. If it is necessary to add or amend an existing document or schedule, the auditor should identify:

- When and by whom such changes were made and reviewed;
- The specific reason or reasons for the change; and
- The effect, if any, of the changes on the auditor's conclusions.

3. Documentation should be reviewed, assembled, cross-referenced, and submitted to the file room for storage no later than 60 calendar days from the engagement's report date.
4. Documentation should contain evidence of supervisory review. OIPA management should review all engagements prior to the issuance of the report or letter. See [Section 530](#) of this chapter for more information on engagement review of documentation.
5. Documentation should include required communications with the entity.
6. Documentation should include evidence of engagement planning, including consideration of internal control, assessment of fraud risk, and analytical procedures that conforms with the professional standards and/or regulatory requirements applicable to the engagement.
7. The auditor should document all significant findings or issues. Significant findings or issues include (1) results from auditing procedures that have exceptions that are considered material; (2) circumstances that prevent, or make it difficult for, the auditor to perform audit procedures considered necessary; (3) matters related to the appropriate selection, application, and consistency of accounting principles used or other management estimates or assumptions.
8. The auditor should obtain and evaluate sufficient appropriate audit evidence to support significant accounting estimates and should document that evidence in the working papers.

9. The information contained in the working papers should be restricted to matters materially important, relevant, and useful to the objectives established for the engagement.
10. A discussion of any differences of opinion among audit staff members or between audit staff members and the r/IPA, and the resolution of these differences, must be included in the documentation.
11. A separate section in the engagement documentation file should be created for an analysis of any changes made to the auditor's opinions, findings or conclusions resulting from material changes made between the draft and final reports or letters or re-issuance of the final report or letter. This analysis should identify the fiscal and non-fiscal impact of the changes and the reason for the changes. This section should be properly referenced to supporting schedules, point sheets, and the revised audit or attestation report.

510.10 Content of Engagement Documentation Package

All engagement documentation must contain, at a minimum the following:

1. Documentation Index

All engagement documentation must have an index that identifies the engagement documentation components. The purpose of the index is to help the auditor, supervisor, or reviewer easily access specific work papers of interest.

The index structure should follow the OIPA's methodology of structuring the work paper set. Usually, this involves three primary sections:

- Engagement Report or Letter
- Preliminary (Planning)
- Fieldwork

The number system assigned to the index is a matter of auditor preference. However, it is good to maintain consistency among the OIPA and auditors.

2. Assignment Information Sheet Refer to Chapter 3 [Section 310](#)

3. Engagement (Start) Letter Refer to Chapter 3 [Section 310](#)

4. Independence Representations Refer to Chapter 2, [Section 215.30](#)

5. Engagement Planning Memorandum Refer to Chapter 3, [Section 310](#).

6. Engagement Program

All engagements require the inclusion of a program. Refer to Chapter 3, [Section 310](#).

7. Risk Assessment – Fraud Brainstorming Discussion

Form is used to document the auditor's assessment of the risk for fraud. Refer to [Section 540.05](#).

8. Entrance Conference write up Refer to Chapter 3 [Section 315](#).

9. Point Sheets
Refer to Chapter 3, [Section 315](#).
10. Supporting work papers
Auditor's detailed work papers documenting analysis, application of procedures, exhibits, sample documents etc., must be included in the hardcopy engagement binder and not simply referenced a system ledger or electronic folder.
11. Internal Controls/Assessment of Engagement Risk
Auditor's documentation should include: gaining an understanding of the control environment, determination of the level of audit risk and materiality, and any summary or bridging documents.
12. Exit Conference
Refer to Chapter 3, [Section 315](#).
13. Engagement Reports or Letters (Draft and Final)
Referenced copy (referenced to supporting work papers) of draft and final reports or letters. Refer to Chapter 5, [Section 520](#).
14. Supervisor's and IPA's Review Checklist Refer to Chapter 5, [Section 535.05](#).

515 CONTENT OF INDIVIDUAL WORKING PAPERS

All individual working papers must contain, *at a minimum*, the source, purpose, and conclusion. Some working papers may also require a scope and methodology or procedures section. Most of the time, these sections (purpose, source, scope, conclusion) are documented in a scope sheet or lead schedule.

Individual working papers may serve different functions. A scope sheet is a working paper that summarizes the results of the work performed, identifies the specific procedures performed, and identifies a conclusion about the results for the work papers set. A lead schedule is a schedule generally located at the beginning of the working paper set that summarizes the detailed schedules behind it.

515.05 Source

The term "source" refers to the specific origin of the information or document. For documents, the source identifies the specific person (name, title, entity) who provided the document. If the document was obtained from an entity (for example, the library, Internet, or other agency), then the name of the entity must be specified. For working papers generated by the auditor (lead or scope sheets or testing spreadsheets), the first source item should state "auditor-generated" and should be followed by a listing of other documents used (with cross-references) and persons interviewed.

Under no circumstances should the source of any working paper be simply a cross-reference to another working paper. The source may include a cross-reference, but it cannot simply be a cross-reference. Again, the "source" should refer to the origin of the information.

515.10 Purpose

The purpose should document the reason(s) why a working paper was prepared and the relationship to the overall audit objective. Purpose may include one of the following.

1. To perform an engagement procedure. The wording of the purpose should be identical to the wording contained in the engagement program. A cross-reference to the engagement program item should also be included. For example:

Purpose: To perform test of significant expenditures as per Engagement Program Item III.2.a at w/p <2D-1, pg 6>.

2. To support another working paper, either by providing documentation or by performing a sub-procedure. For example:

Purpose: To document expenditure ledger used in test of significant expenditures at (w/p reference)

Purpose: To document sample selection process for test of significant expenditures at (w/p reference).

3. To summarize or provide results of multiple working papers. For example:

Purpose: To determine if the auditee's payroll expenditures are properly supported and do not include non-program related employees.

515.15 Conclusion

All working papers involving tests, analysis, or summation must include a conclusion. The conclusion should coincide with the working paper's stated purpose and relate to the overall engagement objective. For working papers documenting an engagement procedure or analysis, the conclusion should state the results of the procedure or analysis. When the purpose of the working paper is to provide supporting documentation, the conclusion should either reference another working paper's conclusion or state the reason or objective for including the documentation in the working papers.

515.20 Scope

The auditor should fully describe the scope of the engagement work. The auditor should identify and define precisely what the engagement procedure involves or tests. For example, for a sampling procedure, the auditor may include such information as:

- The volume of transactions involved;
- The number of items examined;
- The time period represented in the testing;
- The method used in selecting the sample; and
- The sample value and the relationship to the total population.

The scope should document any significant limitations or uncertainties the auditor has uncovered through the auditor's overall assessment of evidence checklist.

515.25 Procedures or Methodology

The auditor should detail in the working papers the specific engagement steps and procedures performed. Some common terms to describe procedures include inquiry, observation, inspection, confirmation, recalculation, comparison, scanned, read, agreed, re-performed, traced and reconciled.

For specific tests using a statistical or non-statistical sampling approach, the auditor should document the specific steps outlined in [Sections 555.30](#) and [555.40](#) of this manual.

As a general rule, engagement work papers should have an indication (or reference) that the auditor has performed an engagement procedure resulting in an analysis or a result. Auditors should refrain from including work papers that simply “document”.

The auditor should consider documenting only those relevant work papers as evidence. It is not necessary to document an entire contract or a multipage report if only certain pages are relevant to the auditor’s tests.

520 FORMAT OF INDIVIDUAL WORKING PAPERS

OIPA staff members should follow the guidelines below for all engagements. The guidelines apply to either the individual working paper or to each individual page of the working paper.

520.05 Headings

Every individual working paper must contain a heading (if the working paper contains more than one page, only the first page requires a heading). The heading should include the following elements and should agree to the corresponding items on the Assignment Information Sheet.

- Name of entity under audit or review
- Name of program
- Engagement period
- Engagement identification number
- Title of the working paper

520.10 Index Number and Page Number

Every individual page included in the engagement working paper file must have an index number and a page number. The index number on the working paper must agree to the corresponding item listed in the engagement index.

The standard index numbering system is as follows:

Section:	1, 2, 3, . . .
Sub-section:	A, B, C, . . .
Working paper Item:	-1, -2, -3, . . .

For example, for Section 3, Subsection B, working paper 1 appears as 3B-1.

If continuation pages are necessary, they should be numbered and include the total number of pages (e.g. 1 of 2 or 1/2). The index and page number should be included on each working paper.

For example:

Index Number	Page Number
3B-1	1 of 4
3B-1	2
3B-1	3
3B-1	4 of 4

This ensures that all working papers are accounted for and allows the auditor to detect any missing working papers. The above example should be used by the OIPA’s auditors when preparing working papers. Auditors can write a header or create one in Microsoft Word for the index number, page number, etc. The header should be placed *in the upper right-hand corner*.

The following example illustrates such a header:

W/P 3B-1	Page 1 of 10
Prepared by (Auditor)	Date
Reviewed by (Supervisor)	Date

520.15 Preparer and Reviewer Identification and Dating

All working papers should be initialed and dated as follows:

- The preparer must initial and date (in black print) each working paper in the upper-right corner. The date should reflect the date on which the working paper was finished.
- The reviewer must include his or her initials and the date of the review on each working paper that has been reviewed.

520.20 Cross-Referencing

“Referencing” between working papers simply means correlating or identifying where certain information or amounts came from and/or where they are going. Cross-referencing means “crossing” references back so that working papers reference one another. The following rules apply to cross-references.

- Cross-references should be written in red and placed in brackets. If the cross-references are typed rather than written, the auditor should underline the cross-references in red.
- References to another working paper should be placed to the right of or below the amount or item being referenced, as follows:

$$\underline{\$500,000} <3A-1> \quad \text{or} \quad \begin{array}{c} \underline{\$500,000} \\ <3A-1> \end{array}$$

- Referenced from another working paper should be placed to the left of or above the amount or item being referenced, as follows:

$$<3A-1> \underline{\$500,000} \quad \text{or} \quad \begin{array}{c} <3A-1> \\ \underline{\$500,000} \end{array}$$

All the relevant working papers in a working paper set should be cross-referenced to one scope sheet or lead schedule that shows the final audited numbers and corresponding working papers that reference tests and procedures performed.

Generally, each working paper should indicate its source(s) of information and the auditor’s conclusion. The auditor should place the purpose, source, scope, and conclusion (p/s/s/c) on each working paper subsequent the scope sheet or lead schedule. The p/s/s/c should be placed on the bottom section of the working paper as follows:

p/s/s/c 3A-1 1 of 20

When documenting a series of working papers, the auditor can perform the following alternative to document the p/s/s/c on the supporting working papers.

If working papers are among a series of similar documents (e.g. all invoices), the auditor should place the p/s/s/c on the bottom section of the first working paper of the series. The p/s/s/c should indicate the range of work papers applicable to the referenced p/s/s/c. The auditor should ensure that all working papers in the series are relevant and support the p/s/s/c indicated.

Guidelines for Cross-Referencing

- All sources of information that are being transferred from one work paper to another must contain **to** and **from** cross references.
- Lead or summary schedules should have references for all sources, scope procedures, analysis and conclusions from supporting schedules.
- Individual scope sheets for detailed tests should have references for all source, scope procedures, analysis and conclusions from supporting schedules. These supporting schedules would include the analysis contained in entity prepared spreadsheets or documents, auditor- prepared work sheets or exhibit documents.
- Summary schedules or tables containing amounts should be referenced from a supporting work paper. Individual amounts should be referenced and not as a range of amounts, unless it is apparent (visually) that the amounts are coming from the same source.
- When the referenced amount is a calculation, the work papers should document the calculation.
- All point sheets should contain references from supporting work papers for any observation, qualitative or quantitative findings,
- Engagement reports or letters (draft and final) should be referenced to point sheets, planning memorandums, and other supporting documents. Elements of the engagement report or letter should be referenced from a supporting document.
- In general, the flow of auditor's findings and results should start first with the individual work paper, then go on to scope and summary schedules, then to point sheets, and then end with the audit report. Cross-referencing should follow this flow.

520.25 Tick Marks and Legends

Tick marks are symbols used as a shorthand method for making explanatory comments or describing procedures or results of procedures.

Although many standard tick mark symbols exist, no standard meaning exists for any tick mark. Therefore, the auditor must explain all tick marks. Any working paper containing tick marks must also include a legend, or a clear explanation of the symbols, or a cross-reference to a working paper that includes a tick mark legend.

As a general rule, tick marks symbols should always appear in red. An illustrative tick mark legend is provided in [Supplement 5A](#) of this chapter.

520.30 Engagement Findings

Preparation of Engagement Point Sheets

Engagement point sheets summarize the audit findings, discussions with the auditee/entity, the conclusions reached, and the auditor's recommendations. Engagement point sheets must be prepared in a clear, concise, and convincing manner.

The following provides guidance on the components of the point sheet:

1. Observation

The observation includes a description of the procedure, transactions, or event that the auditor observed and judged to be in violation of, or in noncompliance with, professional standards, agency rules or regulations, contracts or grant agreements. The observation can include a description of the auditor's physical inspection, analysis, or application of tests and procedures.

2. Judgment Criteria

Criteria are the laws, regulations, contracts, grant agreements, accounting principles, expected performance, accepted business practices, and benchmarks against which the auditor compares and evaluates an existing condition. The criteria support the auditor's observation of a violation or noncompliance of an existing condition.

3. Effect

Effect is the qualitative and quantitative (monetary) results of the auditor's observation. The effect is the logical link that establishes the impact or potential impact between an existing condition and the required or desired condition.

4. Cause

Cause is the reason or explanation for the conditions, or the factors responsible for the violation or noncompliance event identified in the observation. Causes stem from the entity's poorly implemented internal controls, inconsistent application of policies and procedures, circumvention of internal controls, and/or other factors.

5. Discussion with the Entity's Management

The discussion section includes the auditor's communication of the observation to the entity's management or representative. The discussion should provide all of the information necessary to convey the auditor's observation, judgment criteria applied by the auditor, and potential causes and effect. The date of the communication, the name of the entity's management or representative, and the entity's response should be documented.

6. Conclusion

The conclusion should include the auditor's observations, criteria, description of cause and effect, and discussions with the auditor and the entity's management.

7. Recommendation

The recommendation includes a solution for the cause of the deficiency described in the observation. The recommendation should provide for an approach in resolving the deficiency by recommending specific changes to Policies and Procedures, identifying improvements to internal controls, or other functional changes.

The Engagement Point Sheet (EPS) can be located on the OIPA share drive.

525 SUPERVISION AND REVIEW

All OIPA's engagements must be adequately supervised to ensure that they are properly planned and performed in accordance with professional standards, this Policies and Procedures Engagement Manual, and other laws or regulations applicable to the specific engagement. Supervision is the responsibility of the IPA and the supervisor assigned to the engagement and includes:

- Providing on-the-job instruction and training to audit staff members to ensure that they adequately understand and properly perform their assigned procedures;
- Preparing and/or approving the required planning documents that provide staff assignments and budgeted hours, allocate resources, and establish an efficient and effective approach to the performance of the engagement;
- Staying informed of significant problems encountered by auditors during an engagement;
- Resolving technical differences of opinion among staff members; and
- Reviewing auditors' work to determine whether the objectives of the engagement and the results of the procedures performed were consistent with the conclusions presented in the report.

525.05 Supervisory Responsibilities

This section defines the supervisory responsibilities of audit management as they relate to OIPA's engagements.

525.10 Supervision During Engagement Planning

The audit supervisor and/or the IPA are responsible for ensuring that the engagement has been properly planned and that the required planning documents are complete and meet the requirements of GAGAS.

The audit supervisor must prepare (or review, if prepared by audit staff) all three required planning documents: the planning memorandum, the program, and the Assignment Information form. The audit supervisor should sign the planning memorandum and forward it, along with the program and the Assignment Information form, to the IPA for review. The IPA should review the planning documents to ensure that they are adequate and then sign the planning memorandum.

525.15 Supervision During the Engagement

The supervisor and/or the IPA is responsible for providing supervision and on-the-job training to staff members during the course of the engagement. The IPA must consider the training, ability, and experience of all staff members, not only when assigning procedures, but also when determining the amount of instruction and direction each staff member needs while performing his or her assigned tasks.

The IPA may delegate some on-the-job training duties to an audit supervisor; however, the IPA must ensure that the supervisor has sufficient knowledge and ability to provide such training. In addition, the supervisor must have sufficient time for training allocated in his or her budget (this allocation should be reflected in the Planning Memorandum). Although the IPA may delegate some duties to a supervisor, the IPA retains the responsibility for ensuring that adequate supervision is provided to all staff members on the engagement. The IPA should periodically discuss the audit progress with each individual staff member in order to ascertain whether the supervisor is providing adequate and proper on-the-job training. The IPA is responsible for staying informed about significant issues or problems that occur during the course of the engagement. The IPA should be accessible to staff members during business hours and should periodically contact staff to check engagement progress.

525.20 Technical Differences of Opinion

Following is the protocol for situations in which staff members are unable to resolve a technical difference of opinion.

- A difference of opinion among audit staff, including the lead person, should be brought to the audit IPA for resolution. Both the difference of opinion and its resolution must be documented in the working papers.
- A difference of opinion between the audit IPA and audit supervisor may arise. Both the difference of opinion and its resolution must be documented in the working papers.
- The IPA has final responsibility for ensuring that all differences of opinion are resolved and documented.

525.25 Consultation and Technical Resources

Audit staff members are advised to confer with their supervisor and/or IPA for program or technical guidance. For additional assistance, audit staff members should refer to professional auditing standards and other applicable regulations.

530 ENGAGEMENT REVIEW

All engagements performed by the OIPA should be adequately reviewed in accordance with this manual, professional standard, and/or other laws and regulations applicable to the engagement prior to the issuance of the report. The review(s) will be performed by a person with sufficient competence, experience, and responsibility appropriate for the type of engagement under review.

530.05 Review Guidelines

- All engagements performed under professional standards must have, at a minimum, (1) a supervisor's review and (2) an IPA's review completed prior to the issuance of the engagement report or letter.
- The supervisor's and IPA's review are documented by the (1) reviewer's initials, dating, and tick-marks on the individual working papers and (2) reviewer's completion of the required checklist corresponding to the engagement. The checklist must be signed and dated by the reviewer.
- Reviewers should initial and date only the working papers on which they have actually performed some level of review. There is no requirement that every page of the documentation package include a reviewer's initials; however, at minimum the initial and date should be noted on at least the first page of each scope sheet, all point sheets, and all summary sheets. As a general rule, a working paper with the reviewer's initials and date should also have at least one reviewer's tick marks.
- The reviewer should indicate with tick marks what actions he or she has performed on the individual working papers. In general, a checkmark next to cross-references indicates that the reviewer traced and agreed the reference to the indicated working paper. [Supplement 5A](#) provides a suggested tick mark legend. The reviewer should provide explanations for tick marks that deviate from the descriptions provided in Supplement 5A.
- The reviewer should complete and sign the checklist corresponding to the type of review performed. The reviewer must provide explanations for all "NO" responses to the questions in the checklists.

530.10 Use of Review Notes

Review notes are used by the reviewer to communicate specific issues found during the engagement review that require clarification and/or modification from the staff member who prepared or is responsible for the engagement documentation.

Review notes should be written on letter-size paper with space provided for the staff member to write down a response to each comment. It is not acceptable to write review notes on Post-it notes, or similar type note paper, as they are easily misplaced and do not provide adequate space for a proper response.

Staff members must respond to all review notes that are submitted to them by the reviewer. In response to review notes, the staff person should either make a change to the engagement documentation and/or provide an explanation to the reviewer on the review note itself. The staff member must notate his or her response, initials, and the date completed for each review note.

The reviewer must clear all review notes in order for any review to be considered completed. The reviewer should review the staff member's response and ensure that it adequately addresses the review note. The reviewer should draw a bar line vertically through the text of each review note to indicate that it has been cleared or another mark that is defined to show the review comment has been satisfied.

Review notes are to be removed from the engagement documentation package before the completed engagement file is stored. However, staff members should consider retaining personal copies of review notes they have received as a reference tool for future engagements.

530.15 Reviewing the Work of Audit Assistants

GAO professional standards 2018 Revision to the *Government Auditing Standards* - paragraph 5.37 require that “ The audit organization should assign responsibility for each engagement to an engagement partner or director with authority designated by the audit organization to assume that responsibility and should establish policies and procedures requiring the organization to a. communicate the identity and role of the engagement partner or director to management and those charged with governance of the audited entity and b. clearly define the responsibilities of the engagement partner or director and communicate them to that individual”.

An important element of this supervision is the audit supervisor’s and IPA’s review of the audit staff’s work papers.

Engagement documentation should clearly establish that the engagement work papers have been reviewed in sufficient detail as to provide:

- Substantiation that the planning, fieldwork, and reporting phases of the engagement have been conducted in accordance with professional standards;
- Guidance to audit staff to ensure that all accounting and auditing issues have been evaluated properly and technical differences of opinion are addressed and documented; and
- Support for the opinions, conclusions, and findings included in the engagement report or letter.

The work paper review involves various steps, including:

- Sign-offs on planning memorandums and related documentation;
- Reviewing point sheets, scope worksheets, detailed analysis worksheets, and draft and final versions of the engagement’s report;
- Use of supervisor and IPAs work paper review checklists; and
- Preparing work paper review or coaching notes.

535 REQUIRED REVIEWS FOR ALL ENGAGEMENTS

A supervisor’s and IPA’s review must be performed and completed on all OIPA engagements prior to the issuance of the engagement report.

535.05 Supervisor’s Review (detailed review of the engagement documentation)

The audit supervisor is responsible for the detailed review of the engagement documentation. The purpose of the detailed review is to determine that (1) all procedures in the program were performed and documented; (2) the results and conclusions reached are appropriate for the work performed; and (3) the results are properly summarized and in agreement with the report or letter to be issued.

Generally, the audit supervisor assigned to the engagement is the person who performs the review. However, under certain circumstances, such as when the assigned audit supervisor is not available to perform the review, the audit IPA can perform the first level review and the supervisor can perform the IPA’s review.

The supervisor’s review must be documented on the checklist corresponding to the type of engagement being performed. The signature on the checklist attests to the reviewer’s performance of the review and to the reviewer’s direct knowledge of the accuracy and correctness of all the responses to the questions contained in the checklist. A staff member who is not at or above the level of audit supervisor is not authorized to sign a Supervisor’s Review Checklist form.

535.10 IPA’s Review

The purpose of the IPA’s review is to determine that (1) the auditor complied with professional and firm standards; (2) accounting and auditing concerns for the auditee were evaluated properly; and (3) the overall results of the procedures performed are appropriate.

The IPA's review must be performed by a person at the level of supervisor or above.

The IPA's review must be documented on the IPA's Review Checklist form. This checklist applies to all engagement types. The signature on the checklist attests to the reviewer's performance of the review and to the reviewer's direct knowledge of the accuracy and correctness of all the responses to the questions contained in the checklist. A staff member who is not at a supervisor or above is not authorized to sign the IPA's Review Checklist form.

535.15 Independent Review of High-Risk Engagements

For engagements considered to be high-risk, the IPA will ensure that an independent review is performed prior to the issuance of the engagement's report or letter. The independent reviewer must be at or above the level of IPA and must have sufficient technical expertise and experience to perform the review.

The IPA is responsible for identifying those engagements considered to be high-risk; the IPA should consider, when making such a determination, whether:

- The OIPA has prior experience related to the particular program and/or auditee/entity;
- Significant dollar findings exist and/or if it is likely that there will be an appeal of findings;
- The report is being reissued;
- New or complex technical pronouncements are being applied for the first time; and
- Unresolved differences of opinion exist among engagement team members. The

independent reviewer will:

- Discuss with the IPA the significant audit matters or other matters related to the engagement, including identification of any high-risk findings, accounts, or transactions significant to the engagement;
- Discuss with the engagement team any matters that required consultation or research performed during the engagement and review documentation of these items:
- Read the report and/or financial statements to be issued; and
- Review the engagement documentation for accounts, findings, or conclusions that are significant and/or are considered high-risk.

The independent reviewer will document his or her review by completing and signing the Independent Review Checklist. It is not necessary for the independent reviewer to initial working papers. This independent review should be conducted after the audit IPA has completed his or her review of supporting documentation and report or letter.

540 ONGOING INVESTIGATIONS OR LEGAL PROCEEDINGS

Auditors should avoid interfering in ongoing investigations or legal proceedings involving fraudulent or illegal activity. The impact of any ongoing proceeding on the audit engagement should be assessed by the auditor or audit team. Laws, regulations, or policies may require the auditor to report such fraudulent or illegal activity to law enforcement (and oversight agency or organization) before performing additional procedures. It may be appropriate, based on communications with law enforcement, to withdraw or defer further work on the engagement. Initially, all potential fraud reported or identified shall be investigated by the IPA.

540.05 Documenting the Fraud Brainstorming and Risk Assessment

Government Auditing Standards states that the auditor should assess the risks that may result in material misstatements (errors) due to fraud and integrate this potential risk into the overall engagement's risk assessment process for examinations and in regard to performance reviews (*GAGAS 2018 (paragraph 8.71)*). Based on his or her assessment, the auditor is required to respond to the identified fraud risks.

To meet the standards, the auditor shall include as part of the planning phase for every engagement, a fraud brainstorming discussion conducted among engagement team members. The purpose of the brainstorming session is to provide a forum for the engagement team to discuss the potential for fraud and fraud risk factors that might be evident in their engagement.

The assessment of fraud risk requires the auditor to document:

1. How and when the brainstorming session occurred and who participated,
2. Procedures performed by the auditor to obtain information necessary to identify and assess fraud risk, including auditor’s inquiries of the entity’s management, employees, and internal audit staff, and results from analytical procedures performed by the auditor as well as other sources,
3. Specific risks of material misstatements due to fraudulent financial reporting or the misappropriation of assets, gathered from the auditor’s inquiries, analytical procedures and other sources, and
4. Auditor or audit team’s response to those risks in terms of additional engagement procedures. The Fraud Brainstorming Discussion form is located in the IPA’s share drive.

The Risk Assessment – Fraud Brainstorming Discussion form documents these essential steps and should be included in the engagement’s documentation. The auditor should complete the document’s five step approach in order to comply with the fraud risk assessment requirements.

This fraud assessment is an essential element of the auditor’s planned strategy to reduce engagement risk. In addition to completing the aforementioned form, auditors should assess fraud risk throughout the engagement phases. Auditors should evaluate whether engagement results or observations affect their fraud risk assessment.

545 ANALYTICAL PROCEDURES – CONCEPTS

Analytical procedures consist of an evaluation of financial information made by studying plausible relationships among financial and non-financial data. The applications of analytical procedures rely on an expectation that a relationship exists between the data under review. This relationship would continue to exist barring any unforeseen conditions. Analytical procedures are used in the following circumstances:

- To assist the auditor in planning the nature, timing, and extent of other auditing procedures;
- As a substantive test (test of details) to obtain audit evidence to support an assertion or conclusion; and
- As a final overall review of financial information contained in financial statement. Planning

the Audit

Analytical procedures used in planning the audit should focus on the auditor’s understanding of the audited entity’s business operations, transactions, and events that have occurred within a specified period (months or years). This understanding will help the auditor identify areas that represent underlying risks relevant to the audit.

Example - Schedule of Accounts

Account Name	Current Year	Prior Year	Change	% Change
Personnel Services	\$ 2,500,000	\$ 2,175,000	\$ 325,000	15%
Cost of goods sold	1,780, 000	1,566,000	214,000	14%
Selling Expense	230,000	184,000	46,000	25%
Inventory	1,000,000	832,000	168,000	20%
Accounts Payable	498,000	437,000	61,000	14%

In the example above, the auditor prepares the schedule using the general ledger or an unaudited working trial balance. Based on historical information, the auditor expects that selling expense (year over year) increases did not exceed 15%. In this example, the year over year selling expense increase was 25%. The auditor would include in the planning strategy a review of selling expense.

Substantive Tests (Tests of Details)

The auditor may rely on substantive tests, the application of analytical procedures, or a combination of both in achieving the audit objective. The type of analytical procedure to apply will be based on auditor's judgment regarding the procedure's effectiveness and efficiency in meeting the audit objective. An example of an analytical procedure used as a substantive test is illustrated in the supplement section located at the end of this chapter.

Overall Review

The objective of analytical procedures used in the overall review is to assist the auditor in assessing the conclusions reached, disclosures, and presentations in a financial statement. This overall review would result in the auditor reading the financial statements and notes and investigating any unexpected variances in the statement's account balances. Results from the overall review may indicate that additional evidence is needed.

Documentation Requirements

The auditor should document the following as part of the analytical procedure review process:

1. The expected result from applying the analytical procedure and the factors considered in its development.
2. The results from a comparison of expected amounts to recorded amounts or ratios.
3. Additional auditing procedures applied in response to significant unexpected differences arising from the application of analytical procedures.

550 FINALIZATION OF ENGAGEMENT DOCUMENTATION AND SUBSEQUENT CHANGES AFTER THE REPORT IS ISSUED

All engagement documentation must be completed, assembled, reviewed and finalized within 60 calendar days from the date of the final report. Circumstance may arise after the final report is issued that will require the auditor to modify the engagement documentation and report.

550.05 Changes in Engagement Documentation after Issuance of the Report or Letter

Periodically, the auditor(s) may be required to change engagement documentation after the date of issuance of the draft or final report or letter. Generally, these changes result from the consideration of additional information obtained from the audited entity or the auditor(s) performance of additional procedures. These changes in engagement documentation include any addition, substitution, or editing of documentation, including, but not limited to, physical or electronic additions to any engagement documentation file or preexisting engagement documentation.

When such changes are made to the engagement documentation, the auditor(s) and IPA should undertake the following specific steps to maintain documentation integrity:

- Provide the identity of the person(s) making the change, and identity of any person(s) approving the change.
- Provide the date of the change.
- Provide the reason for the change, if the reason is other than the assembling of pre-existing documents.
- Keep the original documentation intact within the engagement documentation file and not be deleted.

- Notations on the original documentation should indicate that worksheet components have been revised or that the entire worksheet has been superseded by a subsequent worksheet.
- Prepare a reconciliation worksheet to identify material changes in findings or conclusions reported between draft and final (or final and revised final) reports or letters issued to the entity.

The documentation that is changed should contain sufficient detail to enable a reviewer with relevant knowledge and experience, having no previous connection with the engagement, to understand the nature, timing, reason for, and extent of the change.

Finalization of Engagement Documentation – 60 Calendar Days

After the engagement final report or letter date, but before the end of 60 calendar days, updated or revised engagement documentation may be added. However, the documentation must contain all the information, evidence, and conclusions that were in the original or superseded documentation. If the information, evidence, or conclusion is no longer relevant, it need not be retained.

During the finalization of engagement documentation period, the auditor is allowed to make changes to the engagement documentation to:

- Complete the documentation and assembly of evidence that has been obtained prior to the report date or letter;
- Add original documentation that was originally faxed prior to the report date or letter; and/or
- Perform routine file assembly work such as sorting and cross-referencing work papers and sign offs on documentation checklists.

After the 60-day documentation finalization date, engagement documentation must not be deleted or discarded prior to the five-year or as required documentation retention period.

Note: Material changes to engagement findings or conclusions subsequent to the issuance of the final report or letter should be reported in a revised final report or letter.

550.10 Procedures Performed or Evidence Obtained Determined to be Inadequate

In certain circumstances, the engagement's management or auditors may determine that evidence obtained will not support the final report. These circumstances may arise because an engagement procedure was not performed, or new information comes to the auditor's attention.

If the auditor determines that the omitted engagement procedure is significant, the omitted procedure or alternative procedure should be performed. If procedures cannot be performed, the engagement's management should determine the proper course of action to be taken. This course of action may require that the audit organization notify entities, organizations, or person (s) known to rely on the engagement's report or letter of the omission and the possible effect on the report or letter.

550.15 Letter of Inquiry

A letter of audit inquiry to the entity's attorneys is the primary communication in corroborating information gathered from the entity regarding any litigation, claims, and/or assessments. The matters that should be covered in the letter include the following:

1. Identification of the audited entity and the date of the audit
2. A list prepared by the entity that describes and evaluates any pending litigation, claims, and assessments
3. A list prepared by the audited entity that describes and evaluates any claims and assessments that have a probability to be asserted against the entity
4. A request that the attorney furnish additional information on the items listed in 2 and 3 above, an evaluation of the likelihood of an unfavorable outcome and an identification of any omitted pending litigation, claims or assessments

5. A statement in the inquiry that asserts the entity's understanding that the entity's attorney has formed a professional conclusion that any unasserted claim or assessment should be disclosed or considered for disclosure in the financial statements
6. Request to the attorney to identify any limitations of his or her response

In addition to sending the letter of inquiry, the auditor should consider the applying other auditing procedures to corroborate the entity's assertion of pending litigation, claims, and assessment. For example, the auditor may need to inspect the following:

- Board minutes of meetings
- Contracts and/or loan agreements
- Correspondence from governmental entities

555 INTRODUCTION – AUDIT SAMPLING

Audit sampling involves reviewing less than 100% of the items within a specific group or population of account balances or classes of transactions in order to evaluate a characteristic. Auditors may find it feasible to collect information about all of the items when the population is small, allowing them to eliminate any sampling or inferential problems.

As the population is often too large to examine all of the items, auditors must examine a sample of items. The sample must be representative—that is, typical of the population—in order for the auditor to prepare valid statistical inferences. This section provides basic requirements and selective applications of audit sampling. Auditors requiring more technical applications of audit sampling techniques should refer to the AICPA Audit Sampling Guide.

555.05 Authoritative Literature

The following references provide guidance on how to apply sampling when auditing:

- AICPA *Codification of Statements on Auditing Standards (AU)*
- AICPA Audit Guide – *Audit Sampling March 1, 2012*. The Audit Guide is considered an interpretative publication providing recommendations on the application of Generally Accepted Auditing Standards.
- SAS 111 (Amendment to Statement on Auditing Standards No. 39, Audit Sampling)

When auditors do not follow the recommendations contained in the AICPA sampling guide, they should be prepared to explain how they complied with the requirements of SASs 39 and 111.

555.10 Concepts

In applying sampling methodology, auditors should consider the concepts described below.

In a statistical sample, the sample size is based on the rules of probability. This scientific and mathematical approach offers a means of measuring the sufficiency and competency of the evidence obtained and objectively evaluating results.

Non-statistical (nonrandom) sampling does not provide a means for generalizing the results to the population. Non-random samples (where the probability of selecting a particular item is not known) may help the auditor gain insight into a problem or explore some initial relationships between the sample and the population from which the sample was taken. However, non-random samples are not good for verifying or testing hypotheses and issues because they are subject to selection biases and inaccurate generalizations.

Statistical and non-statistical sampling requires the auditor to use judgment in planning the sample, selecting the sample, performing tests on the sample, and evaluating the results.

Statistical sampling is a sampling approach that has the following characteristics:

- Random selection of the sample items; and

- The use of an appropriate statistical techniques to evaluate sample results, including a measurement of sampling risk

A sampling approach that does not have these characteristics is considered a non-statistical sample.

555.15 Definition of Audit Sampling Risk

Audit sampling risk is the risk that the auditor will reach an incorrect conclusion because the sample is not representative of the population, resulting in a sampling error. Audit sampling risk is an inherent part of sampling that result from testing less than the entire population.

This chapter will emphasize audit sampling in the auditor's application of test of controls and tests of details (substantive tests). For the test of controls, the auditor's sample risk is the erroneous conclusion that the internal controls are more effective than they actually are. Based on the erroneous conclusion, the auditor relies on the entity's internal controls, and he or she reduces the amount of substantive tests. This will affect the audit effectiveness, as the control risk is understated.

For the tests of details, the auditor is concerned with the sampling risk of erroneous conclusions in which material misstatements (errors) are thought to not exist in the population, when in fact they do exist. This may lead to an inappropriate opinion expressed on the financial statements or incorrect conclusion in regard to the population's account balances and transactions.

The auditor can reduce sampling risk by increasing the sample size and using the appropriate method in selecting the sampling items. Refer to [Supplement 5E](#) for a summary of sampling risks.

555.20 Methods of Sampling Selection

The objective of sampling for the auditor is to determine whether a characteristic of interest is evident in a population. The auditor must select the best sampling methodology to provide for a sample that is representative of the population (i.e. each item in the population has an equal chance of being selected). The use of the specific sampling methodology is a matter of auditor's judgment, with the understanding that sampling methodologies have different attributes and may not provide an adequate sample representation of the population.

Block Sampling

Block sampling is a non-statistical sample approach that selects all items in an (auditor- determined) time period, in a numerical or alphabetical sequence. For example, the auditor would select 100 sequential checks, or all checks for a period of time (week, month). This technique may require a subset sampling plan for the time period being selected. Block sampling also does not lend itself to being representative of the population.

Haphazard Sampling

Haphazard sampling is a non-statistical sample method that consists of sampling units selected without any conscious effort to include or exclude an item from selection. The auditor's sample would not isolate large, unusual, convenient, or small items for selection. The auditor's expectation is that the selection would be representative of the population.

Simple Random Sampling

Simple random sampling is a statistical and non-statistical approach in selecting a sample using random numbers generated by tables or computer software and matching those numbers with document numbers.

Systematic selection sampling is an approach in which a sample that is selected based on a predetermined interval using a population and a desired sample size. For example, if the population size contains 1000 items, and the auditor's desired sample size is 100, the auditor would pick every 10th item (1000/100) using a

random start. A known pattern or trend within the population would prevent the selected sample from being representative unless the auditor used two or more random starting points.

Stratified Selection

Stratified selection is a sample technique applied by grouping sampling units with similar characteristics into separate strata in order to minimize variability among sampling units. For example, if the auditor wants to sample accounts receivable, he or she may stratify (set aside) large dollar receivables in which each item will be selected for testing. This selection method does not provide for a representative sample. However, a stratified selection method can be used in conjunction with another random sample selection method.

Probability Proportional to Size

Probability proportional to size is a sample method that selects items from a population in proportion to the item's recorded monetary amount. This methodology emphasizes large dollar items.

555.25 Tests of Controls Using Audit Sampling

The purpose of a test of controls is to provide evidence about the operating effectiveness of controls. The auditor may anticipate placing his or her reliance on those controls and supporting the level of control risk.

When using sampling in a test of controls, the auditor is concerned as to whether prescribed controls were performed, how they were performed, and by whom were they performed. For example, if the auditor wants to place reliance on monitoring controls over employee time sheets, he or she may be interested in the number of approving supervisor's or IPA's signatures on the timesheets, which indicate controls validating that work time information in the time record was reviewed and deemed accurate. In this circumstance, the auditor would want to sample monthly timesheets from a specified population and observe the number of occurrences that an approving signature was evident on a sampled timesheet. In this case, the auditor is applying an attribute sampling technique that is directed at identifying the rate of occurrence of a specific attribute (control procedure) in a population. The auditor can then determine whether the control procedure was in effect assuming that the same control feature was consistently applied throughout the population.

555.30 Documentation of Sampling Procedures – Test of Controls

In using either a statistical or non-statistical sampling approach, the auditor should document the following sampling plan considerations:

- 1 Description of the Internal Control to be Tested
The description should identify the specific internal control (s) the auditor will test in order to provide support for an assessed level of control risk.
- 2 Sample Test Objectives
The auditor should document the sample test objective, i.e. what is to be inferred by sampling the population and what assertions are being tested.
- 3 Defining the Deviation Conditions
A deviation is a departure from an expected performance of prescribed internal control. The performance of a control consists of all the steps necessary to support the auditor's level of control risk and planned reliance on the prescribed control. For example, in the test of controls for payment authorizations, the

auditor's expectation is that all paid invoices have evidence of an approving signature. The lack of an approving signature detected by the auditor during the sample of invoices would constitute a deviation from prescribed internal controls.

4 Defining the Population

The population should be defined to include account balances, or transactions, and the period covered by the test. A discussion on how the auditor determined that the population is complete should be documented.

5 Defining the Sampling Unit

The sampling unit should be defined. In a test of controls, the sampling unit is a document or a line item or entry in an accounting record that provides evidence of an operation of an internal control(s). For example, the auditor may want to test the authorization controls for the payment of vouchers. The auditor would consider the voucher as the sampling unit. However, if the voucher is used to pay multiple purchases involving multiple lines, the auditor would consider the individual line purchase as the sampling unit; if not all line items are going to be tested for the control.

6 Method for Selecting the Sample

For both statistical and non-statistical sampling, the sample is expected to be representative of the population. The selection methodology should employ the process such] that all items in the populations have an opportunity to be selected. [Section 555.20](#) of the manual describes the various sample selection methodologies.

7 Determining the Sample Size

In a non-statistical sampling approach, the auditor will use his or her estimates in determining the sample size. However, the auditor should take the following into consideration in determining sample size:

- Risk of overreliance of controls: The lower the acceptable risk of overreliance of internal controls, the larger the sample size is needed.
- Tolerable rate of deviations: The lower tolerable rate of deviations the auditor is willing to accept, the larger the sample size is needed.
- Expected population deviation rate: The rate of deviations estimated by the auditor based on prior knowledge or a previous sample.

In a statistical approach, the auditor should use the Attribute Statistical Sampling Tables illustrated in the AICPA Audit Sampling guide, Appendix A.

8 Identification of the Sample Units

Engagement documentation should include an identification or separate listing of the transactions or account balances selected in the sample. Documentation should show the relationship of the selected sample to the population from which it was taken.

9 Determining the Tolerable Rate of Deviation

The tolerable rate of deviations is the maximum rate of deviations the auditor is willing to accept without altering the planned level of control risk. Two factors determine the degree of the tolerable rate of deviations

- Planned level of control risk; and
- Level of assurance obtained from sample's audit evidence.

The higher level of control risk, the less assurance is needed by audit evidence from the sample by the auditor. The higher level of control risk, the lower rate of deviations is expected from the test of controls.

10 Evaluating the Sample Results

The auditor documents the results, including the identification of the samples' internal control deviations, and the rate of deviations from the sample (number of observed deviations divided by the sample size). The auditor should explain possible reasons for the deviations from controls and the auditor's conclusion on the planned reliance on the specific internal controls. If the auditor determines that the test of controls do not provide a basis for reliance, then the conclusion should indicate that additional tests of controls or the application of substantive procedures is necessary in order to address audit risk.

For the tests of controls, the sample's deviation rate is considered the projected deviation rate for the population.

555.35 Sampling in the Substantive Test of Details (Substantive Tests)

The purpose of substantive tests of details of transactions and balances is to detect material misstatements (material errors) in the account balances or class of transactions. The auditor's risk is that the financial statements will contain material misstatements after he or she has applied auditing procedures. Using audit sampling in substantive test of details provides the auditor with evidence regarding the reasonableness of the amounts recorded in the transactions and account balances and a basis for determining whether the financial statements are free from material misstatements.

555.40 Documentation of Sampling Procedures – Test of Details

In substantive tests, the auditor should document the following in the engagement:

1 Objectives of the Test

The objective of the tests (i.e. to reduce the risk of material misstatements for an account balances or class of transactions) and the related assertions should be documented. Assertions are the declarations derived from the audited entity's management regarding the nature of the class of transactions, account balances, and disclosures presented in an entity's financial statement.

2 Defining the Population

The population consists of the items constituting the account balances or class of transactions subject to audit sampling and the period covered by the test. The documentation should include a determination that the population under consideration is complete and not a subset of the population. Items that the auditor has determined to test 100% (high dollar amount, high risk of misstatement) are not considered part of the population.

3 Defining the Sampling Unit

The sampling unit is the individual item that constitutes the population. This includes customer account balances, invoices, cancelled checks, individual expenditure transactions, etc.

4 Method for Selecting the Sample

For both statistical and non-statistical sampling, the sample is expected to be representative of the population. The selection methodology should employ a process in which all items in the populations have an opportunity to be selected. [Section 555.20](#) of the manual describes the various sample selection methodologies

5 Determining the Sample Size

In a non-statistical sampling approach, the auditor will use his or her estimates in determining the sample size. However, the auditor should take the following into consideration in determining sample size:

- Risk of Incorrect Acceptance: The lower the acceptable risk of incorrect acceptance, the larger the sample size is needed.
- Tolerable Misstatements (amount): The lower tolerable rate of deviations the auditor is willing to accept, the larger the sample size is needed.

- Expected misstatement: The amount of misstatement estimated by the auditor based on prior knowledge or a previous sample.

6 Defining the Misstatement

The types of errors in the account balances and class of transactions (and disclosures) may include:

- Differences between recorded and actual amounts
- Omissions of financial amounts or disclosures
- Misclassifications of accounts

7 Definition of Tolerable Misstatement

The amount of monetary misstatement in the test of account balances and classes of transactions the auditor willing to accept without causing the financial statements to be materially misstated.

8 Evaluation of the Sample

The evaluation should address a summary of the overall sampling conclusion, including a description of the items selected for testing and an analysis of the misstatements identified in the sample.

Depending on the objective of the engagement, the auditor should project the results of the audit sampling to the population. Note that there are several methods the auditor can use to project the amount of misstatement found in a statistical or non-statistical sample to estimate the amount of misstatement in a population.

555.45 Alternatives to Audit Sampling

In certain circumstances, an auditor may apply audit methods that are not, by definition, sampling. Such circumstances may include the following:

- When applying an audit procedure limited to a specific group of items within a balance or class of transactions that have a distinct characteristic (e.g., all capital expenditures over a certain dollar amount);
- When examining a few transactions within a balance or class of transactions to gain an understanding of the entity's operations; or
- When applying an audit procedure to one or more transactions to clarify the auditor's understanding of an entity's internal control design.

In each case identified above, the purpose of the test is not to reach any conclusion that applies to the entire account balance or class of transactions. Therefore, the auditor would not have to follow the audit-sampling guidance in SASs No. 39 and 111.

560 DOCUMENTATION CONSIDERATIONS

Auditors should be cognizant of the following documentation considerations.

560.05 Documentation Ownership and Confidentiality

Engagement documentation is the property of the OIPA Audits and all information obtained from the entity is considered confidential. Staff members should safeguard engagement documentation at all times to prevent unauthorized access.

- The auditor should not show engagement documentation to the entity or other persons outside the OIPA during the course of fieldwork or prior to the release of the report or letter. This guideline, however, does not prohibit the auditor, after consultation with the audit IPA, from providing responsible entity officials

with data from the working papers that will allow these officials to respond to either possible findings disclosed during the engagement or actual findings included in the draft report or letter

- The auditor should not leave engagement documentation unattended where it might be accessible to the public, entity personnel, or others who do not have the right to examine it. Also, staff shall take the necessary steps to protect documentation from scrutiny, theft, damage, or loss. The auditor should also ensure security of the working papers at all times, including at audit sites, offices, in automobiles, and in hotel rooms.
- The auditor should safeguard private information contained in documentation, such as Social Security numbers, medical information, and other information protected by privacy laws. The extent and nature of safeguarding is based on auditor judgment; however, the auditor should, at a minimum:
 - Note “Confidential” on both the working paper containing private information and on the corresponding item in the Index.
 - Minimize the number of times confidential information is presented in the documentation. Consider using a master listing that assigns a record number to each confidential item and cross-referencing to the master listing whenever necessary.
- The audit IPA must approve all requests from outside parties to access engagement documentation.

The auditor should be aware that information received from the entity or outside third parties may contain subject information that may be protected under various federal or state regulations or may be proprietary to a business operation. For example, the U.S. Department of Health and Human Services (HHS), under its Privacy Rule, regulates and protects certain health information with regards to how it can be used and disclosed. HHS issued the privacy rule to implement the requirement of the Health Insurance Portability and Accountability Act of 1996 (HIPAA). Under this privacy rule, health information that relates to:

- The individual’s past, present, or future physical or mental health or condition;
- The provision of health care to the individual; or
- The past, present, or future payment for the provision of health care to the individual. This information is protected from public disclosure without the consent of the specific individual or specific allowances under the privacy law. Included under this privacy rule is any information that may identify an individual—e.g. name, address, birthday, and Social Security number.

Proprietary information is information a private business or company wishes to keep confidential. Proprietary information may include trade secrets, processes and methods used in production, marketing plans, salary structure, customer lists, contracts, and details of its computer system. Public disclosure of such information may be detrimental to the business or company.

During the entrance conference, the auditor should discuss with the entity whether certain documents may contain confidential or sensitive information if such records are not clearly marked. The auditor may also discuss whether such documents can be photocopied or scanned and be included in the audit documentation.

Auditors should use extreme care in labeling such information as confidential in the engagement documentation and limiting access to such information. It may be prudent for the auditor to redact such information in the engagement documentation, either through a manual process or electronically.

An additional concern is safekeeping of all electronic, photographic, and hardcopy media (e.g. flash drives, disk drives, and external hard drives) and paper documents containing confidential or sensitive information. Such information should be physically protected from unauthorized use, loss, or theft. All media containing confidential or sensitive information must be secured (e.g. kept in a locked room, drawer, or cabinet) when not in use or unattended.

560.10 California Public Records Act

The California Public Records Act (CPRA) is designed to give the public access to information that is in possession of public agencies. All state and local agencies are required to comply with this act and provide public records that would include all communications (paper, magnetic, media, and electronic form) related to public business. Engagement documentation, related issued reports, and supporting documents (relating to the ordinary course of business) are subject to CPRA.

Certain information is *exempt from disclosure under this act*, including, but not limited to, the following:

- Preliminary drafts, notes, and memos if they are not retained in the ordinary course of business;
- Home addresses;
- Records concerning pending agency litigation; and
- Personnel, medical, and similar documents.

Public records containing partial information that may be considered exempt may still be required to be provided under CPRA. Exempt information should be segregated or redacted from the public record if such measures are feasible and are not unduly burdensome.

When possible, records deemed subject to disclosure should be provided at the time the agency will comply with the request. If this is not possible, the agency must provide the records within a reasonable period of time.

Auditors receiving these requests should immediately forward them to the audit IPA for further action. SANDAG's legal counsel will make the determination as to whether the request is subject to CPRA.

Public requests for records under the federal Freedom of Information Act should be handled in a similar manner.

Considerations

Auditors should notify the audited entity's management that the published report and supporting documentation are subject to the disclosure requirements of the CPRA. Auditors should disclose this at the formal entrance and exit conferences with the entity management and in the entrance or engagement letter.

560.15 Documentation Storage and Retention

Within 60 calendar days from the date of the final audit report or letter, the assigned auditor must ensure that the completed (hard copy) documentation is submitted to the file storage where it is locked and maintained for the required time, according to the record retention policies.

560.20 Permanent Files

A permanent file is used by auditors to assemble certain types of documentation that will be used for future engagements. Permanent files are kept separate from the engagement documentation file. Examples of the documentation to be kept in the permanent file include:

- Articles of Incorporations/bylaws/Ordinances
- Internal Control Questionnaires, flowcharts and narratives
- Long term contracts i.e. lease agreements
- Organizational Charts
- Chart of Accounts

Whether a specific engagement program uses a permanent file depends on its need to retain documentation for ongoing engagements and to maintain a record or chronology of events pertaining to an audited entity. One use of the permanent file may be to document the auditor's initial review of an entity's internal control that will be used as a reference for subsequent internal control reviews. If the permanent file is to be used, it should follow the seven-year documentation-retention policy.

STANDARD TICK MARK SYMBOLS AND EXAMPLE LEGEND

The following legend illustrates several standard tick mark symbols that staff members can use when preparing engagement documentation. In the engagement documentation, **all tick mark symbols should appear in red.** Tick mark legends should be clearly labeled and should appear on every individual working paper that contains tick mark symbols (or a reference to the working paper containing the legend).

Illustrative Tick Mark Legend:

<u>Symbol</u>	<u>Example of Explanation</u>
√	= Agrees to (attribute #1) as defined by auditor.
√ ↘	= Agrees to (attribute #2) as defined by auditor.
И	= Footed
И	= Cross-footed
PY	= Traced and agreed to prior year's working papers.
R	= Reconciled to (auditor defined attribute including w/p reference)
= or ≠	= Equals to (or) does not equal to
Σ	= Sum of
① to ⑨	= Auditor defined
∫	= Auditor defined
θ	= Auditor defined
Ω or Ū	= Auditor defined
Υ	= Auditor defined
† or ‡	= Auditor defined
¶	= Auditor defined

Analytical Procedures – Trend Analysis Example

An analytical procedure can be used as the principal substantive test of a significant financial statement assertion when the procedure is the primary audit evidence. The following example documents a substantive analytical procedure that is the primary test of the account balance.

County of Los Angeles
Sanitation Department
Personnel Expense Analysis

Account Description	Amount as of 6-30-2008	Amount as of 6-30-2009	Change	Percent Increase or (decrease) over prior period
Personnel Expense	\$ 345,960	\$ 289,795	\$ (59,155)	(17.0)

Source:

County of Los Angeles expenditure reports for fiscal year-end 2008 and 2009.
 Interviews with the county's sanitation personnel.

Purpose:

To conduct an analytical procedure to determine the reasonableness of personnel costs for the county's sanitation department for fiscal year-end.

Scope/Procedures:

Compiled staffing and service equipment usage information from interviews with county's sanitation personnel.

Prepared analysis using fiscal year amounts for sanitation personnel costs. Calculated the difference in personnel costs (and percent) between fiscal-year amounts.

Calculated the expected personnel costs and compared to the actual difference between amounts and analyzed difference.

Conclusion:

We noted during our discussion with the auditee regarding its operations that the sanitation department switched from three-crew trucks to two-crew automated trucks for garbage collection. The county has six crews and did not change the number of crews. We noted from our review of the governing board minutes and newspaper and other media accounts that the sanitation department switched to new trucks, and the layoff of six county personnel occurred midway through the year. The average wage per city employee was \$19,220 last year, and we noted from our review of payroll and personnel records that there were no salary increases in the sanitation department during the year. Thus, our expectation is that personnel expenses would decrease by one-sixth (one-third times one-half) or \$57, 600 (\$345,960 times one-sixth) from that of the prior year as follows:

Prior year expense (18 personnel @ 19,220)		\$345,960
Current year expected expense		
18 personnel @ 19,220 X 50%	\$ 172,980	
12 personnel @ 19,220 X 50%	115,320	
		288,300
Current year recorded expense		289,795
Difference		\$1,495
Expected decrease		
Expected decrease		\$57,600
Actual decrease		59,155
Difference *		\$1,495

Based on the above analysis, personnel expense appears reasonable and no further work in this account balance is necessary

*Assumption that difference falls within the auditor’s materiality and tolerable error amounts.

Note: Documentation of the expectation and factors considered in its development is required in analytical review procedures. Additionally, auditors are required to document the results of comparing recorded amounts and any additional procedures to address significant unexplained differences.

ILLUSTRATION: NONSTATISTICAL SAMPLE—TEST OF BALANCES ¹**Objectives of the Audit Test and Defining Population**

Sarah Jones of Jones and Co. designed a non-statistical sample to test the existence and gross valuation of the December 31, 20XX accounts receivable balance of Short Circuit, Inc., an electrical supply company that is a new client of Jones and Co. For the year ended December 31, 20XX, Short Circuit had sales of approximately \$25 million. As of December 31, the company had 905 accounts receivable, with debit balances aggregating \$4.25 million. These balances ranged from \$10 to \$140,000. The company also had 40 credit balances aggregating \$5,000.

Assessing Tolerable Misstatement and Expected Misstatement

Sarah Jones made the following determinations:

- The results of her tests of controls supported an assessed level inherent and control risk of slightly below the maximum for assertions of existence and gross valuation of accounts receivable.
- The preliminary assessment of overall planning materiality is \$187,500, and known and likely misstatement is estimated to be \$62,500; thus, tolerable misstatement is \$125,000. Of the \$62,500, Sarah expects a \$35,000 misstatement of accounts receivable.
- The credit balances in accounts receivable would be tested separately as accounts payable.
- The balance for each selected customer would be confirmed.

Jones obtained additional information, as follows:

- The population contained five balances of more than \$50,000, which totaled \$500,000. Jones decided to examine these five balances 100% and exclude them from the population to be sampled. The population also contained 900 other debit balances, which totaled \$3.75 million.
- Through analytical procedures, Jones obtained reasonable assurance that all shipments were billed and that no material understatements of receivables existed.

Jones performed no other substantive procedures on the assertions of existence and gross valuation of accounts receivable (with the same objectives as confirmation).

Determining the Sample Size

Considering the following factors, Jones determined the sample size.

- *Variation in the population.* Jones separated the population into two groups based on the recorded amounts of the items constituting the population. The first group consisted of 250 balances equal to or greater than \$5,000 (total recorded amount of \$2.5 million) and the second group consisted of the remaining balances that were less than \$5,000 (total recorded amount of \$1.25 million).
- *Assurance factor.* Jones used the non-statistical sampling table to arrive at a 2.7 assurance factor. She selected this factor based on an assessed level of inherent and control risk slightly below maximum and because she did not plan any other substantive test to achieve the same objectives.
- *Tolerable misstatement.* As indicated previously, the amount of tolerable misstatement adjusted for expected misstatement was determined to be \$125,000.
- *Estimated misstatement.* Jones considered expected misstatement in developing tolerable misstatement as described previously.

Jones used the following non-statistical formula to estimate sample size.

$$\frac{\text{Population (less individually tested amounts)}}{\text{Tolerable misstatement}} = \frac{\$3,750,000}{\$125,000} \times 2.7 \text{ (Factor)} = 81 \text{ accounts}$$

Jones also decided to divide the sample between the two groups in a way that was approximately proportional to the recorded amounts of the accounts in the groups. Accordingly, she selected 54 of the 81 customer balances from the first group (balances with recorded amounts equal to or greater than \$5,000) and the remaining 27 customer balances from the second group (balances with recorded amounts under \$5,000).

Evaluating the Sample Results

Jones mailed confirmation requests to each of the 81 customers whose balances had been selected and to each of the five customers selected in the 100% examination group. Customers completed and returned to her 71 of the 86 confirmation requests. She was able to obtain reasonable assurance through alternative procedures that the 15 customer balances that were not confirmed were bona fide receivables and were not misstated. Of the 71 responses, only three customers indicated that their balances were overstated. Jones investigated these balances further and concluded that they were, indeed, misstated. She determined that the misstatements resulted from ordinary misstatements in the accounting process. The sample was summarized as shown in Table 1.

Table 1

Group	Sample Summary			Amount of Over-statement
	Recorded Audited	Recorded Amount		
	Amount	Sample	Sample	
100% examination	\$ 500,000	\$ 500,000	\$ 499,000	\$ 1,000
Over \$5,000	2,500,000	739,000	732,700	6,300
Under \$5,000	1,250,000	62,500	61,750	750
	\$4,250,000	\$1,301,500	\$1,293,450	\$ 8,050

Jones observed that the sample included 29.56% of the dollar amount of the over-\$5,000 group but only 27.00% of the items included in that group. She also observed that the sample included 5% of the dollar amount of the under-\$5,000 group but only 3.86% of the items included in that group.

On the basis of the above computations, Jones believed that the two methods of projecting sample results described in this section might yield different results. She considered the misstatements found and concluded that the amount of misstatement in the population was more likely to correlate to the total dollar amount of items in the population than to the number of items in the population. Therefore, Jones separately projected the amount of misstatement found in each group of the sample by dividing the amount of misstatement in the group by the fraction of total dollars from the population group that was included in the sample.

For the over-\$5,000 group, Jones had calculated that the sample included 29.56% ($\$739,000 \div \$2,500,000$) of the group’s recorded amount. She projected the sample results for that group to the population by dividing the amount of misstatement in the sample by 29.56%. She calculated the projected misstatement to be approximately \$21,300 ($\$6,300 \div 29.56\%$). Similarly, Jones calculated that the sample for the under-\$5,000 group included 5% ($\$62,500 \div \$1,250,000$) of the group’s recorded amount and that the projected misstatement was \$15,000 ($\$750 \div 5\%$).

Therefore, the total projected misstatement from the items sampled was \$36,300 ($\$21,300 + \$15,000$). Management of Short Circuit, Inc., agreed to correct the known misstatements of \$7,050, resulting in a remaining projected misstatement of \$29,250.

Jones compared the projected misstatement from the items sampled (\$29,250) with her \$35,000 expectation of misstatement of accounts receivable and decided that the results were as she expected. She then compared the total projected misstatement of \$29,250 with the \$125,000 tolerable misstatement and

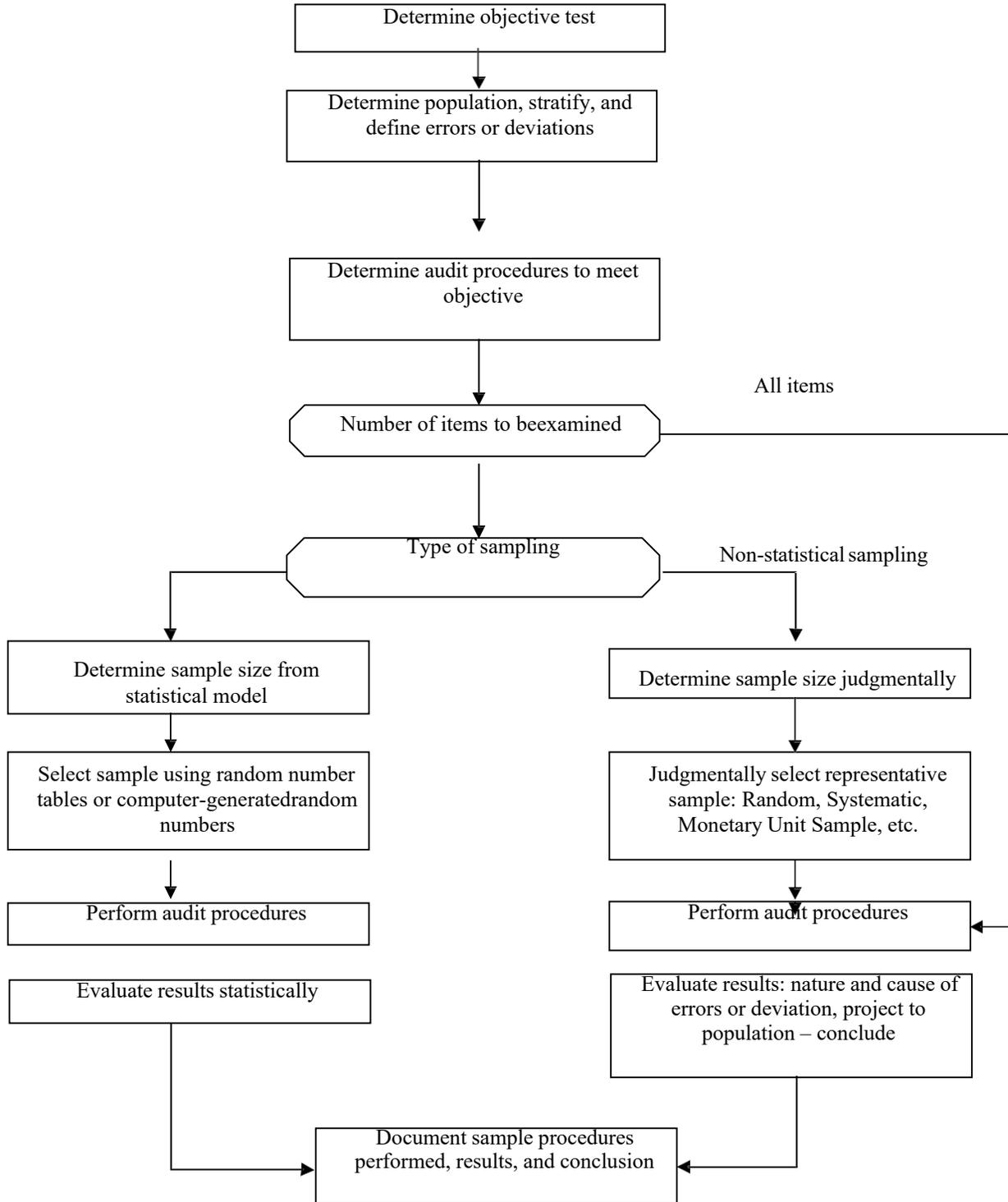
decided that an acceptably small risk existed that she would have obtained the sample results had the recorded amount of the accounts receivable balance been misstated by more than the tolerable misstatement (of \$125,000). In other words, even the addition of a reasonable allowance for sampling risk to her projected misstatement would not have resulted in a total exceeding tolerable misstatement. Jones investigated the nature and cause of the misstatements and determined that, as they resulted from clerical error, they were not indicative of additional audit risk.

Jones concluded that the sample results supported the recorded amount of the accounts receivable balance. However, she did aggregate the projected misstatement from the sample results with other known and likely misstatements to evaluate whether the financial statements taken as a whole might have been materially misstated. The items she examined 100% were not subject to sampling. Therefore, any misstatements from these items represented known misstatements. Because Short Circuit, Inc., agreed to correct the \$1,000 misstatement, Jones concluded that she had no need to consider these items in evaluating whether the financial statements taken as a whole may have been materially misstated.

¹ Adapted from the AICPA Audit Sampling Guide, Nonstatistical Sampling Case Study.

SUPPLEMENT 5D

**SAMPLING
STATISTICAL VERSUS NON-STATISTICAL**



The flowchart displays the basic steps in audit sampling using statistical and non-statistical approaches.

SUPPLEMENT 5E

SAMPLING RISKS

Procedure	Sampling Risk	
<p>Test of Controls – An audit procedure designed to evaluate the operating effectiveness of controls preventing, detecting or correcting material misstatements (errors) at the assertion level</p>	<p>Risk of Overreliance – The risks that the sample supports the conclusion that internal controls are more effective than they actually are.</p>	<p>Risk of Under Reliance – The risk that the sample supports the conclusion that internal controls are less effective than they actually are</p>
<p>Test of Details – An audit procedure applied to transactions and account balances to detect material misstatements</p>	<p>Risk of Incorrect Acceptance – The risk that the sample supports the conclusion that the account balance (transaction) is not materially misstated when the account balance (transaction) is actually misstated</p>	<p>Risk of Incorrect Rejection – The risk that the sample supports the conclusion that the recorded account balance (transaction) is materially misstated when the account balance (transaction) is not materially misstated.</p>

**FACTORS INFLUENCING SAMPLE SIZES
FOR A SUBSTANTIVE TEST OF DETAILS IN SAMPLE PLANNING**

Factor	Conditions Leading to:		Related Factor for Substantive Sample Planning
	Smaller Sample Size	Larger Sample Size	
a. Assessment of inherent risk	Low assessed level of inherent risk	High assessed level of inherent risk	Allowable risk of incorrect acceptance
b. Assessment of control risk	Low assessed level of control risk	High assessed level of control risk	Allowable risk of incorrect acceptance
c. Assessment of risk related to other substantive procedures directed at the same assertion (including substantive analytical procedures and other relevant substantive procedures)	Low assessment of risk associated with other relevant substantive procedures	High assessment of risk associated with other relevant substantive procedures	Allowable risk of incorrect acceptance
d. Measure of tolerable misstatement for a specific account	Larger measure of tolerable misstatement	Smaller measure of tolerable misstatement	Tolerable misstatement
e. Expected size and frequency of misstatements, or the estimated variance of the population	Smaller misstatements or lower frequency, or smaller population size	Larger misstatements, higher frequency, or larger population variance	Assessment of population characteristics
f. Number of items in the population	Virtually no effect on sample size unless population is very small ¹		

1 Some statistical substantive sampling techniques and formulas do consider population size in the determination of sample size, but in most cases the number of logical units in the population will not affect the resulting sample size much, unless the population size is very small.

SUPPLEMENT 5G

Potential Errors and Fraud Schemes and Examples of Fraud-Related Audit Procedures

The following are potential error and fraud schemes an auditor may encounter during the engagement of highly susceptible accounts (or transactions) such as: cash receipts and disbursements, inventories, payroll, and other liabilities. Fraud-related auditing procedures are suggested audit tests that may be applied to these accounts by the auditor to determine the potential for errors or fraud.

Potential Errors and Fraud Schemes

The following are types of potential errors and fraud relating to cash:

Cash Receipts

- Cash receipts are recorded incorrectly.
- Items are sold for cash, but the sale is not recorded, and cash is misappropriated.
- Checks received are deposited but not recorded; checks are written to employees for the same amount and also are not recorded.
- Customer remittances are misappropriated, and collectible accounts are written off or otherwise credited.
- Lapping (cash receipts misappropriated, and shortages concealed by delaying postings of cash receipts – for example, payment from customer A is diverted by the employee; payment from customer B is applied to customer A’s account; customer C’s payment is applied to customer B’s account; and so on).

Cash Disbursements

- Payment for goods or services is not authorized or not received.
- Checks are made out to wrong payees.
- Duplicate payments of invoices are made.
- Vendor invoices are altered and photocopied to conceal alteration; payment benefits third parties.
- Check signature or endorsement is forged.
- Disbursements are misclassified or not recorded.
- Disbursements are recorded at the wrong amount or in the wrong period.
- Checks are issued for benefit of employees or third parties, and payees are changed in the cash disbursements journal.
- Cash disbursements journal is overstated; the overstated amount is recorded, and the difference is misappropriated.
- Kiting (exploiting the time required for a check to clear the bank, commonly referred to as the “float” period, to conceal shortage of cash) may occur.

Fraud-Related Audit Procedures

The following are example audit procedures that may be performed in response to cash fraud schemes:

- Perform a proof of cash, rather than a mere review of the client’s bank reconciliation.
- Perform surprise cash counts.
- Compare payees with approved vendor lists.
- Compare sales price to the price list.
- Search for and investigate disbursements payable to “cash” or unusual sounding vendors.
- Search for and investigate non-payroll check disbursements made to employees and related parties.
- Expand tests of cancelled checks and scrutinize unusual payees, authorized signatures, endorsements, and amounts.

- Examine supporting documentation for held checks.
- Investigate void checks and analyze void transactions.
- Test interbank transfers.
- Obtain cutoff bank statements in addition to obtaining bank confirmations.
- Compare bank deposits to cash receipts, noting any time lags in deposit dates.
- Examine cancelled checks noting unusual patterns, e.g., time lags between the disbursement date per books versus the date the check cleared the bank.
- Match sales returns to original sales.
- Confirm returned sales with customers.
- Perform tests of controls over cash receipts and cash disbursements.

Potential Errors and Fraud and Examples of Fraud-Related Audit Procedures

Potential Errors and Fraud Schemes

The following are types of potential errors and fraud relating to inventories:

- Including nonexistent inventory items in physical count (e.g., empty boxes).
- Transfers from raw materials or work-in-progress are improperly recorded or recorded in the wrong period.
- Unauthorized adjustment of inventory records is made to conceal misappropriation of assets.
- Inventory records are manipulated to improve performance picture.
- Increasing or otherwise altering the inventory counts for those items the auditor did not test count.
- Programming the computer to produce fraudulent physical quantity tabulations or priced inventory listings.
- Manipulating the inventory counts/compilations for locations not visited by the auditor.
- Double-counting inventory in transit between locations.
- Physically moving inventory and counting it at two locations.
- Including in inventory merchandise recorded as sold but not yet shipped to a customer.
- Arranging for false confirmations of inventory held by others.
- Including inventory receipts for which corresponding payables have not been recorded.
- Overstating the stage of completion of work-in-process.
- Manipulating the "roll forward" of an inventory taken before the financial statement date.
- Failing to report scrap sales.
- Physical loss of or deterioration in inventory that is not accounted for.

Fraud-Related Audit Procedures

The following are example audit procedures that may be performed in response to inventory fraud schemes:

- Observe all inventory locations simultaneously.
- Account for all inventory tags used during the physical count and obtain copies of all inventory count sheets or tags before leaving the physical inventory sites.
- Open containers and match contents to description, noting salability.
- Perform extensive test counts during the physical inventory observation.
- Confirm inventories at locations outside the entity.
- Scrutinize any material book to physical inventory adjustments and examine supporting documents.
- Examine consignment agreements and determine proper accounting method.
- Examine production records for indications of stage of completion.
- Perform analytical procedures and predictive tests of key ratios.

- Expand testing of receiving and shipping cutoff.
- Examine supporting documents for significant reconciling items appearing in the inventory account reconciliations.
- Examine individual entries in the general ledger inventory account to search for expenses or other items that are improperly charged to inventory.
- Examine journal entries made to the inventory accounts subsequent to year-end.
- Compare carrying amounts to recent sales amounts.
- Confirm vendors' invoices and unusual terms.
- Test direct labor rates and the calculation of overhead rates.
- Analyze scrap sales.
- Analyze inventory shortages by location or product type.
- Look for evidence of bulk sales at steep discounts which could indicate a declining value for the products.
- Perform tests of controls over inventory.

Potential Errors and Fraud and Examples of Fraud-Related Audit Procedures-

Potential Errors and Fraud Schemes

The following are types of potential errors and fraud relating to payrolls and other liabilities:

Payrolls

- Unauthorized work or work not performed is accrued.
- Accrual of employee benefits (e.g., vacation pay, sick leave) is recorded but not earned, or earned but not recorded.
- Fictitious employees ("ghost employees") are on the payroll.
- Employees' earnings are over-accrued or under-accrued because improper rates are used or computation errors have occurred.
- Payroll costs, expenses, or related liabilities are misclassified.
- Payroll is recorded in period paid rather than in period earned.
- Time cards or reports are padded.
- Terminated employees remain on the payroll.

Other Liabilities

- Unauthorized expenses are incurred.
- Expenses and accruals are misclassified, recorded at the wrong amounts, or not recorded in the period incurred.

Fraud-Related Audit Procedures

The following are example audit procedures that may be performed in response to payroll fraud schemes:

- Observe payroll distributions.
- Follow up on payroll checks that have not been cashed.
- Scrutinize payroll records for employees with little or no deductions.
- Review personnel files for compensation rates.
- Test payroll calculations and deductions.
- Confirm amounts paid to employees who are at remote locations working without direct supervision.
- Examine payroll disbursements subsequent to year-end and compare with accrued payroll at the balance-sheet date.

- Scrutinize the payroll registers and the payroll check registers for unusual items such as: names of former employees; duplicate names or duplicate addresses; unusual pay rates; unusual number of hours worked; and same Social Security numbers for two different people.
- Compare list of current employees in the personnel department to the payroll journal.
- Scrutinize payroll records for unusual pay rates or number of hours worked.
- Examine cancelled payroll checks for suspected fictitious employees.
- Perform tests of controls over payroll transactions.

CHAPTER 6—INTERNAL CONTROLS

600 INTRODUCTION

All OIPA engagements must comply with applicable standards regarding internal control.

Following is a description of the auditor's responsibilities related to internal controls by type of engagement.

Financial Audits

The auditor is to obtain a sufficient understanding of internal control to plan the audit and to determine the nature, timing, and extent of testing to be performed.

AICPA *Codification of Statements on Auditing Standards* (AU-C Section 315) describes the auditor's considerations in a financial audit engagement.

The auditor should obtain an understanding of internal control relevant to the audit. Although most controls relevant to the audit are likely to relate to financial reporting, not all controls that relate to financial reporting are relevant to the audit. It is a matter of the auditor's judgment whether a control, individually or in combination with others, is relevant to the audit.

GAO's *Government Auditing Standards 2018* (paragraph 1.17 (a)) require that auditors include 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.

Performance Audits

Auditors should obtain an understanding of internal control that is significant within the context of the audit objectives. For internal control that is significant within the context of the audit objectives, auditors should assess whether internal control has been properly designed and implemented and should perform procedures to obtain sufficient, appropriate evidence to support their assessment about the effectiveness of these controls. For those internal controls that are deemed significant within the context of the audit objectives, auditors should plan to obtain sufficient, appropriate evidence to support their assessment about the effectiveness of those controls. Information systems controls are often an integral part of an entity's internal control. Thus, when obtaining an understanding of internal control significant to the audit objectives, auditors should also determine whether it is necessary to evaluate information systems controls.

For further guidance auditors should refer to GAO's *Government Auditing Standards 2018* (paragraph 8.39).

Attestation Engagements

AICPA *Codification of Statements on Standards for Attestation Engagements* (AT Section 501) describes the auditor's considerations in an examination – level attestation engagement. This attestation provides guidance for auditors that are engaged to perform an examination of the design and operating effectiveness of the entity's internal controls over financial reporting that is integrated with audit of the financial statements.

The auditor's objective in an examination of internal control is to form an opinion on the effectiveness of the entity's internal control. Because an entity's internal control cannot be considered effective if one or more material weaknesses exist, to form a basis for expressing an opinion, the auditor should plan and perform an examination to obtain sufficient appropriate evidence to obtain reasonable assurance about whether material weaknesses exist as of the date specified in the management's assertion.

600.05 Purpose of Internal Controls

Internal controls provide a framework that encourages sound financial practices and helps management achieve its goals and objectives. Controls increase accountability and reduce fraud and operational breakdowns. Controls can include manual procedures such as approvals, reviews of activities, and reconciliations. Controls can also exist in automated systems (information technology). Technology controls include automated controls such as edit checks that are “imbedded” into the computer system, software change procedures, password controls and protection, and physical access controls (such as controlled entry to server and data storage areas).

605 UNDERSTANDING INTERNAL CONTROL

Gaining an understanding of internal control sufficient to plan the audit entails the following:

1. The auditor should understand those internal control processes that are designed to achieve the objectives relevant to the audit or attest engagement.

An entity's internal control process is designed to achieve several objectives related to operational efficiency.

Objectives relevant to auditors generally relate to:

- Reliability of financial reporting;
 - Compliance with applicable laws and regulations; and
 - Effectiveness and efficiency of operations.
2. The auditor should (1) understand the design of the internal controls and (2) determine whether the internal controls have been placed in operation.
 3. To understand the design of any given internal control, the auditor should understand the five internal control components:
 - Control environment;
 - Risk assessment;
 - Control activities;
 - Information and communication; and
 - Monitoring.
 4. Control environment, risk assessment, control activities, information and communication, and monitoring.
 5. To determine whether the internal controls have been placed in operation, the auditor should determine whether the entity is using them.
 6. The auditor uses his or her understanding of internal control for audit planning to:
 - Identify types of potential misstatements;
 - Consider factors that affect the risk of misstatement;
 - Design tests of controls; and
 - Design substantive tests.

605.05 Understanding the Entity and its Environment and Assessing the Risks of Material Misstatement

The auditor must obtain a sufficient understanding of the entity and its environment, including its internal control, to assess the risk of material misstatement of the financial statements whether due to error or fraud, and to design the nature, timing, and extent of further audit procedures.

The auditor should also perform risk assessment procedures to understand the entity and its environment, including its internal control, through:

- Inquiries of management and others within the entity;
- Analytical procedures; and
- Observation and inspection.

605.10 Discussion Within the Engagement Team

The members of the audit team, including the auditor with the final responsibility for the audit, should discuss the susceptibility of the entity's financial statements to material misstatements.

605.15 Understanding the Entity and its Environment, Including its Internal Control

The auditor should gain an understanding of the entity and its environment. Factors include:

- Industry, regulatory, and other external factors;
- Nature of the entity (e.g. operations, ownership, types of investments, etc.);
- Objectives and strategies and the related business risks that may result in a material misstatement of the financial statements;
- Measurement and review of the entity's financial performance; and
- Internal control, which includes the selection and application of accounting policies.

605.20 Assessing the Risks of Material Misstatement (RMM)

The auditor should identify and assess the risks of RMM at the financial statement level and at the relevant assertion level related to the classes of transactions, account balances, and disclosures. The auditor should:

- Identify risks throughout the process;
- Identify the risks to what can go wrong at the relevant assertion level;
- Consider whether the risks are of a magnitude that could result in a material misstatement of the financial statements;
- Consider the likelihood that the risks could result in a material misstatement of the financial statements;

605.25 Revision of Risk Assessment

During the course of the audit, the auditor’s RMM may change. The auditor should revise the assessment and further modify planned audit procedures accordingly.

605.30 Documentation

The auditor should document:

- The discussion among the engagement team regarding the susceptibility of the entity’s financial statements to material misstatement due to error or fraud.
- Key elements of the understanding obtained regarding each aspect of the entity and its environment, including each of the components of internal control, to assess the RMM of the financial statements, the sources of information, and the risk assessment procedures.
- The assessment of RMM, both at the financial-statement level and at the relevant assertion level, and the basis for the assessment.
- Special audit considerations regarding significant risks identified in the engagement and related controls.

610 INTERNAL CONTROL COMPONENTS

Internal control consists of five interrelated components. The components are derived from the way management runs its operations and are integrated with the management process. The components are control environment, risk assessment, information and communication, monitoring, and control activities.

610.05 Control Environment

The control environment relates to the entity’s management and employees’ roles in establishing and maintaining an environment throughout the organization that sets a positive and supportive attitude toward internal control and conscientious management. Several key factors and elements affect the accomplishment of this goal. These factors are described in the following table.

	<i>Factors</i>	<i>Elements</i>
1.	Integrity and Ethical Values	<p>The entity has established and uses a formal code or codes of conduct and other policies communicating appropriate ethical and moral behavioral standards and addressing acceptable operational practices and conflicts of interest.</p> <p>The entity’s management fosters, encourages, and emphasizes the importance of integrity and ethical values.</p> <p>The entity’s management cooperates with auditors and other evaluators, discloses known problems to them, and values their comments and recommendations.</p> <p>Management acts when violations of policies, procedures, or the code(s) of conduct occur.</p> <p>Management has a sound basis for setting realistic and achievable goals and does not pressure employees to meet unrealistic ones. Management provides fair, non-extreme incentives (as opposed to unfair and unnecessary temptations) to help ensure integrity and adherence to ethical values.</p> <p>Overriding of internal control by low-level management personnel is prohibited except in emergency situations. In such emergency cases, upper-level management is immediately notified, and the circumstances are documented.</p>

	Factors	Elements
2.	Commitment to Competence	<p>The entity's management has identified and defined the tasks required to accomplish particular jobs and fill the various positions. The entity's management has performed analyses of the knowledge, skills, and abilities needed to perform the job appropriately.</p> <p>The entity's management provides training and counseling in order to help employees maintain and improve their competence for their jobs.</p> <p>An appropriate training program is in place to meet the needs of all employees.</p>
3.	Management's Philosophy and Operating Style	<p>Management regularly relies on accounting/financial and programmatic data from its systems for decision-making and performance evaluations.</p> <p>Management looks to the information management function for critical operating data and supports efforts to make improvements in the systems as technology advances.</p> <p>Personnel operations have a high priority and top management emphasizes the importance of good human resources management. Management places a high degree of importance on the work of internal and external audits and other evaluations and studies and is responsive to information developed through such efforts.</p>
4.	Organizational Structure	<p>The organizational structure facilitates the flow of information throughout the entity.</p> <p>The organizational structure is appropriately centralized or decentralized, and management has clearly defined and considered factors in maintaining a balance between the two approaches.</p> <p>Key areas of authority and responsibility are defined and communicated throughout the organization.</p> <p>An accurate and updated organizational chart showing key areas of responsibility is provided to all employees.</p> <p>Top and middle management understand their internal control responsibilities and ensure that their staff members understand their own responsibilities.</p> <p>Reporting relationships between management and units have been established and effectively provide IPAs information they need to carry out their responsibilities and perform their jobs.</p> <p>Management periodically evaluates the organizational structure and makes changes as necessary in response to changing conditions.</p> <p>The entity has the appropriate number of employees, particularly in IPA positions.</p> <p>IPAs and supervisors have time to carry out their duties and responsibilities.</p> <p>Employees do not have to work excessive overtime or outside the ordinary workweek to complete assigned tasks.</p>
5.	Assignment of Authority and Responsibility	<p>Authority and responsibility are clearly assigned throughout the organization and are clearly communicated to all employees. Responsibility for decision-making is clearly linked to the assignment of authority and individuals are held accountable accordingly.</p> <p>Management has effective procedures to monitor results.</p> <p>Each employee knows how his or her actions interrelate with others in relation to the way in which authority and responsibilities are assigned.</p> <p>Each employee is aware of the related duties concerning internal control.</p>
6.	Oversight Groups	<p>The entity has an audit committee or management council that reviews the internal audit work and coordinates closely with oversight agencies and external auditors.</p> <p>The entity has an internal audit operation that reports to its management. The internal audit function reviews that entity's activities and systems and provides information, analyses, appraisals, recommendations, and counsel to the entity's management.</p>

610.10 Risk Assessment

Risk assessment is the process by which the entity's management identifies the risks that could impede the efficient and effective achievement of the entity's goals and objectives. Internal control should provide for an assessment of the risk management faces from both internal and external sources. Once the risks have been identified, they should be analyzed for their possible effect. Once the possible effects of the risks are identified, the entity's management should formulate an approach for risk management and decide which internal control activities are required to mitigate those risks and achieve the internal control objectives of efficient and effective operations, reliable financial reporting, and compliance with laws and regulations. The auditor should gain an understanding of how the entity's management identifies and take action to address risks to the entity's reporting and management objectives. The OIPA can assist and facilitate management's risk assessment process, but should not assess management risk, identify and/or mitigate risk on management's behalf. The auditor's role is to assess overall audit risk.

A key step in the risk assessment process is identifying changed conditions and taking necessary actions. Relevant risks may arise due to the following:

- Changes in the entity's operating environment due to the risks associated with technological advancements and developments and incorporation into existing operational processes.
- Changes in personnel due to downsizing of the entity's operations and personnel resulting in the lack of qualified personnel assigned to critical operations.
- Heavy reliance on contractors or other related parties to perform critical operations.
- Changes arising from the changing needs or expectations of oversight agencies, the public, or newly enacted legislation or regulations.
- Major changes in IPA or IA's responsibilities within the entity's organizational structure.
- Risks posed by disruption of information-systems processing and the extent to which backup systems are available and can be implemented.
- Changes in job assignments or responsibilities resulting in employee access to vulnerable assets.
- Risks resulting from natural catastrophes or criminal or terrorist actions.

610.15 Information and Communication

For an entity to run and control its operations, it must have relevant, reliable information, both financial and nonfinancial, relating to external and internal events. That information should be recorded and communicated to management and others within the entity who need it in a form and within a timeframe that enables them to carry out their internal control and operational responsibilities. In addition, the entity should ensure that the forms of communications are broad-based, and that information-technology management assures useful, reliable, and continuous communications. The entity's management should consider the appropriateness of information and communication systems to the entity's needs and the degree to which they accomplish the objectives of internal control.

Communication relates to providing a clear understanding of internal and management controls, how they function, and the responsibilities of individuals within the entity who are related to the controls. Communication may take the form of policy manuals, memoranda, or oral communications. The form communication will be dependent on the size and organizational structure of the entity.

The auditor should obtain an understanding of the reporting system because it is essential to his or her design of substantive tests. Designing tests of relevant documents and records is not possible unless an

auditor knows their availability and understands their relationships to the financial accounts and program management functions. This knowledge is important when entities maintain data and corroborating evidence only in electronic form.

Following are some of the factors an auditor should evaluate relative to an entity's controls over information and communication:

- Information from internal and external sources is obtained and provided to management as a part of the entity's reporting on operational performance. Relevant information is identified and regularly reported to management.
- Relevant information is identified, captured, and distributed to the right people in sufficient detail, in the right form, and at the appropriate time to enable those people to carry out their duties and responsibilities efficiently and effectively.
- The entity's top management provides a clear message throughout the entity that internal control responsibilities are important and must be taken seriously.
- Open and effective communication channels have been established with clients, customers, suppliers, contractors, consultants, and other groups that can provide significant input on quality and design of the entity's products and services. All outside parties dealing with the entity are clearly informed of the entity's ethical standards and also understand that improper actions, such as improper billings, kickbacks, or other improper payments, will not be tolerated.
- The entity's management makes certain that the advice and recommendations of oversight agencies and other auditors and evaluators are fully considered and that actions are implemented to correct any problems or weaknesses they identify.

610.20 Monitoring

Internal control monitoring should assess the entity's quality of performance over time and ensure that the entity promptly resolves the findings of audits and other reviews. In considering the extent to which the continued effectiveness of internal control is monitored, the auditor should consider both ongoing monitoring activities and separate evaluations of the internal control system, or portions thereof. Ongoing monitoring occurs during normal operations and includes regular management and supervisory activities, comparisons, reconciliations, and other actions employees take in performing their duties. It includes ensuring that IPAs and supervisors know their responsibilities for internal control, and they make control and control monitoring part of their regular operating processes.

Separate evaluations allow the entity to take a fresh look at internal control by focusing directly on the controls. These evaluations may take the form of self-assessments, control design reviews, and direct testing of control.

In addition, monitoring includes policies and procedures for ensuring that any audit and review findings and recommendations are brought to the attention of management and are resolved promptly. The entity's management should consider the appropriateness of the entity's internal control monitoring and the degree to which it helps them accomplish their objectives.

Following are some of the factors an auditor should evaluate relative to an entity's monitoring of internal controls:

- Management has a strategy to ensure that ongoing monitoring is effective and will trigger separate evaluations in which problems are identified. In addition, systems that are identified by management as critical are being tested periodically.

- In the process of carrying out their regular activities, the entity's employees obtain information about whether internal control is functioning properly. Operating reports are integrated or reconciled with financial and budgetary reporting system data and are used to manage operations on an ongoing basis, and management is aware of inaccuracies or exceptions that could indicate internal control problems.
- Appropriate organizational structure and supervision provide oversight of internal control functions. Automated edits and checks, as well as clerical activities are used to help control accuracy and completeness of transaction processing. The entity uses separation of duties and responsibilities to help deter fraud.
- Data recorded by information and financial systems are periodically compared with physical assets and discrepancies are examined. Inventory levels of materials, supplies, and other assets are checked regularly; differences between recorded and actual amounts are corrected; and the reasons for the discrepancies are resolved.
- Oversight agencies and other auditors and evaluators regularly provide recommendations for improvements in internal control, and management takes appropriate follow-up action.

610.25 Control Activities

Control activities are the policies, procedures, techniques, and mechanisms that ensure that the entity's directives to mitigate risks identified during the risk assessment process are carried out. Control activities are an integral part of the entity's planning, implementing, and reviewing, and are essential for government accountability over resources and for achieving effective and efficient program results. These activities include a wide range of activities, such as approvals, authorizations, verifications, reconciliations, performance reviews, security activities, and the production of records and documentation.

Knowledge of the entity's control activities is necessary for the auditor to identify types of potential misstatements or significant areas of noncompliance or error and consider factors that affect the risk of material misstatements or error. Only in certain circumstances would the auditor's knowledge of the entity's control activities need to extend beyond gaining an understanding. In these circumstances, the auditor should assess the adequacy of internal control activities, whether the proper control activities have been established (and sufficient in number), and the degree to which those activities are operating effectively.

Following are some of the factors an auditor should evaluate relative to an entity's control activities:

- Appropriate written policies, procedures, techniques, and mechanisms exist for each of the entity's activities.
- Management has identified the actions and control activities the entity needs to address the risks and has directed their implementation.
- Control activities described in policy and procedure manuals are actually applied and are applied properly.
- Control activities are regularly evaluated to ensure that they are still appropriate and working as intended.
- The entity uses a variety of control activities suited to information-processing systems to ensure accuracy and completeness. The processes include edit checks, which are used in controlling data entry, accounting for transactions using numerical sequences; comparison of file totals to control accounts and exceptions; or following up on violations indicated by other control activities.
- The entity uses physical control to secure and safeguard vulnerable assets.
- Critical duties and responsibilities are divided or segregated among different people to reduce the risk of error, waste, or fraud.

- Transactions and other significant events are authorized and performed by the appropriate personnel.

615 INTERNAL CONTROL—OBTAINING AND DOCUMENTING AN UNDERSTANDING

The auditor is required to document the understanding of internal control components in order to plan the engagement. The auditor ordinarily obtains this understanding through previous experience with the audited entity's procedures; by making inquiries of appropriate management, supervisory, and staff personnel; by inspecting entity documents including policy and procedure manuals; and by observing entity activities and operations. The auditor should consider the influence of engagement procedures performed on other audits by other audit organizations.

The auditor should focus on the significance of controls in achieving management's objectives rather than on isolation specific controls. The absence or inadequacy of a specific control designed to achieve the objectives may not be a deficiency if other controls exist that mitigate the risk.

The form and extent of information obtained to document the understanding of the entity's internal control components is influenced by the nature and complexity of the entity's controls. The auditor should record the information obtained in a flowchart or narrative (or checklist, when applicable). Flowcharts or narratives carried forward from the prior audit should be updated at the time of each examination; however, care should be taken to retain the earlier year's documentation. When electronic versions of the prior audit working papers are not available (i.e., only the paper copy of working papers exist), the auditor should insert a photocopy of the original flowchart in the prior audit's working papers. When prior audit electronic versions of the working papers are available, procedure and internal control reviews can be revised using a copy of the prior electronic versions. When significant changes to processes and related internal controls have occurred, flowcharts or narratives may need to be rewritten. The auditor should ensure that only relevant information is included in the working papers.

615.05 How an Auditor Obtains an Understanding of Internal Control

While internal control is a process, its effectiveness is a state or condition of the process at a certain point in time.

To determine whether a particular internal control system is "effective," the auditor should assess whether the five components are present and functioning effectively. Their effective functioning provides reasonable assurance that the entity is achieving one or more of its stated categories of objectives. Thus, these components are also criteria for effective internal control.

Although all five components should be present in the internal control of any entity, the components need not function identically, or even at the same level, within all entities. Some trade-offs may exist between components. Because controls can serve a variety of purposes, controls in one component can serve the purpose of controls that might normally be present in another component. Additionally, controls can differ in the degree to which they address a particular risk; complementary controls, each with limited effect, together can be satisfactory.

The five components and criteria apply to an entire internal control system, or to one or more objectives categories. When considering any one category—controls over financial reporting, for example—all five criteria should be satisfied in order to conclude that internal control over financial reporting is effective.

615.10 Internal Control—Assessing the Design Effectiveness

The auditor should consider the information developed when performing the audit planning (risk exposure) and should obtain an understanding of the internal control design. The auditor should examine the relevant internal controls to determine if they are logical and reasonably complete and are likely to deter or detect possible misuse, fraud, or errors. For example, incompatible functions (i.e., those that place any person in a position to both perpetrate and conceal fraud in the normal course of duty) should be separated so that opportunities for concealment are minimized or eliminated.

When assessing the control's design effectiveness, the auditor should be aware that a control in place at a given point in time (for example, when the control is observed) might be different from that in other times, such as earlier in the engagement period. If the auditor determines that a significant control was not in place at other times during the engagement period, the auditor should consider the engagement's implications of the weakness, such as the effect on tests and the need to report the matter to the auditee.

Controls should provide reasonable, but not absolute, assurance of deterring or detecting misuse of resources; failure to achieve program objectives; and noncompliance with laws, regulations, and management policies. In assessing the extensiveness of needed controls, the auditor should consider the reasonableness of the controls relative to the benefits to be gained (for example, the costs of implementing the controls).

The auditor should document the relevant strengths and weaknesses of the controls. This typically can be accomplished by preparing a separate working paper that summarizes the controls' strengths and weaknesses and identifies the tests that were conducted either to confirm that the control is in effect (strengths) or to determine whether fraud, errors, or abuse occurred (weaknesses).

620 ASSESSING CONTROL RISK

An independent auditor's work on forming an opinion on financial statements consists of obtaining and evaluating evidential matter concerning the assertions (i.e. declarations) in the audited financial statements. These assertions embody the account balances, transactions, and disclosures within the financial statements and include:

- Existence or occurrence
- Completeness
- Rights and obligations
- Valuations or allocations
- Presentation and disclosure

These assertions pose a risk of material misstatement (RMM) for the independent auditor, categorized in the following ways.

- **Inherent risk** - Susceptibility of an assertion to a material misstatement
- **Control risk** - Risk that a material misstatement could occur in an assertion will not be prevented or detected in a timely manner.
- **Detection risk** - Risk that the auditor will not detect a material misstatement that exists in an assertion.

During the course of a financial audit, the auditor should assess control risk, or the effectiveness of an entity's internal controls in preventing or detecting material misstatements in the financial statements. The auditor may assess control risk at the maximum level for some or all assertions if he or she believes that controls are unlikely to pertain to assertions or that testing controls would be inefficient. In assessing control risk at maximum, the auditor should be satisfied to the extent that performing substantive tests would be effective and more efficient than performing tests of controls.

The auditor may determine that assessing control risk below the maximum level for certain assertions would be effective and more efficient than performing only substantive tests. In addition, the auditor may determine that it is not practical or possible to restrict detection risk to an acceptable level by performing only substantive tests for one or more financial statement assertions. In such cases, the auditor should obtain evidential matter about the effectiveness of both the design and the operation of controls to reduce the level of control risk.

For example, the auditor may find it impossible to design an effective test of details when an entity conducts its business using information technology (IT) and no documentation of transactions is produced or

maintained other than through the IT system. In this case, the auditor should perform tests of controls to obtain audit evidence about the operating effectiveness of the IT system.

Assessing control risk below the maximum level involves three steps:

1. Identifying specific controls relevant to assertions.
2. Gain an understanding of controls. In gaining an understanding, the auditor should identify the controls that are likely to prevent or detect material misstatements.
3. Performing tests of controls. Procedures to evaluate the effectiveness of a control's design are meant to determine whether that control is sufficiently designed to prevent or detect material misstatement to specific assertions. Such procedures would include inquiries of appropriate entity officials; inspection of documents, reports, or electronic files; or observation of the application of a specific control. Tests of controls directed toward the operating effectiveness of a control are concerned with how the control was applied during the audit period, who applied it, and the consistency with which it was applied.

The conclusion reached as a result of assessing control risk is referred to as the assessed level of control risk. In determining the evidential matter necessary to support an assessed level of control risk below the maximum, the auditor should consider the characteristics of the evidential matter. Generally, the lower the assessed level of control risk, the greater assurance the evidential matter must provide that controls relevant to an assertion are designed and operate effectively. The auditor uses the assessed level of control risk to determine the level of detection risk for financial statement assertion. The assessed level of detection risk is used to determine the nature, timing, and extent of the auditing procedures to be applied to the account balances and/or class of transactions.

625 INTERNAL CONTROL – TESTING AND EVALUATING OPERATING EFFECTIVENESS

In every engagement, the auditor should obtain an understanding of the five components of internal control. In a financial audit, this understanding should be sufficient to assess the risk of material misstatement of the financial statements, or in the case of a performance audit, the risk of incorrect conclusions and findings included in the engagement report. This understanding should include an evaluation of the design of controls and a determination of whether the controls have been implemented.

The evaluation of control design and implementation is accomplished through the performance of risk-assessment procedures. Risk of material misstatement includes a control risk component. Based on the auditor's assessment of risk, he or she determines which further audit tests to perform; these may include the tests of operating effectiveness (test of controls).

After testing controls, the auditor should evaluate the sufficiency and appropriateness of the evidence obtained to reach a conclusion about operating effectiveness of the controls being tested. Effectiveness relates to how and by whom controls are applied and the consistency in which the controls are applied. As necessary, the auditor should modify his or her initial audit risk assessment of material misstatements and reconsider the nature, timing, and extent of planned procedures.

Keep in mind that tests of controls are not a requirement for every audit.

When to Test Controls

The auditor should perform tests of controls when he or she plans to reduce the control risk assessment, based on his/her expectation that controls are operating effectively, and reduce detection risk to appropriate low level. Tests of controls provide the support for the auditor's expectation that controls are operating effectively.

Additionally, specific circumstances may dictate the performance of test of control procedures, for example:

- When substantive tests alone do not provide sufficient evidence at the relevant assertion level; and
- When the audit involves a Single Audit under OMB Super Circular (previously OMB A-133) in testing of internal controls over compliance for major programs to support a low assessed level of control risk for assertions relevant to the compliance requirements for each major program.

If the auditor is unable to identify controls in place that would prevent or detect material misstatements in a relevant assertion and finds no basis for an expectation on operating effectiveness, then he or she should assess the control risk as high.

The auditor’s focus on test of controls has multiple purposes:

- To obtain a sufficient understanding of the specific controls that are likely to prevent or detect and correct material misstatements for relevant assertions;
- To evaluate the design of those controls and be satisfied that controls are capable of preventing or detecting and correcting a material misstatement in an assertion;
- To determine that controls exist and are being used; and
- To decide whether or not to rely on the effective operation of those controls.

The auditor may conclude that controls are appropriately designed and implemented but may decide that the test of controls over the effectiveness of those controls may not be warranted. The auditor may conclude that the available evidence lacks the persuasiveness to support a reduced level of control risk assessment, or that the test of controls is not being an efficient means of using auditing resources.

Considerations

Controls, and not processes, are the focus of the test of controls. A control prevents, detects, or corrects a misstatement. For example, supervisory review of amounts entered by an account clerk into an accounts payable system is a control. The control, in this circumstance, is to eliminate or minimize incorrect data into an information-processing system. The actual input of information by an accounts payable clerk into the accounts payable system is a process.

Control testing should be performed on controls that would result in a risk that an assertion is misstated. The misstatement, for example, may be that the assertion (valuation) on an account payable balance is understated due to unrecorded or erroneous transactions. Control testing would focus on tests for proper evaluation and completeness of transactions in this circumstance.

Test of Controls –Types

Tests of Control	Considerations/Definitions
Inquiries of the entity’s personnel	Generally, not sufficient by itself but effective in conjunction with other testing procedures, i.e. Observation and inspection of documents or records.
Observation of the application of the control	Used in conjunction with inquiry when reviewing general or application controls that do not produce documentary evidence of performance.
Inspection of documents, reports or electronic files	Inspection of source documents, reports, accounting procedure manuals, or electronic files.
Walk through	A run-through of the control procedures involving a trail of procedures and records. Used in conjunction with gaining an understanding of the control environment. Not generally useful in determining the effectiveness of controls.

Reviews of reconciliations	Includes inspecting evidence that the routine was performed throughout the period, inspecting examples of performed routines, and investigating the resolution of significant material misstatements or exceptions.
Re-performance of the application of the control	Examples include recomputing extensions and totals of vendor's invoices, or gross pay independent of the specified control.

625.05 Communicating Internal Control Related Matters Identified in an Engagement

The auditor should evaluate the severity of each deficiency in internal control identified during the engagement to determine whether the deficiency, individually or in combination with other deficiencies, is a significant deficiency or a material weakness.

The auditor should:

- Consider the likelihood and magnitude of misstatement.
- Evaluate individual control deficiencies that affect the same account balance, disclosure, relevant assertion, or component of internal control, to determine whether they collectively result in a significant deficiency or material weakness.
- Evaluate the possible mitigating effects of effective compensating controls that have been tested and evaluated as part of the financial statement audit.
- Conclude whether prudent officials, having knowledge of the same facts and circumstances, would agree with the auditor's classification of the deficiency.

625.10 Communication

The auditor should document in writing, to management and those charged with governance, significant deficiencies or material weaknesses, including those that were discussed in previous audits that have not been remediated.

Written communication is best made by the date of the final report, which is the date on which the auditor grants the entity permission to use the auditor's report; written communication should be made no later than 60 days following the date of the final report.

630 ITEMS AFFECTING THE REVIEW OF INTERNAL CONTROLS

Auditors should take into consideration factors that may affect the review of internal controls.

630.05 Service Organizations

Some entities use outside service organizations to provide services that are significant to the audit objectives – services such as accounting, budgeting, or procurement. Examples of engagements where service organizations might be present include Joint Powers Authorities (who might use a county agency to perform accounting or other administrative functions,) or a smaller entity (who might contract with the outside service organizations for operational services.)

In engagements where service organizations' activities are significant to the user entity's financial statements (and the engagement objectives,) the auditor should obtain an understanding of the internal controls over those services and conclude as to their adequacy. To do this, the auditor should consider the information available from the entity about the service organization's policies and procedures when documenting and evaluating internal controls. Sources for this information might include user manuals, technical manuals, system overviews, contracts, or reports prepared by the service auditor.

630.10 Internal Control—Computer Systems

When the auditor determines that computer systems are an integral component of the internal control of the entity being audited (i.e. significant to the audit objectives) and that internal control outside of the system (manual controls) are not sufficient to minimize risk, the auditor should obtain and document his or her understanding of the system controls, assess the effectiveness of the controls' design, and conduct tests to evaluate the effectiveness of the controls.

Information system controls include "general" controls and "application" controls. General controls are the policies and procedures created to safeguard data, protect application programs, prevent unauthorized system access, and ensure continued operations in case of unexpected interruptions. Application controls relate directly to an individual computer application, such as ensuring that transactions are valid (edit checks), authorized, correctly processed, and reported.

630.15 Consideration of Internal Auditors' Work

Auditors should consider the work of internal auditors in determining the nature, timing, and extent of auditing procedures. Internal auditors are responsible for providing analyses, evaluations, assurances, recommendations, and other information to the entity's management or to others with equivalent authority and responsibility. An important responsibility of the internal auditor is to monitor the performance of an entity's controls.

SAS 65, "The Auditor's Consideration of the Internal Audit Function in an Audit of Financial Statement," requires the auditor to undertake certain procedures before using the services of the internal auditor. These would include:

- Obtaining an understanding of internal audit function; and
- Assessing the competence and objectivity of the internal auditor.

In certain circumstances, the work of the internal auditor(s) may have an effect on the auditor's procedures. The auditor and the internal auditors should coordinate their work by holding periodic meetings, scheduling audit work, providing access to the internal auditors' working papers and reviewing audit reports.

After the auditor obtains and documents his or her understanding, he or she should assess the design effectiveness. That is, the relevant internal controls should be examined to determine if they are logical, reasonably complete, and are likely to ensure data reliability. The auditor should test controls performed to evaluate the operating effectiveness of automated controls. The auditor should assess the extent of internal controls used and help the report users reasonably interpret the audit report. 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.

635 INTERNAL CONTROL – ASSESSING THE RELIABILITY OF COMPUTER - PROCESSED INFORMATION

Information systems receive, store, and generate nearly all of the data that auditors rely on to conduct their audits. Such systems can be as simple as a client-prepared spreadsheet, or as complex as a large-scale computer database. Regardless, auditors must understand how computer-processed information impacts their potential audit findings and conclusions.

Computer-processed information may be data that is (1) entered into a computer system or (2) results from computer processing. Examples include information extracted from databases, data maintained within Excel or Access applications, information extracted from enterprise-wide software applications, or data summarized in a report or copied from a table in a document.

Audit standards (GAO, 2018 Yellow Book, paragraph 8.66) states "the evaluation of information systems controls may be done in conjunction with the auditor's consideration of internal control within the context of the audit objectives or as a separate audit objective or audit procedure, depending on the objectives of the audit. Depending on the significance of information systems controls to the audit objectives, the extent of audit procedures to obtain such an understanding may be limited or extensive." Note: Information pertaining to this subject can also be found in the codified AICPA audit standards, Section AU-C.315. Specifically, AU-C 315.A53 notes that an entity's system of internal control often contains automated elements. Therefore, even

for financial statement audits, the auditors must consider IT systems when completing their understanding of internal controls and assessing risks of material misstatement.

635.05 Required Assessment of Computer-Processed Information

During the planning phase of an audit, the auditor should identify computer-processed information that will be material to the audit objectives (and thus, used to support findings, conclusions, and recommendations). For any data that will materially support findings, conclusions, or recommendations, the auditor should conduct a computer system assessment; document his or her review; and report (in the objectives, scope, and methodology area of the report) the work done, results, and any limitations found.

For data assessment, the auditor will make one of three determinations:

- Sufficiently Reliable Data - A positive conclusion by the auditor, based on documented evidence that data is reliable
- Not Sufficiently Reliable Data - A negative conclusion by the auditor, based on documented evidence that data is not reliable
- Data of Undetermined Reliability - The auditor is unable to determine, because of a lack of evidence or limitations in resources to obtain evidence, that the data is reliable or nonreliable

Model disclosure statements are discussed in [Section 635.25](#)

635.10 Conditions Not Requiring Data Reliability Assessment

The auditor does not need to assess the reliability of data that will not materially affect findings, conclusions, or recommendations. Data that merely sets the stage or puts audit work into context, for example, does not require a reliability assessment. The auditor should, however, still ensure that the data comes from the best source available.

As an example, an audit of a county's redevelopment funds would require a data reliability assessment of some kind for the systems that receive, store, or generate the county's fund information. Alternatively, putting the county's redevelopment funds into context against the State's total redevelopment funds would not require an assessment of the reliability of the state-wide figures. Instead, the auditor would need to determine that the state-wide amount came from another reliable source, for example the Department of Finance.

635.15 Planning a Data Reliability Assessment

A data reliability assessment is performed as early as possible, preferably during the planning phase of an audit.

635.20 Assessment Steps

The auditor will use judgment to select which of the following steps will be necessary to complete a data assessment.

1. Review existing information, such as past internal or external audit reports, user manuals, system documentation, or quality assurance materials available from the auditee.
2. Perform data testing. Data testing can be done by applying logical tests to electronic data files or to paper copies of reports. Such tests could include:
 - Total number of records
 - Testing for missing data or fields

- Looking for duplicate records
- Testing for values outside of a designated range
- Testing for dates outside of a designated period
- Testing for relationships between data elements
- Verifying edit checks or formulas

Note: in some situations, listed above, testing may exceed the abilities of general auditors, and may require assistance from IT specialists.

3. Trace to and from source documents. When source documents are available, tracing a sample of data records to source documents can be an efficient method by which to assess reliability. Likewise, tracing from source documents to data records is also useful. The auditor must use judgment in determining which "direction" to test, or whether both "directions" should be tested. Again, the significance of the data on the potential findings, conclusions, and recommendations will affect the amount of testing necessary.
4. Review selected system controls. Examples of system controls include limits on access and edit checks, exception reports, and reconciliations. To assess system controls, the auditor will make inquiries or observations to verify the existence of password controls or physical access controls. Likewise, the auditor could review operating manuals for information about the nature and extent of edit checks. Similarly, the auditor could inquire whether exception reports exist and how exceptions are tracked and/or corrected. Overall, the goal of reviewing system controls is to assess whether errors can be prevented or detected and corrected.

Some audits require very short turnaround times. Regardless, the auditor will still need to consider reviewing existing information (internal or external audit reports, for example), interviewing knowledgeable agency staff, and/or electronically test critical data elements.

635.25 Documenting and Reporting the Results of the Data Assessment

Once the data reliability assessment is completed and documented in the engagement work papers, the auditor should conclude on the reliability of the data. There are three possible conclusions:

- Data is sufficiently reliable.
- Data is not sufficiently reliable. In this situation, the auditor should document the limitations of the data and the potential impact on the findings, conclusions, and recommendations. The auditor should also discuss the potential impacts with his or her supervisor or manager.
- Data is of undetermined reliability. Likewise, the auditor should document the limitations of the data and the potential impact on the findings, conclusions, and recommendations. The auditor should also discuss the potential impacts with his or her supervisor or manager.

The auditor should also consider whether the assessment and conclusion should be reported in the engagement's report. This decision, to report or not report, involves auditor judgment and applicability of the relevant standards.

Model language:

Data is sufficiently reliable

Example 1: We assessed the reliability of (entity's name) data by (1) performing electronic testing of required data elements, (2) reviewing existing information about the data and the system that produced them, and (3) interviewing agency officials knowledgeable about the data. We determined that the data were sufficiently reliable for the purposes of this report.

Example 2: To assess the reliability of (entity's name) data, we (1) performed electronic testing for obvious errors in accuracy and completeness; (2) reviewed related documentation, including contractor audit reports on data verification; and (3) worked closely with agency officials to identify data problems. When we found discrepancies (such as unpopulated fields or data entry errors), we brought them to (individual's name)'s attention and worked with (individual's name) to correct the discrepancies before conducting our analyses. We determined that the data were sufficiently reliable for the purposes of our report.

Not sufficiently reliable

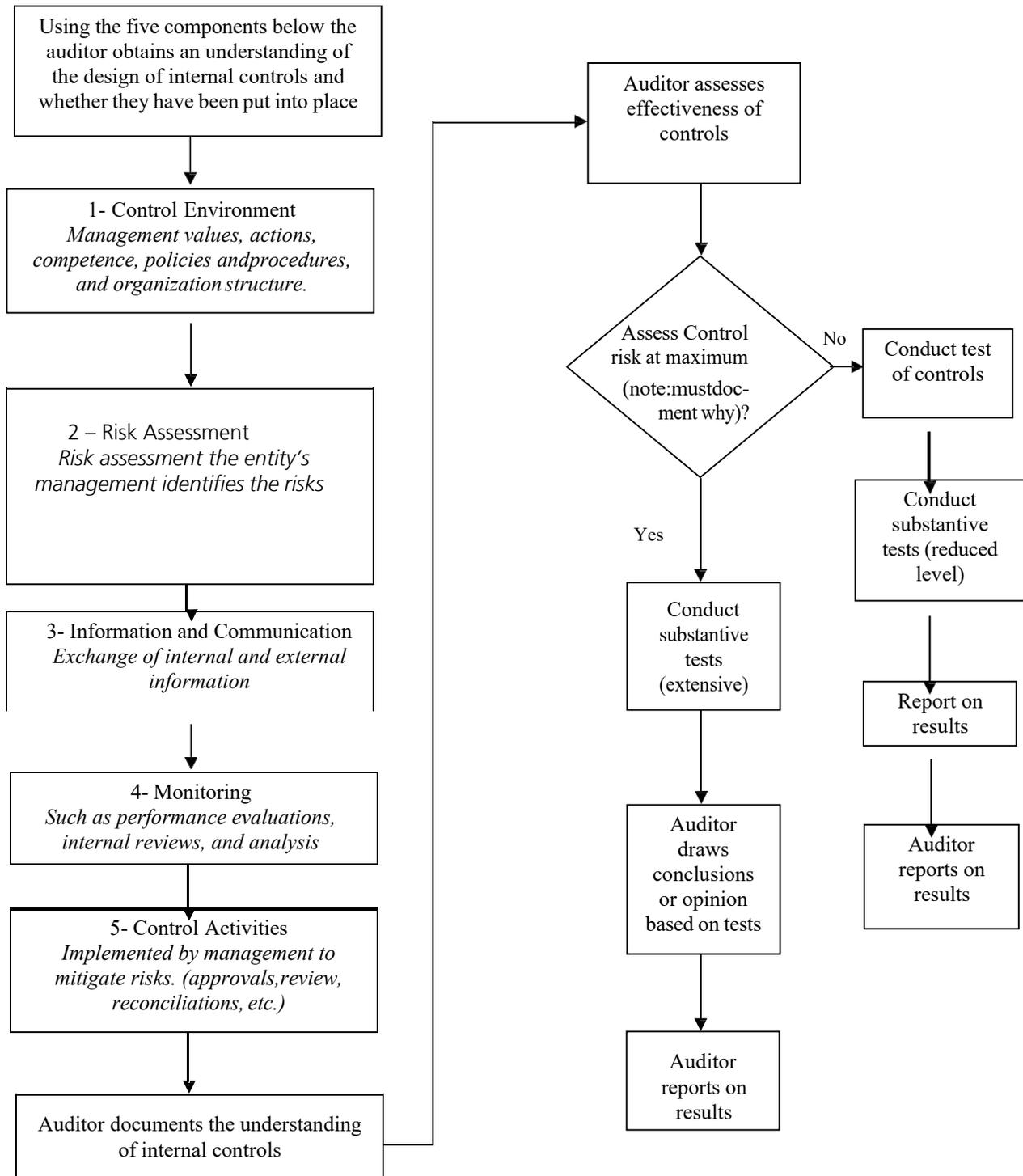
Example: To assess the reliability of the data elements needed to conduct our engagement, we (1) performed electronic testing of required data elements, (2) reviewed related documentation, and (3) interviewed agency officials knowledgeable about the data. The results of our electronic testing showed that data elements key to our review contained high percentages of missing data. (See Appendix XYZ for further details.) Therefore, we determined that the data were not sufficiently reliable for the purposes of this report.

Undetermined reliability

Example: To test the accuracy of the data, we randomly selected a sample of XX records from the (entity's name) database obtained from Department Y and conducted tests to ensure the data contained in those records matched to source documents. We found that Department Y was unable to provide documentation that supported the entries it keyed into the data fields used to do XXX, and YYY. Because we were unable to test the completeness of the (entity's name) data base, due to the lack of source documents, we concluded that the data has undetermined reliability.

Note: if the data is determined to be unreliable or cannot be determined to be reliable by the auditor, this condition should be disclosed as a scope limitation or a finding in the performance report.

Internal Controls – Determination of Level of Control Risk



The flowchart displays the basic steps and related documents in the process of reviewing internal controls and assessing control risk.

CHAPTER 7—QUALITY CONTROL

700 INTRODUCTION

The OIPA's policies and procedures for the elements of quality control are described in the following pages. All staff members of the OIPA are responsible for understanding, implementing, and adhering to these policies and procedures.

705 INDEPENDENCE, INTEGRITY, AND OBJECTIVITY

It is the policy of the OIPA that all professional staff be familiar with and adhere to the independence, integrity, and objectivity rules, regulations, interpretations, and rulings of the AICPA, the California State Board of Accountancy, and the California CPA Society, as well as guidelines presented in this Policies and Procedures Engagement Manual. In this regard, any transaction, event, circumstance, or action that would impair the OIPA's independence or violate its integrity and objectivity policy is prohibited. The following procedures ensure compliance with this policy.

1. When hired, and annually thereafter, all top management personnel are required to submit a statement of economic interests (Form 700, Statement of Economic Interests) that discloses information about all interest in business and financial holdings and gifts received.
2. The appropriate level of management resolves all independence, integrity, and objectivity questions. The resolutions are documented and filed in the auditee's working papers.
3. To ensure that the OIPA's independence is properly considered at the engagement level, the work programs and the standard forms the OIPA uses contain steps that require a determination of independence on each engagement.
4. At least annually, the IPA reviews the independence, integrity, and objectivity policies and procedures to determine whether they are appropriate and operating effectively. Changes to the system, if necessary, based on the results of the review are implemented and properly documented.

710 PERSONNEL MANAGEMENT

The audit organization should have the following management policies in place.

710.05 Hiring

It is the policy of the OIPA that professional-staff hiring decisions be based on an objective evaluation of personnel needs, that staff members hired possess the appropriate skills and qualifications to perform competently, and that new employees be adequately informed of the OIPA's policies and procedures. The following procedures ensure compliance with this policy.

1. The OIPA prepares a hiring plan on an annual or as-needed basis.
2. The Audit Committee makes hiring decisions and approves the recruiting of staff after considering the needs of the OIPA.
3. Each member of the OIPA plays a role in the interviews and evaluates prospective applicants.
4. New employees are informed of the OIPA's personnel and working procedures on their first day of employment.

710.10 Assigning of Personnel

It is the policy of the OIPA that personnel be assigned to engagements in an objective manner, in order to achieve a proper blend of technical expertise, supervision, staff use, on-the-job training, and client satisfaction. The following procedures ensure compliance with this policy.

1. The IPA prepares (or direct the preparation of) the staffing assignment.
2. A copy of the annual staffing plan is circulated to all employees.
3. The OIPA recognizes that modifications to the staff assignment schedules will be required due to addition limited resources, delays in the timing of work, or other unforeseen events.
4. Staff should be rotated, when possible, to encourage and promote professional development, technical proficiency, and advancement opportunities.
5. At least annually, the IPA performs a QC review of the personnel assignment policies and procedures to determine whether they are appropriate and operating effectively.

710.15 Continuing Professional Education

It is the policy of the OIPA that all professional audit staff members comply with the continuing professional education requirements (CPE) of the AICPA, the California State Board of Accountancy, and the General Accountability Office; that all professional staff maintain an adequate awareness and understanding of current developments in technical literature; and that all professional staff assist in the training and development of audit staff members under their supervision or direction.

710.20 CPE Requirements

Paragraph 4.16 of the 2018 Revision of *Government Auditing Standards* states:

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.

Consequently, OIPA auditors must meet the following GAO training requirements.

- All auditors must complete at least 80 hours of CPE every two years;
- At least 24 of the 80 hours of CPE must be directly related to the government environment and to governmental auditing or the specific or unique environment in which the audited entity operates; and
- At least 20 hours must be completed in each year of the two-year period.

In addition to the GAO training requirements listed above, the OIPA has implemented the following additional requirements for audit staff.

- Auditors are to complete at least 40 hours of CPE in the first year of the two-year training period; and
- Auditors are to complete at least 40 hours of CPE in accounting and auditing subjects during the two-year training period.

710.30 Management

Management staff involved in performing/reviewing audits must meet the same GAO and OIPA training requirements as field auditors.

The OIPA requires that all IPAs and supervisors be aware and familiar with the organization's policies and other labor relation matters.

710.35 Training

The IPA and supervisors are mainly responsible for monitoring employees' progress toward meeting CPE requirements. The IPA develops and implements the OIPA's two-year training plan using input from audit staff. The following is considered in the plan's development:

- Subjects that are of particular interest to audit staff;
- Professional staff experience;
- Audit responsibilities;
- New or emerging technical literature; and
- The OIPA's needs for specialists or experts in a particular area.

In addition to coordinating all training activities for OIPA staff and management, the IPA and supervisor maintains training records, including appropriate documentation for each credit hour earned by professional audit staff to comply with the GAO requirements. CPE records are maintained for each auditor for at least five years.

710.40 Quality Control

The IPA is responsible for the Quality Control Review and for ensuring that the OIPA is following applicable professional standards (i.e. audits or attestation). The IPA conducts periodic reviews of the OIPA's engagement reports or letters and related work papers to ensure that established policies and procedures are followed along with the applicable professional standards. The IPA maintains and updates the Policies and Procedures Engagement Manual. The Policies and Procedures Engagement Manual documents the policies and procedures for conducting all engagements types and provides guidance on the application of professional standards.

710.45 Advancement

It is the policy of the OIPA that professional-personnel advancement decisions be based on a timely and objective evaluation of individual performance.

Management uses staff classification levels to designate staff experience, evaluate individual performance, and establish criteria for promotion.

715 ACCEPTANCE AND CONTINUANCE OF CLIENTS AND ENGAGEMENTS

It is the policy of the OIPA that the following procedures be followed before any work engagement is accepted or continued.

1. The acceptability of the client and the engagement should be evaluated by OIPA management before the engagement is accepted and professional services are rendered.
2. An engagement should only be accepted if, after considering the risk associated in providing professional services, the OIPA IPA decides that the engagement can be completed with professional competence.

3. An engagement should be only accepted if the OIPA can comply with:
 - Professional standards
 - Legal requirements and authority
 - Ethical principles

715.05 Definitions

The following are important elements in the acceptance and continuance of clients:

Client – The entity that contracts with the OIPA to perform an engagement and is ultimately responsible for assessing the work for the services provided (e.g. BOD, AC Members, ED).

Auditee – The entity that is the subject of the engagement deliverable or deliverables, to our client or under a statutory requirement (Dept. Director, Contractor or other entity).

Note: In some cases the Client is the Auditee.

Engagement – Work that is performed by the auditor on behalf of the client which results in a deliverable to our primary client. The deliverable is the auditor’s report or letter. An engagement does not necessarily have to be an audit or an attestation engagement as defined by standards of the General Accountability Office (GAO) and the American Institute of Certified Public Accountants (AICPA) but may involve a non-audit service.

715.10 Prospective Clients

Under this policy, the IPA or designee is required to undertake the following steps to determine the acceptability of the prospective client:

1. Inform staff as to the policies and procedures concerning the undertaking of a new client.
2. Obtain and evaluate available financial information about the client (i.e. annual reports, financial statements, information from regulatory agencies and prior audit reports issued by other audit organizations).
3. Make inquiries of the client as to the nature of the professional services to be provided (audit, attestation or non-audit service).
4. Make inquiries of other government agencies or organizations that had a previous business relationship with the prospective client.
5. Make a determination on whether performing a service for the prospective client would create a potential conflict of interest or impairment for the audit organization’s independence on current or future engagements.
6. Communicate with the predecessor accountant or auditor when doing so is required by professional auditing standards.
7. Make a determination whether the OIPA has experienced audit staff to perform the engagement or will the services of an internal or external specialist be needed.

715.15 Engagement Reevaluation

Following are conditions that may necessitate an engagement reevaluation (in the case of a continued engagement).

1. Significant management changes in the client organization.
2. Changes in the nature or scope of the engagement that result in the OIPA needing additional services from the client.
3. Changes in the client's key personnel.
4. The development of conditions that would have caused the IPA to reject the client or engagement initially.
5. Disagreements between the client and the OIPA on the nature, extent and timing of procedures or the disclosures included in the engagement report.

Significant changes in the entity's (client/audittee's) key personnel, lack of cooperation with the OIPA's staff as well as other factors may be red flags for the OIPA on whether to continue an engagement relationship. At such time, the OIPA should determine whether a continuation of the engagement relationship is in the best interest of SANDAG. Such decisions to terminate a client/audit organization relationship should be well document and have the concurrence of the BOD, AC, or the Executive Director (ED).

715.20 Withdrawal from Engagements

After the commencement of an engagement, situations or conditions may occur that may warrant a withdrawal from the engagement. Usually, the decision to withdraw is made during the course of the engagement. Professional auditing standards provide guidance as to conditions that may require withdrawal from the engagement.

For financial statement engagements, professional auditing standards require the auditor to withdraw when:

- The client is unwilling to make a material revision to the financial statements or to accept a modified auditor's report;
- The client fails to undertake remedial action with regard to fraud, noncompliance with provisions of laws, regulations, contracts, and grant agreements, and abuse that might be discovered during the course of the engagement; and/or
- The client has not disclosed fraud, noncompliance with provisions of laws, regulations, contracts, and grant agreements, and abuse in the financial statements and is unwilling to accept a modified auditor's report.

In compilations and review engagements, professional standards require an auditor to withdraw when:

- The auditor becomes aware that information supplied by the client is incorrect, incomplete, or otherwise unsatisfactory and the client refuses to provide additional or revised information;
- When the auditor, during a review engagement, is unable to apply analytical review procedures or the client fails to provide a representation letter and the auditor decides not to issue a compilation report;
- The client will not accept a modified report; and/or
- Modification of the standard report will not adequately indicate the deficiencies in the financial statements as a whole.

Attestation standards require an auditor to withdrawal from an attestation engagement when:

- During an examination or review engagement, the client does not provide the auditor with a written assertion (declaration) as to whether or not the subject matter is based on, or is in conformity with, the criteria against which the assertion will be evaluated;
- In an examination or review engagement, the responsible party refuses to provide all written representations the auditor believes are necessary in order to issue a report;
- In a review engagement, the auditor is unable to perform the inquiry, analytical, or other procedure considered necessary to conduct the engagement;
- In an agreed –upon procedure engagement, the client (who is the responsible party) refuses to provide an assertion; and
- In an agreed –upon procedure engagement, the responsible party refuses to provide a written representation determined by the auditor to be appropriate and critical for the performance of the engagement,

The IPA or designee is responsible for documenting the circumstances leading to a recommendation to withdraw from an audit engagement. It is the OIPA IPA's responsibility to decide whether to proceed with the withdrawal. The OIPA IPA will further decide how to inform the client of the decision and whether the County's legal counsel should be consulted.

715.25 Non-Audit Services

Under *Government Auditing Standards, 2018 Revision*, audit organizations must make a determination on whether providing non-audit services to an entity potentially creates threats to independence in regard to the current engagement or prospective engagements with the same entity. This determination is made before acceptance by the audit organization to take on the non- audit service.

The GAO adopted a conceptual framework of evaluating the relationship between the auditor (and audit organization) and the entity to be audited. Under this evaluation, a determination would be made by the auditor and the audit organization if such a relationship posed an unacceptable risk to the auditor's or audit organization's independence. The key to this evaluation is to assess the extent to which a threat to the auditor's/audit organizations independence exists, and whether such threat would compromise (or give the perception of compromising) the auditor's professional judgment. And if such a threat existed, could such a threat be effectively mitigated or eliminated by the use of safeguards. Refer to the OIPA Policies and Procedures Engagement Manual section regarding independence, threats to independence, and safeguards for guidance.

The audit IPA or designee should proceed with the following steps in making this evaluation:

1. Document a description of the objectives, services to be performed, and entity's acceptance of its responsibilities, auditor's responsibilities, and limitations of the non-audit services (if any).
2. Document the identification of the individual or individuals representing the entity's management who will oversee the performance of the non-audit services. The individual(s) should possess the skills, knowledge or experience necessary to understand the significance of the services to be provided.
3. Document the determination whether the proposed non-audit service creates a threat to auditor independence.
4. Document whether supplemental safeguards are in place for non-audit services.

Auditors should refer to GAO paragraph 3.34 for guidance in this area.

The Independence Standard – Assessment of Non-Audit Services form has been created to document these considerations. This form is located on the OIPA of Internal Audit share drive.

In certain circumstances, the independence threats created by taking on the non-audit service are not at an acceptable level. The application of organization's safeguards does not reduce or eliminate the independence threat that results in impairment to independence for the auditor and the audit organization. In this case, the IPA, in consultation with the Audit Committee, should decline to take on the non-audit service or terminate the service in progress. The IPA or designee should communicate with the entity's management that the audit organization would be in violation of the independence standard if it were to perform the non-audit service.

Constitutional or statutory requirements may require the auditors and the audit organization to conduct both audit and non-audit services for the same entity that would result in impairment to independence. The auditor would be required to disclose in the audit report the nature of the independence threat that could not be eliminated or reduced by safeguards and modify the *Government Auditing Standards* compliance statement. The modified compliance statement would indicate that the auditor did not meet the independence standard.

For individual audits selected for inspection during a peer review, the audit organization should disclose all related non-audit services to the audit organization's peer reviewer and make available the audit documentation required available for inclusion in the audit organization's peer review.

The IPA or designee should consult with the Audit Committee regarding any independence issues prior to accepting non-audit services.

720 ENGAGEMENT PERFORMANCE

The supervision and consultation policies provide for the engagement to be performed in an efficient manner.

720.05 Supervision

It is the policy of the OIPA that all audits, attestation, reviews and survey engagements be properly planned, performed, supervised, reviewed, and documented, and that the results be properly communicated. Management should inform staff members of their responsibilities and clarify the objectives of the procedures they are to perform. Management should inform staff members about matters that may affect the nature, extent, and timing of procedures they are to perform, such as the nature of the entity's business as it relates to their assignments and possible accounting and auditing problems. The auditor with final responsibility for the engagement should direct staff to bring to his or her attention significant accounting and auditing questions raised during the engagement so that he or she may assess their significance.

720.10 Consultation

It is the policy of the OIPA that personnel refer to authoritative literature or other sources when appropriate. The OIPA also recognizes the need for a constant exchange of ideas and opinions about technical issues in all professional engagements, and it is policy that all professional staff seek consultation within or outside the OIPA whenever they have a technical question or are uncertain as to the application of a professional procedure or standard; the application of a rule, regulation, or other regulatory agency; or the application of policy. The following procedures ensure compliance with this policy.

1. The OIPA can provide support and online references to be consulted by professional staff members in their research of technical issues.
2. The OIPA recognizes that it would be impossible to list all situations that might require referral to authoritative literature or other sources, or that might require a consultation. However, the following situations, due to their complexity, would normally require a consultation.

- Any engagement in which a qualified or nonstandard report is likely to be issued;
 - Going concern situations;
 - Any engagement involving material litigation or other uncertainty; and
 - Other situations involving, for the first time, the application of new or complex technical pronouncements.
3. Members of the engagement team must discuss issues requiring consultation before seeking consultation. If the team decides that further consultation is necessary, the members should consult persons within the OIPA who have the appropriate expertise.
 4. The OIPA IPA must approve consultations with specialists outside of the OIPA, including non-accounting specialists. When planning to use a specialist, the auditor should consider the specialist's professional qualifications, reputation, objectivity, and relationship to the auditee. The auditor should obtain an understanding of the specialist's methods and assumptions, make appropriate tests of data provided to the specialist, and determine whether the specialist's findings support the related financial statement assertions.
 5. The OIPA IPA resolves differences of opinion within the OIPA as to the resolution of a consultation issue. Any party to the consultation who disagrees with the resolution has the option of preparing a memorandum and filing it in the working papers.
 6. The auditor should document in the working papers all technical research and consultations that are unusual, controversial, complex, and material in nature.

725 INSPECTION AND INTERNAL QUALITY CONTROL MONITORING

It is the policy of the OIPA that the quality control system be monitored to provide the OIPA reasonable assurance that the policies and procedures are suitably designed and effectively applied. As an integral part of the monitoring process, the IPA inspects the OIPA's quality control system annually to determine whether the OIPA has stated quality control policies and procedures. The following procedures ensure compliance with this policy.

1. The IPA is responsible for reviewing, at least annually, the OIPA's quality control system. The review will consist of pre-issuance and post-issuance inspection of audit reports and working papers of audit work conducted by audit staff. The IPA determines the appropriate methods used to select audit reports and working papers for review and conducts announced and unannounced reviews of audit reports and working papers.

The IPA uses quality control checklists in its review of audit reports and working papers. These checklists help determine whether the audit and attestation engagements follow AICPA and GAGAS auditing standards and quality control procedures.

2. The OIPA is subject to a peer review every three years. The IPA is responsible for scheduling and coordinating the review with the external peer review organization. The most recent external peer review report should be posted on the OIPA's Web site and be made available upon a public request.
3. Based on the peer review report, letter of comment, letter of response, and exit conference with the external peer review team, the OIPA IPA or designee will determine what, if any, corrective actions the OIPA should pursue.

4. The IPA monitors each professional auditor's CPE files and formulates corrective action for any CPE hour deficiencies.
5. The OIPA IPA issues an annual report that summarizes its monitoring results to the Audit Committee.

730 EXTERNAL PEER REVIEW

The audit organization as part of its quality assurance system and a requirement under *Government Auditing Standards* will undergo an external peer review. The external peer review evaluates the audit organization's quality control system comprising the management review, engagement documentation and report processes, as well whether such processes are properly documented in the Policies and Procedures manuals. The evaluation determines whether the quality assurance system was suitably designed, and whether the audit organization is complying with the system in order to provide assurances of conforming to professional auditing standards. The evaluation's results are communicated in a report to the audit organization. The evaluation period covers one fiscal year chosen by the audit organization.

Quality Control Responsibilities

The OIPA IPA is designated the coordination responsibility for the peer review process covering the following areas:

- The contract for peer review services,
- Information needed to respond to the external peer review questionnaire,
- Policies and Procedures,
- Engagement documentation and related reports for engagements selected by the external peer review team,
- Coordination with the external peer review team leader.

Review Scope

The scope of the external peer team includes the inspecting and reviewing the following aspects of the audit organization's quality control system:

- Policies and Procedures manuals,
- Internal monitoring procedures,
- Selected engagement reports and documentation,
- Independence, continuing professional education and human resources documentation,
- Audit staff and management's understanding of the quality control policies and procedures.

Reporting of Results

Upon completion of its review, the external peer review will communicate its findings during a formal exit conference. The external peer review team will explain the procedures that were applied, and disclose any deficiencies identified in the review of the policies and procedures, the selected engagement reports and supporting documentation. The external peer team will explain the deficiency(s), the criteria used to support the deficiency observation, the deficiency significance and pervasiveness. Based on the peer review team's judgment, they will communicate their assessment of the audit organization's quality control system. This assessment (or opinion) will follow one of the following categories identified in the following table:

Peer Review Team's Assessment	Explanation
Peer Review Rating of Pass	A conclusion that the audit organization's internal control has been suitably designed and complied with to provide the audit organization with reasonable assurance of performing and reporting in conformity with applicable professional standards in all material aspects.
Peer Review Rating of Pass with Deficiency	A conclusion that the audit organization's system of quality control has been suitable designed and complied with to provide the audit organization with reasonable assurance of performing and reporting in conformity with applicable standards in all material aspects with the exception of a certain deficiency that are described in the report.
Peer Review Rating of Fail	A conclusion, based on the significant deficiencies that are described in the report, that the audit organization's system of quality control is not suitably designed to provide the audit organization with reasonable assurance of performing and reporting in conformity with applicable standards in all material aspects or the audit organization has not complied with its system of quality control to provide the audit organization with reasonable assurance of performing and reporting in conformity with applicable professional standards in all material respects.

The peer review team will communicate their assessment in a report and/or separate communication. Any identified deficiencies that are deemed by the external peer review team as severe or serious will be disclosed in the peer review report or separate communication. The report and separate communication should describe in detail the findings, conclusions and recommendations for corrective action related to the deficiencies. Insignificant and isolated deficiencies will be verbally communicated to the audit organization.

If there are no severe or serious deficiencies, the external peer review team will issue the peer review report to the audit organization at the exit conference. If there are severe or serious deficiencies, the audit organization will be allowed to address these items in writing. This formal response will be incorporated in the peer review report. Once the audit organization receives the peer review report, it should post it to its public website.

APPENDIX A—OVERVIEW OF THE SINGLE AUDIT ACT, SUPER CIRCULAR (PREVIOUSLY A-133), AND THE COMPLIANCE SUPPLEMENT

To facilitate a [recipient's compliance](#) with [Federal laws](#) and [regulations](#), and as well as its annual [Single Audit](#), the OMB created fourteen basic and standard compliance requirements that recipients must comply with when receiving and using such Federal assistance.

The OMB also provides detailed explanations, discussions, and guidance about them in the OMB Super Circular (previously A-133) Compliance Supplement. Compliance requirements are only guidelines for compliance with the hundreds of laws and regulations applicable to the specific type assistance used by the recipient, and their objectives are generic in nature due to the large number of Federal programs. Each compliance Requirements is identified by a letter, in alphabetical order.

Reviewed and updated – August 1, 2023