

United States General Accounting Office

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By the Comptroller General  
of the United States

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1988 Revision

# Government Auditing Standards

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1988 Revision

# **Government Auditing Standards**

Standards for Audit of  
Governmental Organizations,  
Programs, Activities, and Functions

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# Foreword

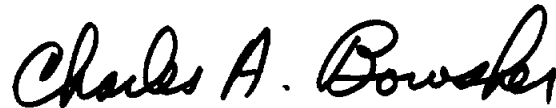
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The past three decades have seen a substantial increase in the number and dollar amounts of government programs and services, including large expenditures of public moneys to solve critical social and financial problems in the public, government and industry. This increase has brought with it a demand for full accountability by those entrusted with public funds and the responsibility for properly managing government programs and services.

Auditing has become an integral element of government accountability. This reliance on auditors has enhanced the need for standards to guide auditors and allow others to rely on auditors' work. Standards help ensure that audits are fair, objective, and reliable assessments of government performance.

This revision of the standards supersedes the 1981 revision, and becomes effective for audits starting January 1, 1989. Early application of the standards is permissible.

I want to personally thank those who provided suggestions and comments for improving the standards, and to especially thank the members of the Auditing Standards Advisory Council and the project team for their advice and efforts in preparing this revision of the standards.



Charles A. Bowsher  
Comptroller General  
of the United States

July 1988

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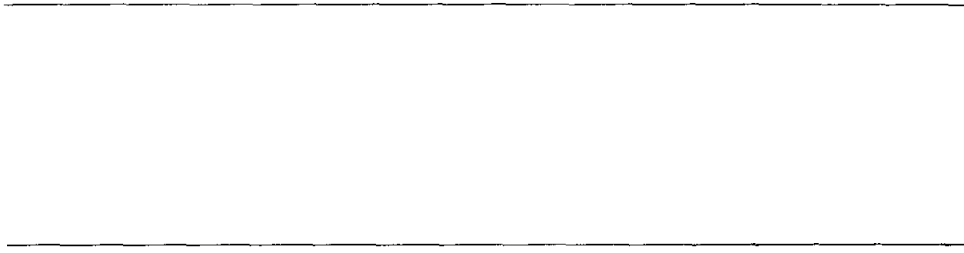
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# Introduction

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## Purpose

1. This statement contains standards for audits of government organizations, programs, activities, and functions, and of government funds received by contractors, nonprofit organizations, and other nongovernment organizations. The standards are to be followed by auditors and audit organizations when required by law, regulation, agreement or contract, or policy. The standards pertain to the auditor's professional qualifications, the quality of audit effort, and the characteristics of professional and meaningful audit reports.

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## Applicability

2. Federal legislation requires that the federal inspectors general comply with audit standards established by the Comptroller General for audits of federal organizations, programs, activities, and functions. The legislation further states that the inspectors general are to ensure that audit work conducted by nonfederal auditors of federal organizations, programs, activities, and functions complies with these standards.<sup>1</sup>
3. Other federal auditors must also follow these standards. The Office of Management and Budget (OMB) included these standards as basic audit criteria for federal executive departments and agencies in OMB Circular A-73.<sup>2</sup>
4. The Single Audit Act of 1984 requires that these standards be followed by auditors auditing state

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<sup>1</sup>See the Inspector General Act of 1978, as amended, 5 U.S.C. App. (1982).

<sup>2</sup>See section 6 of OMB Circular A-73, "Audit of Federal Operations and Programs "

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**Introduction**

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and local governments which receive federal financial assistance.<sup>3</sup>

5. Implementation of other federal policies and regulations, such as OMB Circular A-110, requires that these standards be followed in audits of entities receiving federal assistance.<sup>4</sup>
6. Auditors conducting government audits under agreements or contracts also may be required to comply with these audit standards under the terms of the agreement or contract.
7. The audit standards set forth in this statement are generally applicable to and recommended for use by state and local government auditors and public accountants in audits of state and local government organizations, programs, activities, and functions. Several state and local audit organizations, as well as several nations have officially adopted these standards.
8. The Institute of Internal Auditors and the American Evaluation Association (formerly the Evaluation Research Society) have issued related standards.<sup>5</sup>

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<sup>3</sup>See the Single Audit Act of 1984 (31 U.S.C. 7501-7507); OMB Circular A-128, "Audits of State and Local Governments;" and American Institute of Certified Public Accountants (AICPA) Audit and Accounting Guide for Audits of State and Local Governmental Units. The act and circular establish audit requirements for state and local governments and Indian tribal governments that receive federal financial assistance. The act and circular require that audits of these entities be made in accordance with the standards in this statement. The act also includes specific audit requirements that exceed the minimum audit requirements set forth in the standards in this statement.

<sup>4</sup>See OMB Circular A-110 "Grants and Agreements With Institutions of Higher Education, Hospitals, and Other Nonprofit Organizations "

<sup>5</sup>Standards for the Professional Practice of Internal Auditing, The Institute of Internal Auditors, Inc., copyright 1978; and New Directions for Program Evaluation: Standards for Evaluation Practice, no. 15. San Francisco: Jossey-Bass, September 1982.



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Relationship  
to AICPA  
Standards

9. The AICPA has issued standards that are applicable to and generally accepted for audits conducted to express opinions on the fairness with which an organization's financial statements present the financial position, results of operations, and cash flows or changes in financial position.<sup>6</sup>
10. The AICPA standards for field work and reporting have been incorporated into this statement for financial audits. As additional statements on auditing standards are issued by the AICPA, they will be adopted and incorporated into these standards unless GAO excludes them by formal announcement.
11. GAO has established a formal system for issuing government auditing standards and related interpretations and guidance to the audit community.

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Accountability

12. Our system of government today rests on an elaborate structure of interlocking relationships among all levels of government for managing public programs. Officials and employees who manage these programs must render a full account of their activities to the public. While not always specified by law, this accountability concept is inherent in the governing processes of this nation.
13. The requirement for accountability has caused a demand for more information about government programs and services. Public officials, legislators, and private citizens want and need to know not only whether government funds are handled properly and in compliance with laws and regulations,

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<sup>6</sup>The standards are included in "Statements on Auditing Standards" (SAS) issued by the AICPA. The AICPA Statement on Standards for Attestation Engagements may apply to some financial audits. The AICPA also issues interpretations and audit guides to provide guidance on the application of standards. These interpretations and guides do not have the authority of a standard issued by the AICPA; however, auditors may have to justify departures from them if the quality of their work is questioned.

but also whether government organizations, programs, and services are achieving the purposes for which they were authorized and funded and whether they are doing so economically and efficiently.

14. This statement provides auditing standards to help ensure full accountability and assist government officials and employees in carrying out their responsibilities. The audit standards are more than the codification of current practices. They include concepts and audit areas that are still evolving and are vital to the accountability objectives sought in auditing governments and their programs and services.

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**Basic Premises**

15. The following premises underlie these standards and were considered in their development.
- a. The term “audit” includes both financial and performance audits as described in this statement.
  - b. Public officials have the responsibility to apply resources efficiently, economically, and effectively to achieve the purposes for which the resources were furnished. This responsibility applies to all resources, whether entrusted to public officials by their own constituency or by other levels of government.
  - c. Public officials are accountable both to the public and to other levels and branches of government for the resources provided to carry out government programs and services. Consequently they should provide appropriate reports to those to whom they are accountable.
  - d. Public officials are responsible for establishing and maintaining an effective internal control system to ensure that appropriate goals and objectives

are met; resources are safeguarded; laws and regulations are followed; and reliable data are obtained, maintained, and fairly disclosed.

**e.** Public officials are responsible for complying with applicable laws and regulations. That responsibility encompasses identifying the requirements with which the entity and the official must comply and implementing systems designed to achieve compliance with those requirements.

**f.** Financial auditing is an important part of the accountability process since it provides an independent opinion on whether an entity's financial statements present fairly the results of financial operations, and whether other financial information is presented in conformity with established or stated criteria. Performance auditing is also an important part of the accountability process because it provides an independent view on the extent to which government officials are faithfully, efficiently, and effectively carrying out their responsibilities.

**g.** Unless legal restrictions or ethical considerations prevent it, auditees or audit organizations should make audit reports available to the public and to other levels of government that have supplied resources.<sup>7</sup>

**h.** Different levels of government share common interests in many programs. In many government financial assistance programs, the interests of individual governments often cannot be isolated because the resources applied have been commingled. Therefore, audits of financial assistance programs having common interests and shared funding should, to the extent practicable, be designed to satisfy the common accountability interests of each contributing government.

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<sup>7</sup>The Single Audit Act (31 U.S.C. 7502 (f)) requires that the report on single audits be made available for public inspection

i. Cooperation by federal, state, and local governments in auditing programs of common interest will minimize duplication of audit effort and benefit all concerned, and is a practical approach in auditing intergovernmental operations.

j. Auditors may rely on the work of others to the extent feasible once they satisfy themselves as to the other's independence, capability, and performance by appropriate tests of the work or by other acceptable methods.<sup>8</sup>

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**Auditor  
Responsibility**

16. The comprehensive nature of government auditing places on the audit organization the responsibility for ensuring that the audit is conducted by personnel who collectively have the necessary skills, that independence is maintained, that applicable standards are followed in conducting government audits, and that the organization has an appropriate internal quality control system in place, and participates in an external quality control review program.

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**Procurement  
of Audit  
Services**

17. While not an audit standard, it is important that a sound procurement practice be followed when contracting for audit services. Sound contract award and approval procedures, including the monitoring of contract performance, should be in place. The objectives and scope of the audit should be made clear. In addition to price, other factors to be considered include: the responsiveness of the bidder to the request for proposal; the past experience of the bidder; availability of bidder staff with professional qualifications and technical abilities; and whether the bidder organization participates in an external quality control review program.<sup>9</sup>

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<sup>8</sup>See chapter 3, paragraph 37, for guidance to follow in relying on the work of others

<sup>9</sup>See How to Avoid a Substandard Audit. Suggestions for Procuring an Audit, National Intergovernmental Audit Forum, May 1988.

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**Chapter 1**  
**Introduction**

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18. The remainder of this statement describes types of government audits and prescribes standards for conducting such audits.

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# Types of Government Audits

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## Purpose

1. This chapter describes the types of audits that government and nongovernment audit organizations conduct, and that government organizations arrange to have conducted, of government organizations, programs, activities, functions, and funds. This description is not intended to limit or require the types of audits that may be conducted or arranged. In conducting these types of audits, auditors should follow the applicable standards included and incorporated in the chapters which follow.
2. All audits begin with objectives and those objectives determine the type of audit to be conducted and the audit standards to be followed. The types of government audits, as defined by their objectives, are classified in this statement as financial audits or performance audits.

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## Financial Audits

3. Financial audits include financial statement and financial related audits.
  - a. Financial statement audits determine (1) whether the financial statements of an audited entity present fairly the financial position, results of operations, and cash flows or changes in financial position in accordance with generally accepted accounting principles,<sup>1</sup> and (2) whether the entity has complied with laws and regulations for those transactions and events that may have a material effect on the financial statements.

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<sup>1</sup>Three authoritative bodies for generally accepted accounting principles are: the Governmental Accounting Standards Board (GASB), the Financial Accounting Standards Board (FASB), and the General Accounting Office (GAO). GASB establishes accounting principles and financial reporting standards for state and local government entities. GAO establishes accounting principles and financial reporting standards for the federal government. FASB establishes accounting principles for nongovernment entities. Some state and local governments and regulatory bodies also have established specific accounting principles.

- b.** Financial related audits include determining (1) whether financial reports and related items, such as elements, accounts, or funds are fairly presented, (2) whether financial information is presented in accordance with established or stated criteria, and (3) whether the entity has adhered to specific financial compliance requirements.<sup>2</sup>
4. Financial related audits may include audits of the following items:<sup>3</sup>
- a.** Segments of financial statements.
  - b.** Financial information (e.g., statement of revenue and expenses, statement of cash receipts and disbursements, statement of fixed assets).
  - c.** Reports and schedules on financial matters, such as expenditures for specific programs or services, budget requests, and variances between estimated and actual financial performance.
  - d.** Contracts (e.g., bid proposals, contract pricing, amounts billed, amounts due on termination claims, compliance with contract terms).
  - e.** Grants.
  - f.** Internal control systems and structure over accounting, financial reporting, and transaction processing.
  - g.** Computer-based systems.
  - h.** Financial systems (e.g., payroll systems).
  - i.** Fraud.

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<sup>2</sup>The AICPA Statement on Standards for Attestation Engagements may apply to some financial related audits.

<sup>3</sup>Performance audits may also be conducted on these subjects.

5. The audit standards included and incorporated in chapters 3, 4, and 5 of this statement apply to all aspects of financial statement and financial related audits, unless otherwise stated.

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**Performance  
Audits**

6. Performance audits include economy and efficiency and program audits.<sup>4</sup>
- a.** Economy and efficiency audits include determining (1) whether the entity is acquiring, protecting, and using its resources (such as personnel, property, and space) economically and efficiently, (2) the causes of inefficiencies or uneconomical practices, and (3) whether the entity has complied with laws and regulations concerning matters of economy and efficiency.
- b.** Program audits include determining (1) the extent to which the desired results or benefits established by the legislature or other authorizing body are being achieved, (2) the effectiveness of organizations, programs, activities, or functions, and (3) whether the entity has complied with laws and regulations applicable to the program.
7. Economy and efficiency audits may, for example, consider whether the entity:
- a.** Is following sound procurement practices.
- b.** Is acquiring the appropriate type, quality, and amount of resources when needed at the lowest cost.
- c.** Is properly protecting and maintaining its resources.

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<sup>4</sup>Performance audits encompass value-for-money audits which assess whether government entities are managed with regard for economy and efficiency, and for effectiveness measurement, and in compliance with applicable laws, regulations, and directives. However, the objectives in performance audits are more comprehensive than those in value-for-money audits.



**d.** Is avoiding duplication of effort by employees and work that serves little or no purpose.

**e.** Is avoiding idleness and overstaffing.

**f.** Is using efficient operating procedures.

**g.** Is using the minimum amount of resources (staff, equipment, and facilities) in producing or delivering the appropriate quantity and quality of goods or services in a timely manner.

**h.** Is complying with requirements of laws and regulations that could significantly affect the acquisition, protection, and use of the entity's resources.

**i.** Has an adequate system for measuring and reporting performance on economy and efficiency.

**8.** Program audits may, for example:<sup>5</sup>

**a.** Assess whether the objectives of a proposed, new, or ongoing program are proper, suitable, or relevant.

**b.** Determine the extent to which a program achieves a desired level of program results.

**c.** Assess the effectiveness of the program and/or of individual program components.

**d.** Identify factors inhibiting satisfactory performance.

**e.** Determine whether management has considered alternatives for carrying out the program that might yield desired results more effectively or at a lower cost.

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<sup>5</sup>These audits may also apply to services, activities, and functions as well as programs.

f. Determine whether the program complements, duplicates, overlaps, or conflicts with other related programs.

g. Identify ways of making programs work better.

h. Assess compliance with laws and regulations applicable to the program.

i. Assess the adequacy of management's system for measuring and reporting effectiveness.

9. Generally, at the completion of a performance audit the auditor does not express an opinion on the overall level of performance. Therefore these standards do not contemplate that the auditor will be called upon to give such an opinion. Rather, the auditor would report findings and conclusions on the extent and adequacy of performance, and on specific processes, methods, and internal controls that can be made more efficient or effective. If potential for improvement is found, the auditor would recommend appropriate corrective actions.
10. The audit standards included in chapters 3, 6, and 7 of this statement apply to all aspects of economy and efficiency and program audits unless otherwise stated.

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**Understanding  
the Audit  
Objectives and  
Scope**

11. The importance and comprehensive nature of government auditing places on government officials who authorize or arrange government audits the responsibility for providing audit coverage that is broad enough to help fulfill the reasonable needs of potential users of the audit report. This comprehensive nature of auditing also highlights the importance of the auditor having a clear understanding of the audit objectives, the scope of the work to be conducted, and the reporting requirements.

12. Audits may have a combination of financial and performance audit objectives, or may have objectives limited to only some aspects of one audit type. For example, auditors conduct audits of government contracts and grants with private sector organizations, as well as government and nonprofit organizations, that often include both financial and performance objectives. These are commonly referred to as "contract audits" or "grant audits." Other examples of such audits include specific audits of internal controls, compliance, and computer-based systems. Auditors should follow the appropriate standards in this statement that are applicable to the individual objectives of the audit.

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**Other Activities  
of an Audit  
Organization**

13. Auditors may perform services other than audits. For example, the auditor may gather information about a program, activity, or function without analysis, conclusions, and recommendations. The head of the audit organization should establish policy on which audit standards from this statement should be followed by the auditors in performing such services. However, as a minimum, auditors should collectively possess adequate professional proficiency and exercise due professional care for the service being performed.
14. An audit organization may be authorized to perform investigative work. The head of the audit organization should establish policy on whether the audit standards in this statement, or some other appropriate standards, are to be followed by the employees performing this work.
15. Employees of an audit organization may also perform, within the audit organization, nonaudit activities, such as legal, administrative, and computer processing functions. The head of the audit organization should establish policy on what standards in this statement are to be followed, or whether some other appropriate standards are to be followed, by the employees in performing this type of work.

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# General Standards

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## Purpose

1. This chapter prescribes general standards for conducting financial and performance audits. These general standards relate to the qualifications of the staff, the audit organization's and the individual auditor's independence, the exercise of due professional care in conducting the audit and in preparing related reports, and the presence of quality controls. General standards are distinct from those standards that relate to conducting field work and preparing related reports.
2. These general standards apply to all audit organizations, both government and nongovernment (e.g., public accounting firms and consulting firms), conducting government audits unless excluded in the general standards that follow. (The AICPA's general standards are similar to these general standards but apply mainly to the members of the AICPA.)

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## Qualifications

3. The first general standard for government auditing is:

**The staff assigned to conduct the audit should collectively possess adequate professional proficiency for the tasks required.**

4. This standard places responsibility on the audit organization to ensure that the audit is conducted by staff who collectively have the knowledge and skills necessary for the audit to be conducted. They should also have a thorough knowledge of the government environment and government auditing relative to the nature of the audit being conducted.
5. The qualifications mentioned herein apply to the knowledge and skills of the audit organization as a whole and not necessarily to every individual auditor. If an organization employs personnel, or hires outside consultants, with acceptable knowledge and skills in such areas as accounting, statistics, law,

engineering, audit design and methodology, automatic data processing, public administration, economics, social sciences, and actuarial science, each individual staff member need not possess all these skills and knowledge.

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**Continuing  
Education  
Requirements**

6. To meet this standard, the audit organization should have a program to ensure that its staff maintain professional proficiency through continuing education and training. To satisfy this requirement, auditors responsible for planning, directing, conducting, or reporting on government audits should complete, every 2 years, at least 80 hours of continuing education and training which contributes to the auditor's professional proficiency. At least 20 hours should be completed in any one year of the 2-year period. Individuals responsible for planning, directing, conducting substantial portions of the field work, or reporting on the government audit should complete at least 24 of the 80 hours of continuing education and training in subjects directly related to the government environment and to government auditing.<sup>1</sup> If the audited entity operates in a specific or unique environment, auditors should receive training that is related to that environment.
  
7. The audit organization is responsible for establishing and implementing a program to ensure that auditors meet the continuing education and training requirements stated above. The organization should maintain documentation of the education and training completed.

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<sup>1</sup>All continuing education and training requirements should be met within 2 years from the effective date of the standards. For entry-level employees with less than 2 years with the audit organization, on the effective date of this requirement, a prorata number of hours would be acceptable.

8. The continuing education and training may include such topics as current developments in audit methodology, accounting, assessment of internal controls, principles of management and supervision, financial management, statistical sampling, evaluation design, and data analysis. It may also include subjects related to the auditor's field of work, such as public administration, public policy and structure, industrial engineering, economics, social sciences, and computer science.
9. External consultants and internal experts and specialists should be qualified and maintain their professional proficiency in their area of expertise and/or specialization but are not required to meet the above continuing education and training requirements. Auditors performing nonaudit activities and services also are not required to meet the above continuing education and training requirements.

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**Staff  
Qualifications**

10. Qualifications for staff members conducting government audits include:
  - a. A knowledge of the methods and techniques applicable to government auditing and the education, skills, and experience to apply such knowledge to the audit being conducted.
  - b. A knowledge of government organizations, programs, activities, and functions.
  - c. The skills to communicate clearly and effectively, both orally and in writing.
  - d. Skills appropriate for the audit work being conducted. For instance:
    - (1) If the work requires use of statistical sampling, the staff or consultants to the staff should include persons with statistical sampling skills.

(2) If the work requires extensive review of computerized systems, the staff or consultants to the staff should include persons with computer audit skills.

(3) If the work involves review of complex engineering data, the staff or consultants to the staff should include persons with engineering skills.

(4) If the work involves the use of nontraditional audit methodologies, the staff or consultants to the staff should include persons with the necessary skills.

e. The following qualifications are needed for financial audits that lead to an expression of an opinion:

(1) The auditor should be proficient in the appropriate accounting principles and standards and in government auditing.

(2) The public accountants engaged to conduct audits should be: (a) licensed certified public accountants or persons working for a licensed certified public accounting firm or (b) public accountants licensed on or before December 31, 1970, or persons working for a public accounting firm licensed on or before December 31, 1970.<sup>2</sup>

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## Independence

11. The second general standard for government auditing is:

**In all matters relating to the audit work, the audit organization and the individual auditors, whether government or public, should be free**

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<sup>2</sup>Accountants and accounting firms meeting these licensing requirements should also comply with the applicable provisions of the public accountancy law and rules of the jurisdiction(s) where the audit is being conducted and the jurisdiction(s) in which they are licensed.

**from personal and external impairments to independence, should be organizationally independent, and should maintain an independent attitude and appearance.**

12. This standard places responsibility on the auditor and the audit organization to maintain independence so that opinions, conclusions, judgments, and recommendations will be impartial and will be viewed as impartial by knowledgeable third parties.
13. Auditors should consider not only whether they are independent and their attitudes and beliefs permit them to be independent, but also whether there is anything about their situation that might lead others to question their independence. All situations deserve consideration because it is essential not only that auditors are, in fact, independent and impartial, but also that knowledgeable third parties consider them so.
14. Government auditors, including hired consultants and internal experts and specialists, need to consider three general classes of impairments to independence—personal, external, and organizational. If one or more of these impairments affect an auditor's ability to do the work and report findings impartially, the auditor should either decline to perform the audit, or in those situations when the auditor cannot decline to perform the audit, the impairment(s) should be reported in the scope section of the audit report. In addition, in cases when the auditors are employees of the audited entity, that fact should be reflected in a prominent place in the audit report.
15. Nongovernmental auditors also need to consider those personal and external impairments that might affect their ability to do their work and report their findings impartially. If their ability is adversely affected, they should decline to perform the audit. Public accountants should also follow the AICPA code



of professional ethics, the code of professional conduct of the state board with jurisdiction over the practice of the public accountant and the audit organization, and the personal and external impairments included in this statement.

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**Personal  
Impairments**

16. There are circumstances in which auditors may not be impartial, or may not be perceived to be impartial. The audit organization is responsible for having policies and procedures in place to help determine if auditors have any personal impairments. Managers and supervisors need to be alert for personal impairments of their staff members. Auditors are responsible for notifying the appropriate official within their audit organization if they have any personal impairments. These impairments apply to individual auditors, but they may also apply to the audit organization. Personal impairments may include, but are not limited to, the following.
- a. Official, professional, personal, or financial relationships<sup>3</sup> that might cause the auditor to limit the extent of the inquiry, to limit disclosure, or to weaken or slant audit findings in any way.
  - b. Preconceived ideas toward individuals, groups, organizations, or objectives of a particular program that could bias the audit.
  - c. Previous responsibility for decision-making or managing an entity that would affect current operations of the entity or program being audited.
  - d. Biases, including those induced by political or social convictions, that result from employment in,

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<sup>3</sup>When auditing state and local governments, the public accountant should be familiar with AICPA Professional Ethics Interpretation 101-10. This interpretation establishes specific rules on financial relationships that impair the public accountant's independence.

or loyalty to, a particular group, organization, or level of government.

**e.** Subsequent performance of an audit by the same individual who, for example, had previously approved invoices, payrolls, claims, and other proposed payments of the entity or program being audited.

**f.** Concurrent or subsequent performance of an audit by the same individual who maintained the official accounting records.<sup>4</sup>

**g.** Financial interest, direct or substantial indirect, in the audited entity or program.

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**External  
Impairments**

17. Factors external to the audit organization may restrict the audit or interfere with an auditor's ability to form independent and objective opinions and conclusions. For example, under the following conditions an audit may be adversely affected and the auditor may not have complete freedom to make an independent and objective judgment.

**a.** Interference or influence external to the audit organization that improperly or imprudently limits or modifies the scope of an audit.

**b.** Interference external to the audit organization with the selection or application of audit procedures or in the selection of transactions to be examined.

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<sup>4</sup>For example, an individual performs a substantial part of the accounting process or cycle, such as analyzing, journalizing, posting, preparing adjusting and closing entries, and preparing the financial statements, and later the same individual performs an audit. In instances in which the auditor acts as the main processor for transactions initiated by the audited entity, but the audited entity acknowledges responsibility for the financial records and financial statements, the independence of the auditor is not necessarily impaired.

**c.** Unreasonable restrictions on the time allowed to competently complete an audit.

**d.** Interference external to the audit organization in the assignment, appointment, and promotion of audit personnel.

**e.** Restrictions on funds or other resources provided to the audit organization that would adversely affect the audit organization's ability to carry out its responsibilities.

**f.** Authority to overrule or to influence the auditor's judgment as to the appropriate content of an audit report.

**g.** Influences that jeopardize the auditor's continued employment for reasons other than competency or the need for audit services.

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**Organizational Independence**

**18.** Government auditors' independence can be affected by their place within the structure of the government entity to which they are assigned and also by whether they are auditing internally or auditing other entities.

Internal Auditors

**19.** A federal, state, or local government audit organization, or an audit organization within other government entities, such as a government college, university, or hospital, may be subject to administrative direction from persons involved in the government management process. To help achieve organizational independence, the audit organization should report the results of their audits and be accountable to the head or deputy head of the government entity and should be organizationally located outside the staff or line management function of the unit under audit.

**20.** Auditors should also be sufficiently removed from political pressures to ensure that they can conduct

their audits objectively and can report their findings, opinions, and conclusions objectively without fear of political repercussion. Whenever feasible, they should be under a personnel system in which compensation, training, job tenure, and advancement are based on merit.

21. If the above conditions are met, and no personal or external impairments exist, the audit staff should be considered *organizationally independent to audit internally* and free to report objectively to top management.
22. When organizationally independent internal auditors conduct audits external to the government entity to which they are directly assigned, they may be *considered independent of the audited entity* and free to report objectively to the head or deputy head of the government entity to which assigned.

External Auditors

23. Government auditors employed by audit organizations whose heads are elected and legislative auditors auditing executive entities may be considered free of organizational impairments when auditing outside the government entity to which they are assigned.
24. Government auditors may be presumed to be independent of the audited entity, assuming no personal or external impairments exist, if the entity is:
  - a. A level of government other than the one to which they are assigned (federal, state, or local).
  - b. A different branch of government within the level of government to which they are assigned (legislative, executive, or judicial).
25. Government auditors may also be presumed to be independent, assuming no personal or external

impairments exist, if the audit organization's head is:

- a. Elected by the citizens of their jurisdiction.
- b. Elected or appointed by a legislative body of the level of government to which they are assigned and report the results of their audits to and are accountable to the legislative body.
- c. Appointed by the chief executive but are confirmed by, report the results of their audits to, and are accountable to a legislative body of the level of government to which they are assigned.

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Due  
Professional  
Care

26. The third general standard for government auditing is:

**Due professional care should be used in conducting the audit and in preparing related reports.**

27. This standard places responsibility on the auditor and the audit organization to follow all applicable standards in conducting government audits. Auditors should use sound professional judgment in determining the standards that are applicable to the work to be conducted, and therefore should be followed. Situations may occur where government auditors are not able to follow an applicable standard and are not able to withdraw from the audit. In these situations, the auditors should disclose in the scope section of their report, the fact that an applicable standard was not followed, the reasons therefor, and the known effect not following the standard had on the results of the audit. The auditors' determination that certain standards do not apply to the audit should be documented in the working papers.
28. Exercising due professional care means using sound judgment in establishing the scope, selecting the

methodology, and choosing tests and procedures for the audit. The same sound judgment should be applied in conducting the tests and procedures and in evaluating and reporting on the audit results. At a minimum, determining the scope of the audit to be conducted, the methodology to be used, and the extent of tests and procedures to be conducted requires consideration of:

- a.** What is necessary to achieve the audit objectives.
  - b.** Materiality and/or significance of matters to which the tests, procedures, and methodology are applied.
  - c.** Effectiveness and/or efficiency of internal controls.
  - d.** Cost versus benefits of the audit and the extent of the work being done. (However, situations may occur in which an audit organization is required to conduct an audit even though the cost of the audit exceeds the benefits to be derived.)
  - e.** Reporting timeframes that must be met.
- 29.** The quality of audit work and related reports depends upon the degree to which:
- a.** The audit scope, methodology, and the tests and procedures used in the audit are adequate to provide reasonable assurance that the audit objectives are accomplished. When appropriate, statistical sampling, standardized data collection, statistical inference, quantitative techniques, and other aspects of quantitative analysis should be used.
  - b.** Findings and conclusions are based on an objective evaluation of pertinent evidence.
  - c.** Findings and conclusions in reports are fully supported by sufficient, competent, and relevant evidence obtained or developed during the audit.

**d.** The audit process conforms with the field work standards and the reporting standards set forth in this statement.

**e.** A supervisory review is made of the work conducted, the judgments made in the audit, and the audit report.

30. A body of technical knowledge on types of audits, tests, procedures, and methodology exists. Some are generalized and some are specific to certain industries, types of audits, or special circumstances. Auditors should have a sufficient awareness of this body of knowledge to apply it to the audit being undertaken. This awareness is necessary to ensure that the selected methodology, tests and procedures are appropriate.
31. Due professional care also includes obtaining a mutual understanding of the audit objectives and scope with the audited entity as well as with those who authorized or requested the audit. It also includes obtaining a working understanding of the operations to be audited and when necessary, available performance measurement criteria (including laws and regulations). When the criteria are vague, the auditors should seek interpretation. If interpretation is not available, auditors should strive to agree on the appropriateness of these measures with the interested parties, or if applicable, indicate that they were unable to report upon performance because of the lack of definitive criteria.
32. While this standard also places responsibility on the auditor and audit organization to exercise due professional care in the performance of a quality appropriate for the audit assignment undertaken, it does not imply unlimited responsibility; neither does it imply infallibility on the part of either the individual auditor or the audit organization.

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**Materiality and  
Significance**

33. The auditor should consider materiality and/or significance in planning the audit and in selecting the methodology and designing audit tests and procedures as well as in deciding whether a matter requires disclosure in an audit report. One of the criteria to be considered in determining materiality includes the monetary value of the item. However, materiality and significance often depend on qualitative as well as quantitative factors. Qualitative factors include, but are not limited to the cumulative effect and impact of immaterial items, the objectives of the work undertaken, and the use of the reported information by the user or groups of users of the information. Decisions on these criteria are based on the auditor's professional judgment. In government audits the materiality level and/or threshold of acceptable risk may be lower than in similar-type audits in the private sector because of the public accountability of the entity, the various legal and regulatory requirements, and the visibility and sensitivity of government programs, activities, and functions.
34. In determining materiality and/or significance and audit risk the auditor may consider the following.
- a. Amount of revenues and expenditures.
  - b. Newness of the activity or changes in its conditions.
  - c. Adequacy of internal controls.
  - d. Results of prior audits.
  - e. Level and extent of review or other form of independent oversight.
  - f. Adequacy of the internal controls for ensuring compliance with laws and regulations.
  - g. Management's adherence to applicable laws and regulations.



**h.** Audit report users' expectations.

**i.** Public perceptions and political sensitivity of the areas under audit.

**j.** Audit requirements.

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**Relying on Work  
of Others**

35. One factor underlying government auditing is that federal, state, and local governments cooperate in auditing programs of common interest so that auditors may use other's work and avoid duplicate audit efforts. In conducting an audit, auditors may rely on the work of others to the extent feasible once they satisfy themselves of the quality of the others work by appropriate tests or by other acceptable methods.
36. Relying on the work of others reduces the amount of work necessary for the auditor to accomplish the audit objective(s).
37. In determining whether to rely upon the work of others, the auditor should consider the following guidance.
- a.** When the other auditors are external auditors, tests should include making inquiries into the professional reputation, qualifications, and independence of the auditors. The auditors should consider whether to (1) conduct additional tests and procedures such as reviewing the audit procedures followed and results of the audit conducted by the other auditors; (2) review the audit programs of the other auditors; and/or (3) review the working papers, including their understanding and assessment of internal controls, tests of compliance, and the conclusions reached by the other auditors. The auditors may review the documentary evidence in the other auditors' working papers or make supplemental tests of the work conducted.

**b.** When the other auditors are internal auditors, tests should include (1) determining whether they are qualified, (2) determining whether they are properly located in the organization in order to provide them with sufficient independence to conduct the audit objectively, (3) determining whether their work is acceptable by examining, on a test basis, the documentary evidence of the work conducted, and (4) conducting tests of the work. These tests may either (i) examine some of the transactions, balances, or work the internal auditors examined or (ii) examine similar transactions, balances, or work, but not those actually examined by internal auditors. Based upon this review, the auditors would decide what additional work, if any, would have to be done in order to accept the work of the internal auditors.

**c.** When relying upon the work of nonauditors (consultants, experts, specialists, etc., other than those hired to assist in the audit), the auditors should satisfy themselves as to the nonauditors professional reputation, qualifications, and independence from the organization, program, activity, or function under audit. The auditors should also consider whether to (1) conduct additional tests and procedures such as reviewing the procedures followed and the results of the work conducted, (2) review the work program, (3) review the working papers, (4) make supplemental tests of the work conducted, and (5) consider the methods or assumptions used.

**d.** The auditors should determine whether the above audit organizations have an appropriate internal quality control system in place and whether the organization participates in an external quality control review program.

- 38.** Auditors need access to the working papers of other auditors and nonauditors to satisfy certain of the above requirements. For working papers containing restricted information, the appropriate policies should be followed.

39. Arrangements need to be made to ensure that working papers will be made available upon request to other government audit staffs and individual auditors. All contractual arrangements for government audits should provide for access to working papers.
40. When auditors decide to rely on the work of others, but do not take full responsibility for that work, the auditors should indicate in the scope section of the audit report the division of responsibility between that portion of the work they conducted and that conducted by others, and the magnitude of the audit work completed by others.<sup>5</sup>

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Audit  
Follow-Up

41. Due professional care also includes follow-up on known findings and recommendations from previous audits that could have an effect on the current audit objectives to determine whether prompt and appropriate corrective actions have been taken by entity officials or other appropriate organizations. Management of the audited entity is primarily responsible for directing action and follow-up on recommendations. The auditor's report should disclose the status of known but uncorrected significant or material findings and recommendations from prior audits that effect the current audit objective. Government auditors should have a process that enables them to track the status of management's actions on significant or material findings and recommendations from their prior audits.

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Audit Scope  
Impairments

42. For all audits, auditors should consider whether audit scope impairments will adversely affect their ability to conduct the audit in accordance with the

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<sup>5</sup>This guidance does not preclude auditors from referring to other's work in their audit report even if the auditors did not verify it, if the work is used only for background or informational purposes and is not material or significant to the auditors' report. In these situations the auditors may just cite the information and its source in their audit report.

standards in this statement. Audit scope impairments are factors external to the audit organization which can restrict the auditors' ability to render objective opinions and conclusions. The auditors should attempt to remove the impairment. Failing that, the auditors should disclose the impairment in the scope section of their report and the known effect it had on the results of the audit. Two examples of audit scope impairments are the denial of access to sources of information by the audited entity, such as books, records, and supporting documents, and denial by the audited entity of the opportunity to meet with officials and employees of the organization, program, or activity under audit.

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**Quality  
Control**

43. The fourth general standard for government auditing is:

**Audit organizations conducting government audits should have an appropriate internal quality control system in place and participate in an external quality control review program.**

44. This standard places responsibility on government and nongovernment audit organizations conducting government audits to have an appropriate internal quality control system in place and to participate in an external quality control review program.
45. The internal quality control system established by the organization should provide reasonable assurance that it: (1) has established, and is following, adequate audit policies and procedures and (2) has adopted, and is following, applicable auditing standards. The nature and extent of an organization's internal quality control system depends on a number of factors, such as its size, the degree of operating autonomy allowed its personnel and its audit offices, the nature of its work, its organizational structure, and appropriate cost-benefit considerations. Thus, the systems established by

individual organizations will vary, as well as the extent of their documentation.

46. Organizations conducting government audits should have an external quality control review at least once every 3 years by an organization not affiliated with the organization being reviewed.<sup>6</sup> The external quality control review program should determine that: (1) the organization's internal quality control system is in place and operating effectively and (2) established policies and procedures and applicable auditing standards are being followed in its audit work, including its government audits. However, external quality control review procedures should be tailored to the size and nature of an organization's audit work. For example, an organization that performs only a few government audits may be more effectively reviewed by placing the primary emphasis on a review of the quality of specific government audits rather than on the organization's internal quality control policies and procedures.
47. Audit organizations should make the report on external quality control reviews available to auditors using their work and to appropriate oversight bodies. It is recommended that the report be made available to the public.
48. External quality control review programs, such as those conducted through or by the AICPA, National State Auditors Association, Intergovernmental Audit Forums, GAO, and the Institute of Internal Auditors, would be acceptable. Public accountants should participate in the AICPA practice-monitoring program or an equivalent program.

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<sup>6</sup>Organizations conducting government audits should have an external quality control review within 3 years from the effective date of the standards.

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# Field Work Standards for Financial Audits

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## Purpose

1. This chapter prescribes standards of field work for government financial audits. It incorporates the AICPA standards of field work for financial audits, and does not restate them<sup>1</sup> but rather prescribes supplemental standards of field work needed to satisfy the unique needs of government financial audits.
2. The field work standards of the AICPA and the supplemental standards in this chapter apply to both financial statement audits and financial related audits.
3. In conducting audits in accordance with the standards in this statement, the auditors choose and conduct auditing tests and procedures that, in their professional judgment, are appropriate in the circumstances to achieve the audit objectives. Such tests and procedures are designed to obtain sufficient, competent, and relevant evidence that will provide a reasonable basis for their opinions, judgments, and conclusions regarding the audit objectives.

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## Planning

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### Audit Requirements for All Government Levels

4. The first supplemental planning field work standard for government financial audits is:  
**Planning should include consideration of the audit requirements of all levels of government.**
5. In many instances, audits of the same organizations, programs, activities, or functions may be required by federal, state, and local laws, regulations, and

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<sup>1</sup>Future statements will be adopted and incorporated unless GAO excludes them by formal announcement.

ordinances.<sup>2</sup> When this situation exists, the auditor should ascertain what governments are to be served by the audit, and, to the maximum extent practicable, plan the audit so that it will help fulfill the legal and regulatory needs of identified potential users.

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**Legal and  
Regulatory  
Requirements**

6. The second supplemental planning field work standard for government financial audits is:

**A test should be made of compliance with applicable laws and regulations.**

7. In government auditing, compliance with laws and regulations is important because government organizations, programs, activities, and functions are usually created by law and are subject to more specific rules and regulations than the private sector.
8. An entity's management is responsible for establishing an internal control structure to assure compliance with laws and regulations. The lack of administrative continuity in government units because of continuing changes in elected legislative bodies and in administrative organizations increases the need for an effective internal control system.
9. In determining the nature, timing, and extent of the audit steps and procedures to test for compliance, the auditor should assess the risk of noncompliance with laws and regulations occurring and having a direct and material effect on the financial statements or the results of financial related audits. The

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<sup>2</sup>When auditing state and local governments that receive federal financial assistance, the auditor should be familiar with the Single Audit Act of 1984 (31 U.S.C. 7501-7507), OMB Circular A-128, "Audits of State and Local Governments," "OMB Compliance Supplement," and AICPA audit and accounting guide, Audits of State and Local Governmental Units. The act and circular include specific audit requirements that exceed the minimum audit requirements set forth in the standards in chapters 4 and 5 of this statement, mainly in the areas of internal control and compliance with laws and regulations.

auditor should assess the risk that the entity did not comply with those laws and regulations and the risk that the entity's control structure to ensure compliance with laws and regulations might not prevent or detect that noncompliance.<sup>3</sup>

10. In planning and conducting the tests of compliance the auditor should:
  - a. Identify the pertinent laws and regulations and determine which of those laws and regulations could, if not observed, have a direct and material effect on the financial statements or the results of a financial related audit.
  - b. Assess, for each material requirement, the risks that material noncompliance could occur. This includes consideration and assessment of the internal controls in place to assure compliance with laws and regulations.
  - c. Based on that assessment, design steps and procedures to test compliance with laws and regulations to provide reasonable assurance of detecting both unintentional instances of noncompliance and intentional instances of noncompliance that could have a material effect on the financial statements or the results of a financial related audit.
11. Auditors can obtain information about the applicable laws and regulations from the audited entity. When funding from another level of government is involved and the source of funding is known, the auditor can obtain or corroborate information about the applicable laws and regulations from that source.

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<sup>3</sup>The Single Audit Act (31 U.S.C. 7502 (d) (2) (B)) also requires the auditor to determine and report whether the entity has internal controls that provide reasonable assurance that it is managing federal financial assistance programs in compliance with applicable laws and regulations.



12. The laws and regulations of primary concern in financial audits are those that have a direct and material effect on the determination of financial amounts.<sup>4</sup> Other laws and regulations that pertain more to the operations aspects of an entity often will relate only indirectly to the financial amounts that effect the financial statements or the results of financial related audits.

Errors, Irregularities  
and Illegal Acts

13. In determining compliance with laws and regulations:

**The auditor should design audit steps and procedures to provide reasonable assurance of detecting errors, irregularities, and illegal acts that could have a direct and material effect on the financial statement amounts or the results of financial related audits.**

**The auditor should also be aware of the possibility of illegal acts that could have an indirect and material effect on the financial statements or results of financial related audits.**

14. In fulfilling the above requirements relating to errors, irregularities, and illegal acts, the auditor should follow the guidance contained in the AICPA standards entitled The Auditor's Responsibility to Detect and Report Errors and Irregularities and Illegal Acts By Clients.

Due Care  
Concerning  
Illegal Acts

15. Auditors should exercise due professional care and caution in extending audit steps and procedures relative to illegal acts so as not to interfere with potential future investigations and/or legal proceedings.

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<sup>4</sup>The Single Audit Act (31 U.S.C. 7502 (d) (2) (C)) expands upon these requirements and also requires the auditor to determine and report on whether the entity has complied with laws and regulations that may have a material effect upon each major federal assistance program as defined in the act. Other similar requirements may exist in state and local government jurisdictions.

Due care would include consulting appropriate legal counsel and/or the applicable law enforcement organizations, where appropriate, to determine the audit steps and procedures to be followed.

16. Circumstances may exist where laws, regulations, or policies require the auditor to promptly report indications of certain types of illegal acts to law enforcement or investigatory authorities before extending audit steps and procedures. The auditor may also be required to withdraw from or defer further work on the audit or a portion of the audit in order not to interfere with an investigation. However, the auditor should consider whether the above circumstances would restrict the completion of the remaining portion of the audit or interfere with the auditor's ability to form objective opinions and conclusions. If it restricts or interferes, the auditor should consider discontinuing further action until completion of the investigation, or terminate the audit.
17. Most auditors are not trained to conduct investigations of certain types of illegal acts which are the responsibility of the investigator or law enforcement authorities. However, auditors are responsible for being aware of the characteristics and types of illegal expenditures and acts associated with the area being audited to be able to identify indications that these acts may have occurred.
18. An audit made in accordance with the standards in this statement will not guarantee the discovery of all illegal acts or contingent liabilities resulting from noncompliance. Nor does the subsequent discovery of illegal acts committed during the audit period necessarily mean that the auditor's performance was inadequate provided the audit was made in accordance with these standards.

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## Evidence

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### Working Papers

19. The AICPA field work standards and this statement require that:

**A record of the auditors' work be retained in the form of working papers.**

20. Working papers are the link between field work and the auditors' report. They serve as a record of the results of the audit and the basis of the auditors' opinions.
21. Audit organizations should establish policies and procedures to ensure the safe custody and retention of working papers for a time sufficient to satisfy legal and administrative requirements.
22. Supplemental working paper requirements for financial audits are that working papers should:
- a. Contain a written audit program cross-referenced to the working papers.
  - b. Contain the objective, scope, methodology, and results of the audit.
  - c. Contain sufficient information so that, supplementary oral explanations are not required.
  - d. Be legible with adequate indexing and cross-referencing, and include summaries and lead schedules, as appropriate.
  - e. Restrict information included to matters that are materially important and relevant to the objectives of the audit.
  - f. Contain evidence of supervisory reviews of the work conducted.

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Internal  
Control

23. The AICPA field work standards and this statement require that:

**A sufficient understanding of the internal control structure is to be obtained to plan the audit and to determine the nature, timing, and extent of tests to be performed.**

24. Establishing and maintaining an internal control structure is an important management responsibility. Good internal controls are essential to achieving the proper conduct of government business with full accountability for the resources made available. They also facilitate the achievement of management objectives by serving as checks and balances against undesired actions. An entity's internal control structure consists of the policies and procedures established to provide reasonable assurance that specific entity objectives will be achieved. The internal control structure may include a wide variety of objectives and related policies and procedures, only some of which may be relevant to an audit of the entity's financial statements.
25. For financial audits, the auditor is primarily concerned with policies and procedures that pertain to the entity's ability to record, process, summarize, and report financial data consistent with the assertions embodied in the financial statements, financial related items and information as discussed previously, to ensure compliance with laws and regulations. Other policies and procedures, however, may be relevant if they pertain to data the auditor uses in applying auditing procedures. This may include, for example, policies and procedures that pertain to nonfinancial data that the auditor uses in analytical procedures.
26. An entity generally has internal control structure policies and procedures that are not relevant to a particular audit and therefore need not be considered. For example, policies and procedures concerning the effectiveness, economy, and efficiency of

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**Chapter 4**  
**Field Work Standards for**  
**Financial Audits**

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certain management decision-making processes, while important to the entity, do not ordinarily relate to a financial audit.

27. In fulfilling the audit requirement relating to an understanding of the internal control structure and assessing the level of control risk, the auditor should follow, at a minimum, the guidance contained in the AICPA standard, entitled Consideration of the Internal Control Structure in a Financial Statement Audit.

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# Reporting Standards for Financial Audits

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## Purpose

1. This chapter prescribes standards of reporting for government financial audits. It incorporates the AICPA standards of reporting for financial audits, and does not restate them<sup>1</sup> but rather prescribes supplemental standards of reporting needed to satisfy the unique needs of government financial audits.
2. The reporting standards of the AICPA and the supplemental standards in this chapter apply to both financial statement audits and financial related audits.

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## Statement on Auditing Standards

3. The first supplemental reporting standard for government financial audits is:  
  
**A statement should be included in the auditor's report that the audit was made in accordance with generally accepted government auditing standards.<sup>2</sup> (AICPA standards require that public accountants state that the audit was made in accordance with generally accepted auditing standards. In conducting government audits, public accountants should also state that their audit was conducted in accordance with the standards set forth in chapters 3, 4, and 5.)**
4. The above statement refers to all the applicable standards that the auditors should have followed during their audit. The statement need not be qualified when standards that were not applicable were not followed. However, the statement should be qualified in situations where the auditors did not

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<sup>1</sup> Future AICPA statements will be adopted and incorporated unless GAO excludes them by formal announcement.

<sup>2</sup> Generally accepted government auditing standards (GAGAS) include the audit standards set forth in this publication, Government Auditing Standards - Standards for Audit of Governmental Organizations, Programs, Activities, and Functions, subsequent revisions and interpretations, and guidance concerning these standards

follow an applicable standard. In these situations, the auditors should modify the statement to disclose in the scope section of their report the applicable standard that was not followed, the reasons therefor, and the known effect not following the standard had on the results of the audit.

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**Report on  
Compliance**

5. The second supplemental reporting standard for government financial audits is:

**The auditors should prepare a written report on their tests of compliance with applicable laws and regulations. This report, which may be included in either the report on the financial audit or a separate report, should contain a statement of positive assurance on those items which were tested for compliance and negative assurance on those items not tested.<sup>3</sup> It should include all material instances of noncompliance,<sup>4</sup> and all instances or indications of illegal acts which could result in criminal prosecution.**

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**Positive and  
Negative  
Assurances**

6. Positive assurance consists of a statement by the auditors that the tested items were in compliance with applicable laws and regulations. Negative assurance is a statement that nothing came to the auditors' attention as a result of specified procedures that caused them to believe the untested items were not in compliance with applicable laws

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<sup>3</sup>If a statistically valid and projectable sample of items was tested, an opinion on the relevant universe's compliance may be warranted.

<sup>4</sup>The Single Audit Act (31 U.S.C. 7502 (d) (3)) also requires the auditor to report all instances of noncompliance with laws and regulations found during the audit

and regulations.<sup>5</sup> When the financial audit did not require tests of compliance with laws and regulations, the report should contain a statement that the auditor did not test for compliance with laws and regulations.

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**Noncompliance**

7. All material instances of noncompliance related to the entity's financial statements or the program, award, claim, fund, or group of accounts being audited should be reported. Further, several instances of noncompliance that separately may not be material, but that cumulatively could have a material effect on the financial statements or results of the financial related audit, should be reported. All instances of illegal acts that could result in the audited entity, or an officer or employee of the audited entity, being subject to criminal prosecution should also be reported.
8. Other nonmaterial instances of noncompliance need not be disclosed in the compliance report but should be reported in a separate communication to the audited entity, preferably in writing.<sup>6</sup> Such instances of noncompliance when communicated in a management letter to top management should be referred to in the report on compliance. All communications should be documented in the working papers.
9. In reporting material noncompliance, the auditors should place their findings in proper perspective. The extent of noncompliance should be related to the number of cases examined to give the reader a basis for judging the prevalence of noncompliance.

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<sup>5</sup>The Single Audit Act (31 U.S.C. 7502 (d) (2) (C)) contains additional requirements for the auditor to determine and report on whether the entity has complied with laws and regulations that may have an effect upon each major federal assistance program as defined in the act. Other similar requirements may exist in state and local government jurisdictions.

<sup>6</sup>See footnote 5 above



If a valid statistical and projectable sample was tested, an opinion on compliance may be warranted. In presenting the findings, the auditor should follow the report contents standards, as appropriate, for objectives, scope and methodology, audit results, and views of responsible officials, and the report presentation standards, discussed in chapter 7.<sup>7</sup>

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**Illegal Acts**

10. If, during or in connection with an audit of a government entity, external government auditors become aware of illegal acts or indications of such acts affecting the government entity, they should promptly report to the top official of that entity. The auditor should also consider reporting to the appropriate oversight body. If the top official is believed to be a party to such acts or otherwise implicated, the auditor should in all cases report to the appropriate oversight body. If the acts involve funds received from other government entities, auditors should also promptly report to the proper officials, including the audit officials, of those entities.
11. Internal government auditors auditing a government entity that is external to the government entity to which they are assigned should promptly report to officials and authorities in accordance with the preceding paragraph.

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<sup>7</sup>Audit findings have often been regarded as containing the elements of criteria, condition, and effect, plus cause when problems are found. However, the elements needed for a complete finding depend entirely on the objectives of the audit. Thus, a finding or set of findings is complete to the extent that the audit objectives are satisfied and the report clearly relates those objectives to the finding's elements. It is recognized that material internal control weaknesses and noncompliance found by the auditor may not always have all of these elements fully developed, given the scope and objectives of the specific financial audit. But at least the auditor should identify the condition, criteria and possible asserted effect to provide sufficient information to federal, state, and local officials to permit them to determine the effect and cause in order to take timely and proper corrective action.

12. Internal government auditors auditing within the government entity to which they are assigned should report to the top officials of the entity under audit (unless the official is believed to be a party to such acts) and/or appropriate entity investigative personnel.
13. Public accountants conducting audits of government entities will discharge their responsibilities for reporting illegal acts or indications of such acts found during or in connection with an audit by promptly reporting to the top official of the entity arranging for the audit (including audit committees or others with equivalent authority). The auditor should also consider reporting to the appropriate oversight body. If the audited entity and the top official is believed to be a party to such acts or otherwise implicated, the auditor should in all cases report to the appropriate oversight body. Also, when the illegal acts involve funds received from other government entities, the audited entity should report to the proper officials, including those at the audit organization, of those entities. If the audited entity does not do so within a reasonable time or was unable to because the top official was involved, the auditor should report to the officials of those other government entities.
14. It is the responsibility of an entity receiving the information from the various auditors, both the audited entity and external funding entity, to report to appropriate law enforcement authorities and other government entities whose funds are involved.
15. In the case of an audit of government funds received by a nongovernment entity, the auditors should promptly report to the appropriate government entity requiring or arranging for the audit and such other officials designated by law or regulation to receive the audit reports.

16. Illegal acts or indications of such acts that auditors become aware of need not be included in the required audit reports, but may be covered in a separate written report and submitted in accordance with the preceding paragraphs, thus permitting the required report or reports to be released. However, auditors generally should not release information or reports containing information on such acts or reports with references that such acts were omitted from reports, without consulting with appropriate legal counsel, since this release could interfere with legal processes, subject the implicated individuals to undue publicity, or subject the auditor to potential legal action.

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Report on  
Internal  
Controls

17. The third supplemental reporting standard for government financial audits is:

**The auditors should prepare a written report on their understanding of the entity's internal control structure and the assessment of control risk made as part of a financial statement audit,<sup>8</sup> or a financial related audit. This report may be included in either the auditor's report on the financial audit or a separate report. The auditor's report should include as a minimum: (1) the scope of the auditor's work in obtaining an understanding of the internal control structure and in assessing the control risk, (2) the entity's significant internal controls or control structure including the controls established to ensure compliance with laws and regulations that have a material impact on the financial statements and results of the financial related audit, and**

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<sup>8</sup>This standard does not require any additional audit work other than that required as part of a financial audit described in this statement. However, the Single Audit Act (31 U.S.C. 7502 (d) (2) (B)) expands upon this requirement and also requires that the auditor determine and report whether the entity has internal controls that provide reasonable assurance that it is managing federal financial assistance programs in compliance with applicable laws and regulations.

**(3) the reportable conditions, including the identification of material weaknesses, identified as a result of the auditor's work in understanding and assessing the control risk.**

18. In identifying the scope of the auditor's work, the report should include a description of the work conducted. Generally accepted government auditing standards require the auditor to understand and assess the audited entity's internal control structure, which consists of the control environment, accounting systems, and specific internal control procedures, to plan the financial audit. The extent of the auditor's assessment can vary from one audit to another and within different elements of an entity's internal control structure, based on both the auditor's understanding of that internal control structure and the auditor's judgment about alternative forms of audit evidence. That understanding and assessment by itself is not sufficient for expressing an opinion about the design and operation of the entity's internal control structure as a whole or of its specific elements.
19. The auditor may limit the consideration of internal control structure for a number of reasons. These include:
  - a. An adequate internal control structure does not exist for reliance thereon because of the small size of the entity.
  - b. The auditor may conclude that it would be inefficient to evaluate the effectiveness of internal control structure policies and procedures and that the audit can be conducted more efficiently by expanding substantive audit tests, thus placing very little reliance on the internal control structure.
  - c. The existing internal control structure may contain so many weaknesses that the auditor has no choice but to rely on substantive testing, thus virtually ignoring the internal control structure.

- d.** The objectives of a financial related audit did not require an understanding or assessment of the internal control structure.
20. The above circumstances should be documented in the working papers and included in the report on internal control.
21. In identifying the significant internal controls, the report should list those controls identified by the auditor.
22. The following are examples of different ways in which the internal control structure might be classified. Auditors may modify these examples or use other classifications as appropriate for the particular circumstances on which they are reporting.
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**Cycles of the entity's activity**

Treasury or financing  
Revenue/receipts  
Purchases/disbursements  
External financial reporting

**Financial statement captions**

Cash and cash equivalents  
Receivables  
Inventory  
Property and equipment  
Payables and accrued liabilities  
Debt  
Fund balance

(continued)

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**Chapter 5**  
**Reporting Standards for**  
**Financial Audits**

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**Accounting applications**

Billings  
Receivables  
Cash receipts  
Purchasing and receiving  
Accounts payable  
Cash disbursements  
Payroll  
Inventory control  
Property and equipment  
General ledger

**Controls used in administering compliance with laws  
and regulations**

General controls  
Specific controls

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23. In reporting reportable conditions, the auditors should identify those that are material weaknesses. The auditors should also follow report content standards, as appropriate, for objectives, scope and methodology, audit results, and views of responsible officials, and the report presentation standards, discussed in chapter 7.<sup>9</sup>
24. The AICPA's statements on auditing standards, and interpretations thereof, give guidance on reporting conditions that relate to an entity's internal control structure observed during an audit. The supplemental requirements for reporting on internal controls stated in the above standard should also be included in the report.

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<sup>9</sup>See footnote 7 on page 5-4.

25. Nonreportable conditions in an audited entity's internal control structure not included in the required reports, should be separately communicated to the audited entity, preferably in writing. Such control structure conditions when communicated in a management letter to top management should be referred to in the report on internal controls. All communications should be documented in the working papers.

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Reporting on  
Financial  
Related Audits

26. The fourth supplemental reporting standard for government financial audits is:
- Written audit reports are to be prepared giving the results of each financial related audit.**
27. The AICPA reporting standards, to the extent that they are relevant, also apply to financial related audits. However, if the AICPA reporting standards are not relevant, the reporting standards in chapter 7 should be followed by the auditor in reporting on financial related audits to the extent appropriate.

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Privileged and  
Confidential  
Information

28. The fifth supplemental reporting standard for government financial audits is:
- If certain information is prohibited from general disclosure, the report should state the nature of the information omitted and the requirement that makes the omission necessary.**
29. Certain information may be prohibited from general disclosure by federal, state, or local laws or regulations. Such information may be provided on a need-to-know basis only to persons authorized by law or regulation to receive it.

30. If the auditors are prohibited by such requirements from including pertinent data in the report, they should state the nature of the information omitted and the requirement that makes the omission necessary. The auditors should obtain assurance that a valid requirement for the omission exists and, where appropriate, consult with legal counsel.
31. Auditors should consult with appropriate legal counsel before releasing reports which refer to the fact that illegal acts or indications of such acts were omitted from reports.<sup>10</sup>

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Report  
Distribution

32. The sixth supplemental reporting standard for government financial audits is:

**Written audit reports are to be submitted by the audit organization to the appropriate officials of the organization audited and to the appropriate officials of the organizations requiring or arranging for the audits, including external funding organizations, unless legal restrictions, ethical considerations, or other arrangements prevent it. Copies of the reports should also be sent to other officials who have legal oversight authority or who may be responsible for taking action and to others authorized to receive such reports. Unless restricted by law or regulation, copies should be made available for public inspection.<sup>11</sup>**

33. Audit reports should be distributed in a timely manner to as many interested officials as is practicable. In some cases, the subject of the audit may involve material that is classified for security purposes or cannot be released to particular parties or to the

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<sup>10</sup>See paragraph 16 on page 5-6.

<sup>11</sup>See the Single Audit Act of 1984 (31 U.S.C. 7502 (f)) and section 13 (f) of OMB Circular A-128 for the distribution of reports on single audits of state and local governments.



public for other valid reasons. Generally, however, the report should be distributed to officials interested in the results. Such officials include those designated by law or regulation to receive such reports, those responsible for taking action, legislators, and those of other levels of government that have provided funds to the audited entity.

34. When public accountants are engaged, the engaging organization must ensure that appropriate distribution is made. If the public accountants are to make the distribution, the engagement agreement should indicate what officials or organizations should receive the report.
35. Internal auditors should follow their entity's own arrangements and statutory requirements for distribution. Usually, they report to their entity's top management and the entity's management is responsible for distribution of the report.
36. The auditor's report on the financial audit, the report on compliance, and the report on internal control, if separate reports, should normally be bound together so that the three reports are issued together in one bound document. If the three reports are not issued together in one bound document, it is recommended that the auditor's report on the financial audit include a statement that reports on compliance and internal control were also issued.

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# Field Work Standards for Performance Audits

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## Purpose

1. This chapter prescribes standards of field work for government performance audits.

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## Planning

2. The first field work standard for government performance audits is:

**Work is to be adequately planned.**

3. This standard places responsibility on the auditor or audit organization to thoroughly plan an audit. This includes defining the audit objectives and planning how they can be attained while establishing a balance between audit scope, time frames, and staff-days to be spent to ensure optimum use of audit resources. The details of the plan for the audit should be included in the audit program.
4. Planning is important to ensure that the audit results will satisfy the objectives of the audit. Adequate planning is especially important in performance audits because the methodology and implementing steps and procedures employed in such audits are varied and complex.
5. Planning is also important in intergovernmental auditing because, in many instances, the audit work conducted at one level of government should be coordinated with other audit work conducted at the same level or different levels.

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## Considerations in Planning

6. The information needed by the auditor to plan an audit varies with the audit objectives and the entity to be audited. In many instances, an audit survey of the entity may be made before preparing a plan for conducting the field work. The survey is an effective method to help identify specific audit areas and to obtain information for use in planning. It is a process for quickly gathering information, without

detailed verification, on the entity's organization, programs, activities, and functions.<sup>1</sup>

7. A survey will provide information about the key systems and procedures used for managing finances and operations and for evaluating and reporting performance. It will also provide information about the size and scope of the entity's activities as well as areas in which there may be internal control weaknesses, uneconomical or inefficient operations, lack of effective goal achievement, or lack of compliance with laws and regulations. However, tests to determine the significance of such matters are generally conducted in the detailed audit work as specified in the audit programs.
8. Adequate planning should include consideration of:
  - a. Audit objectives, scope, and methodology.
  - b. Criteria for assessing performance (where applicable).
  - c. Coordination with other government auditors, when appropriate, including work already conducted and other work that may be intended.
  - d. Skill and knowledge of the personnel to staff the assignment and the use of consultants, experts, and specialists.
  - e. Compliance with laws and regulations and potential abuse and illegal acts. (See paragraph 30 below.)
  - f. Assessment of internal controls. (See paragraph 49 below.)

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<sup>1</sup>The concepts and procedures of the audit survey are discussed in GAO publication entitled, The Audit Survey - A Key Step in Auditing Government Programs.

**g. Materiality and/or significance and audit risk.**  
(See chapter 3, paragraph 33.)

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**Audit Objectives,  
Scope, and  
Methodology**

9. Determining and explaining the rationale for selecting an audit's objectives, scope, and methodology require logical and systematic thinking.
10. The first step in planning a performance audit is to define carefully the audit objectives. The statement of audit objectives should clearly articulate what the audit is to accomplish. This means phrasing the objectives to identify the audit subject and the performance aspect to be included. Because it is rare for one audit to cover all aspects of performance, it is important to know, in planning, what aspect or aspects are going to be included. This is critical in establishing the audit boundaries.
11. Audit findings have often been regarded as containing the elements of criteria, condition, and effect, plus cause when problems are found. Recommendations and conclusions are added, as appropriate, in reporting. However, the elements needed for a complete finding and report depend on the objectives of the audit. Thus, the objectives should be phrased to identify those finding and reporting elements that are to be developed. For example, the auditor may have as an objective to ascertain the level of performance being achieved; or to go a step farther and determine if that level of performance is satisfactory. If not satisfactory, the auditor may or may not have as an objective, identifying the cause and making recommendations. Knowing what finding and reporting elements are to be developed is critical in planning so as to gather the evidence necessary to support the finding elements that may be required.
12. The objectives of an audit extend throughout every phase of the audit, from the selection of scope, methodology, and staff, to the conduct of the audit, and the timing and nature of reports. Time invested in determining an audit's objectives is usually time

well spent because an audit with clear objectives is unlikely to result in wasted resources, delays, and poor quality reports. In analyzing possible audit objectives, auditors need to consider all that they know about the significance of an issue, the contribution they can make, and the availability of data and resources.

13. Decisions about the scope of audit work necessary to achieve the audit objectives are based on such factors as, the availability and recency of data, and the ease and appropriateness with which particular analytic techniques could be applied. Questions to be considered include: What period should be considered? Will the results be projected? What level of validity is needed in documenting the existence of a problem and its cause? What comparisons will be made?
14. "Methodology" refers to the process used to gather and analyze data and to reach conclusions and recommendations. The methodology selected needs to provide evidence that will achieve the objectives of the audit.

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Criteria

15. *When criteria are needed to evaluate matters subject to audit, the audit plan should, where possible, state the criteria to be used. Criteria are standards against which the adequacy of performance can be assessed. In selecting criteria, auditors have a responsibility to use only criteria that are suitable. Suitable criteria are those that are relevant to the matters being audited and are reasonable and attainable.*

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Coordination

16. In government auditing, a central audit agency, such as a federal or state audit organization, may be responsible for audits involving work by its field office staff at several different locations. The central agency should carefully plan these audits to

ensure that they will be conducted effectively and efficiently.

17. Planning for audits should be tailored to the specific audit objectives. Ordinarily the central audit agency should specify the compliance requirements to be considered by the auditor, the aspects of economy and efficiency to be included in the audit, and the program goals and objectives, and measurement criteria to be used. Unless such planning is carefully done and communicated to the participating staffs, the audit results may not meet the needs and expectations of the central audit agency. Unplanned audit effort will make it difficult to compare and consolidate the results from various locations.
18. An audit, or certain aspects of an audit to be conducted at several locations by different staff can be planned more efficiently and economically by a designated audit organization. For example, researching the program laws and regulations and establishing clear and concise audit objectives are time-consuming. To have each participating staff do this would be duplicative and more costly than necessary. Some audits require even closer coordination because a given event may be audited at more than one location by different staffs. The preparation of audit programs for such audits is an integral part of the standard for planning.
19. In many instances, audits of the same organizations, programs, activities, or functions may be required by federal, state, and local laws, regulations, and ordinances. When this situation exists, to avoid duplicate efforts, auditors in planning their work should coordinate with other government auditors to determine whether they have any audit work planned, in process, or completed that may be used to satisfy some or all of their planned work.

**Personnel**

20. Staff planning should include:
- a. Assigning staff with the appropriate skills and knowledge for the job.
  - b. Assigning an adequate number of experienced staff and supervisors to the audit. Consultants should be used when necessary.
  - c. Providing for on-the-job training of staff.

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**Audit Program**

21. Written audit programs should be prepared for each audit and are essential to conducting audits efficiently and effectively. Audit programs provide:
- a. A description of the methodology and suggested audit steps and procedures to be conducted to accomplish the audit objectives.
  - b. A systematic basis for assigning work to supervisors and staff.
  - c. The basis for a summary record of work.
22. Written audit programs should not be used merely as a checklist of steps to be conducted. Effective work on performance audits requires that the staff understand the objectives of the audit and use their own initiative in determining the appropriateness of steps in the audit program and in assessing the results of the work.
23. Audit programs should generally include the following information:
- a. Introduction and background: Information should be provided about the legal authority for the audited organization, program, activity, or function; its history and current objectives; its principal locations; and similar information needed by the auditor to understand and carry out the audit program.

**b. Objectives of the audit:** The objectives should be clearly stated.

**c. Scope of the audit:** The scope should be clearly described.

**d. Audit methods:** The methodology should be clearly described, and for most audits, it is desirable to include suggested steps and procedures, and sampling plans for the auditors to follow. For coordinated audits, the audit organization planning the work should ordinarily suggest the audit methods to be followed in the audit to be sure that the data obtained from participating locations will be comparable. However, this should be done in a manner that does not restrict the auditor's professional judgment.

**e. Definition of terms:** Any known unique terms used by the audited entity should be defined or explained.

**f. Special instructions:** The auditors should clearly understand and reach early agreement on the responsibilities in each audit. This agreement is especially important when the work is to be directed by a central audit organization with work to be conducted at several different locations. This section of the program may be used to list the responsibilities of each audit organization, such as preparing audit programs, conducting audit work, supervising audit work, drafting reports, handling auditee comments, and processing the final report.

**g. Report:** The audit program should set forth the general format (if not included in organization audit policy and procedures) to be followed in the audit report and cite, to the extent possible, the types of information to be in it.



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Supervision

24. The second field work standard for government performance audits is:
- Staff are to be properly supervised.**
25. This standard places responsibility on the auditor and audit organization for seeing that staff who are involved in accomplishing the objectives of the audit receive appropriate guidance and supervision to ensure that the audit work is properly conducted, the audit objectives are accomplished, and staff are provided effective on-the-job training. External consultants and specialists also should be given appropriate guidance.
26. The most effective way to ensure the quality and expedite the progress of an assignment is by exercising proper supervision from the start of the planning to the completion of audit work and reporting. Supervision adds seasoned judgment to the work performed by less experienced staff and provides necessary training for them.
27. Assigning and using staff is important to satisfactory achievement of objectives. Since skills and knowledge vary among auditors, work assignments must be commensurate with abilities.
28. Supervisors should satisfy themselves that staff members clearly understand their assigned tasks before starting the work. Staff should be informed of not only what work they are to do and how they are to proceed but also why the work is to be conducted and what it is expected to accomplish. With experienced staff, the supervisors' role may be more general. They may outline the scope of the work and leave details to assistants. With a less experienced staff, the supervisor may have to perform many details and specify to the staff how to conduct specific data gathering and analysis techniques.

29. Supervisory reviews of audit work and the report should be timely and determine whether (1) conformance with audit standards is obtained, (2) the audit programs are followed, unless deviation is justified and authorized, (3) the audit work has been conducted with due professional care, (4) the working papers adequately support findings and conclusions and provide sufficient data to prepare a meaningful report, and (5) the audit objectives are met. Supervisory reviews of the work conducted should be documented in the working papers.

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Legal and  
Regulatory  
Requirements

30. The third field work standard for government performance audits is:
- An assessment is to be made of compliance with applicable requirements of laws and regulations when necessary to satisfy the audit objectives.**
31. In government auditing, compliance with laws and regulations is important because government organizations, programs, services, activities, and functions are usually created by law and are subject to more specific rules and regulations than the private sector. For example, what is to be done, who is to do it, the goals and objectives to be achieved, the population to be served, and how much can be spent on what are usually set forth in laws and regulations.
32. The need to assess compliance with requirements of laws and regulations, and the nature of that assessment, varies with the objectives of the audit. Where assessment of compliance is called for, this standard places responsibility on the auditor to design steps and procedures that will provide reasonable assurance that the audited entity has adhered to the requirements of laws and regulations applicable to the audit which, if not followed, could significantly affect the audit results.

33. Management is responsible for establishing an effective system of internal control to ensure compliance with laws and regulations. In designing steps and procedures to assess compliance, auditors should consider the entity's internal controls.
34. The nature of requirements of laws and regulations that the auditor might assess are illustrated below.
  - a. Economy and efficiency: Compliance with laws and regulations that could significantly affect the acquisition, protection, and use of the entity's resources, and the quantity, quality, timeliness, and cost of the products and services it produces and delivers.
  - b. Program: Compliance with laws and regulations pertaining to the objectives of the entity's programs, activities, and functions; the manner in which programs and services are to be delivered; the population a program or service is to serve; and whether the programs, activities, and functions are being carried out in conformity with these laws and regulations.
35. Auditors are responsible for determining which requirements of laws and regulations are to be considered in the audit. This responsibility requires that those planning the audit be knowledgeable of the compliance requirements that apply to the subject under audit. Because the laws and regulations that may apply to a specific audit are often numerous, the auditors need to exercise professional judgment in determining those laws and regulations that might have a significant impact on the audit objectives.
36. A variety of sources exist for information on requirements of laws and regulations. The audited entity is expected to know the applicable requirements, and thus is a good first source. When funding from another level of government is involved and the source is known, auditors can obtain and/or

corroborate information about the applicable requirements from the funding entity. Auditors should consult with appropriate legal counsel when questions arise concerning application and the interpretation of laws and regulations.

37. Where an assessment of compliance with laws and regulations is required:

**Auditors should design the audit to provide reasonable assurance of detecting abuse or illegal acts that could significantly affect the audit objectives.**

38. In conducting audits in accordance with this standard, the auditors choose and perform audit steps and procedures that, in their professional judgment, are appropriate in the circumstances to achieve the audit objectives. These audit steps and procedures are designed to obtain sufficient, competent, and relevant evidence that will provide a reasonable basis for their judgments and conclusions regarding the audit objectives.
39. This standard places responsibility on the auditor when assessing compliance with laws and regulations to:
- a. Assess, for each applicable compliance requirement, the risk that abuse and illegal acts could occur.
  - b. Based on that assessment, design steps and procedures to provide reasonable assurance of detecting abuse or illegal acts.
40. When audit steps and procedures indicate that abuse or illegal acts have or may have occurred, the auditor needs to determine the extent to which these acts significantly affect the audit results.
41. Detecting noncompliance resulting from illegal acts is generally difficult. Doing so commonly requires

special steps, and auditors are expected to devise and apply such steps as may be effective. Because a sound internal control structure can be effective in ensuring compliance, an assessment of the control structure is generally useful.

42. In all performance audits:

**Auditors should be alert to situations or transactions that could be indicative of abuse or illegal acts.**

43. When information comes to the auditor's attention (through audit procedures, tips, or other means) indicating that abuse or illegal acts may have occurred, the auditor should consider the potential impact of these acts on the audit results. If these acts could significantly affect the audit results, the auditor should extend the audit steps and procedures, as necessary (a) to determine whether the acts occurred and (b) if so, to determine the extent to which these acts significantly affect the audit results.

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**Due Care  
Concerning  
Illegal Acts**

44. When an audit is conducted under contract and the contract does not permit the auditor to unilaterally extend steps and procedures, the auditor should obtain written approval to perform the necessary additional work. If such approval is not given to the auditor, a scope impairment generally exists which should be stated in the auditor's report.
45. Auditors should exercise due professional care and caution in pursuing indications of illegal acts so as not to interfere with potential future investigations and/or legal proceedings. Due care would include consulting appropriate legal counsel and/or the applicable law enforcement organization, where appropriate, before proceeding.

46. Circumstances may exist in which laws, regulations, or policy require auditors to promptly report indications of illegal acts to law enforcement or investigatory authorities before extending audit steps and procedures. The auditor may also be required to withdraw from, or defer further work on, the audit or a portion of the audit in order not to interfere with an investigation. However, the auditor should consider whether this would restrict the completion of the remaining portion of the audit or interfere with the auditor's ability to form objective opinions and conclusions. If it restricts or interferes, the auditor should terminate the audit or discontinue further action until completion of the investigation. (See reporting requirements in chapter 7.)
47. Most auditors are not trained to conduct investigations of certain types of illegal acts which are the responsibility of the investigator or law enforcement authorities. However, auditors are responsible for being aware of the characteristics and types of vulnerabilities and potential illegal acts associated with the area being audited in order to be able to identify indications that these acts may have occurred.
48. An audit made in accordance with the standards in this statement will not guarantee the discovery of all abuse or illegal acts. Nor does the subsequent discovery of abuse or illegal acts committed during the audit period necessarily mean the auditors' performance was inadequate, provided the audit was made in accordance with the standards in this statement.

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**Internal  
Control**

49. The fourth field work standard for government performance audits is:

**An assessment should be made of applicable internal controls when necessary to satisfy the audit objectives.**

50. Management is responsible for establishing an effective system of internal controls. The lack of administrative continuity in government units because of continuing changes in elected legislative bodies and in administrative organizations increases the need for an effective internal control system.
51. Internal controls include the plan of organization and methods and procedures adopted by management to ensure that its goals and objectives are met; that resources are used consistent with laws, regulations, and policies; that resources are safeguarded against waste, loss, and misuse; and that reliable data are obtained, maintained, and fairly disclosed in reports.
52. The need to assess internal controls and the focus of that assessment varies with the objectives of the audit.
- a.** An assessment is required in audits having as objectives the assessment of the adequacy of particular internal controls. Here, the auditor should design steps and procedures to assess the effectiveness of the prescribed control procedures or actual control practices.
- b.** An assessment of internal controls is a natural adjunct in audits having as their objectives an assessment of the adequacy of the process (e.g., procedures and practices) for carrying out a particular program, service, activity, or function. Here, the auditor should design steps and procedures to determine if controls needed in the process exist and if the existing controls are adequate to achieve the desired objectives.
- c.** An assessment may be necessary in audits having as objectives determining the underlying cause of unsatisfactory performance (e.g., lack of improvement achieved by recently installed automation intended to increase productivity). Here, if the

unsatisfactory performance could occur from weaknesses in internal controls, the auditor should design steps and procedures to assess the adequacy of those specific controls that if weak could cause the unsatisfactory performance.

53. The focus of the assessment of internal controls varies with the objective of the audit being conducted.
- a. Economy and efficiency audits:** The auditors may assess those policies, procedures, practices, and controls applicable to the programs, functions, and activities, under audit to the extent necessary, as determined by the audit objectives.
- b. Program audits:** The auditors may assess those policies, procedures, practices, and controls which specifically bear on the attainment of the goals and objectives specified by the law or regulations for the organization, program, activity, or function under audit to the extent necessary, as determined by the audit objectives.
54. Auditors may be required or contracted to audit or assess particular internal controls. Such assessments should be made in accordance with the standards in this statement.<sup>2</sup>
55. Internal auditing is an important part of internal control, and the auditors should consider this in conducting the audit. Where an assessment of internal controls is called for, external auditors should consider the extent to which the work of the internal auditors can be relied upon to help provide reasonable assurance that internal control is functioning properly and to prevent duplication of effort.<sup>3</sup>

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<sup>2</sup>Examples include the Federal Managers' Financial Integrity Act of 1982 (Public Law 97-255) and the laws of several states

<sup>3</sup>See chapter 3, paragraph 37 for guidance the auditor should follow when relying on the work of others.



56. In view of the wide range in the size and nature of government organizations, programs, activities, and functions and in view of their organizational structures and operating methods, no single pattern for internal audit and review activities can be specified. Many government entities have these activities identified by other names, such as inspection, appraisal, investigation, organization and methods, or management analysis. These activities assist management by reviewing selected functions.

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Evidence

57. The fifth field work standard for government performance audits is:

**Sufficient, competent, and relevant evidence is to be obtained to afford a reasonable basis for the auditors' judgments and conclusions regarding the organization, program, activity, or function under audit. A record of the auditors' work is to be retained in the form of working papers. Working papers may include tapes, films, and discs.**

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Types of  
Evidence

58. Evidence may be categorized as (1) physical, (2) documentary, (3) testimonial, and (4) analytical.

**a. Physical evidence:** Physical evidence is obtained by direct inspection or observation of (1) activities of people, (2) property, or (3) events. Such evidence may be documented in the form of memoranda summarizing the matters inspected or observed, photographs, charts, maps, or actual samples.

**b. Documentary evidence:** Documentary evidence consists of created information such as letters, contracts, accounting records, invoices, and management information on performance.

**c. Testimonial evidence:** Testimonial evidence is obtained from others through statements received in response to inquiries or through interviews.

Statements important to the audit should be corroborated when possible with additional evidence. Testimonial evidence also needs to be evaluated from the standpoint of whether the individual may be biased or only have partial knowledge about the area.

**d. Analytical evidence:** Analytical evidence includes computations, comparisons, reasoning, and separation of information into components.

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**Tests of  
Evidence**

59. The evidence should meet the basic tests of sufficiency, relevance, and competence. The working papers should reflect the details of the evidence and disclose how it was obtained.

**a. Sufficiency:** Sufficiency is the presence of enough factual and convincing evidence to support the auditors' findings, conclusions, and any recommendations. Determining the sufficiency of evidence requires judgment. When appropriate, statistical methods may be used to establish sufficiency.

**b. Relevance:** Relevance refers to the relationship of evidence to its use. The information used to prove or disprove an issue is relevant if it has a logical, sensible relationship to that issue. Information that does not is irrelevant and therefore should not be included as evidence.

**c. Competence:** To be competent, evidence should be valid and reliable. In evaluating the competence of evidence, the auditors should carefully consider whether reasons exist to doubt its validity or completeness. If so, the auditors should obtain additional evidence or reflect the situation in the report.

60. The following presumptions are useful in judging the competence of evidence. However, these presumptions are not to be considered sufficient in themselves to determine competence.

- a.** Evidence obtained from an independent source is more reliable than that secured from the audited organization.
  - b.** Evidence developed under a good system of internal control is more reliable than that obtained where such control is weak, unsatisfactory, or nonexistent.
  - c.** Evidence obtained through physical examination, observation, computation, and inspection is more reliable than evidence obtained indirectly.
  - d.** Original documents are more reliable than copies.
  - e.** Testimonial evidence obtained under conditions where persons may speak freely is more credible than testimonial evidence obtained under compromising conditions (e.g., where the persons may be intimidated).
- 61.** Auditors should, when they deem it useful, obtain from officials of the audited entity written representations concerning the relevance and competence of the evidence they obtain.

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**Reliability of  
Evidence From  
Computer-Based  
Systems**

- 62.** When computer-processed data are an important or integral part of the audit and the data's reliability is crucial to accomplishing the audit objectives, auditors need to satisfy themselves that the data are relevant and reliable. This is important regardless of whether the data are provided to the auditor or the auditor independently extracts them. To determine the reliability of the data, the auditors may either (a) conduct a review of the general and application controls in the computer-based systems including tests as are warranted;<sup>4</sup> or (b) if the general and

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<sup>4</sup>When the reliability of a computer-based system is the primary objective of the audit, the auditors should conduct a review of the system's general and application controls.

application controls are not reviewed or are determined to be unreliable, conduct other tests and procedures.

63. When computer-processed data are used by the auditor, or included in the report, for background or informational purposes and are not significant to the audit results, citing the source of the data in the report will usually satisfy the reporting standards for accuracy and completeness set forth in this statement.

Review of General  
and Application  
Controls

64. In reviewing the general and application controls, the auditor is to consider the effectiveness of those general controls relevant to the application system being reviewed. General controls are normally applicable to all data processing being carried out within an installation and provide a control environment affecting the applications being processed. Application controls, however, apply on an individual basis, and may vary among applications.

Review of General  
Controls

65. General controls include the plan of organization and methods and procedures that apply to the overall computer operations in an agency. In reviewing the general controls, the auditor should determine whether the controls (a) have been designed according to management direction and known legal requirements and (b) are operating effectively to provide reliability of, and security over, the data being processed. The objectives and procedures followed in conducting this work are discussed in the three areas below.
66. Organization and management controls: The auditor should determine whether (a) there is a clear assignment of responsibilities and accountability for planning, managing, and controlling the functions of the data processing organization, (b) personnel are qualified and adequately trained and supervised, and (c) there is proper separation of

duties. Such controls will help ensure that the organization's objectives are achieved, and that errors or irregular acts are prevented or detected.

67. Security controls: The auditor should determine whether adequate security is provided over the computer programs, data files, telecommunications network, and input and output materials. These controls, such as physical restrictions and the use of passwords to limit system access, help ensure that only authorized persons are granted access to the computer system for authorized purposes.
68. Systems software and hardware controls: Computer systems are controlled by systems software such as operating, data base management, and program library systems. Systems software and hardware normally include built-in error-checking features to detect any errors during processing. The auditor should be aware (a) of the procedures used to ensure that the systems software and hardware are functioning properly, and (b) that when errors are detected, appropriate and authorized corrective actions are taken. The auditor should also be aware of the controls the systems software can exercise over the system, how these controls can be bypassed or overridden, and how modifications to the software are controlled.
69. Application controls are designed to ensure the authority of data origination, accuracy of data input, integrity of processing, and verification and distribution of output. The auditor should review the application controls upon which the auditor is relying to assess their reliability to process only authorized data and to process them promptly, accurately, and completely. This includes a review of the controls used to ensure that application software and later modifications are authorized and tested before implementation. These controls are

Review of  
Application  
Controls

intended to protect the integrity of the application software.

Testing for Data  
Reliability

70. The degree of testing needed to determine data reliability generally increases to the extent that the general or application controls were determined to be unreliable or were not reviewed. Testing procedures could include:
- a.** Confirming computer-processed data with independent sources, such as third parties, and knowledgeable internal sources, such as regular users of the data, and suppliers of data.
  - b.** Comparing the data with source documents, or physical counts and inspections.
  - c.** Reviewing agency test procedures and results, and processing test transactions through the application.

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Working Papers

71. Working papers are the link between field work and the audit report. They should contain the evidence to support the findings, judgments, and conclusions in the report. Audit organizations need to establish policies and procedures for the preparation and maintenance of working papers, including safe custody and retention for a time sufficient to satisfy legal and administrative requirements.
72. As a general guideline, working papers should:
- a.** Contain a written audit program cross-referenced to the working papers.
  - b.** Contain adequate indexing and cross-referencing, schedules, and summaries.
  - c.** Be dated and signed by the preparer.

- d.** Be reviewed by a supervisor. (That review should be documented in the working papers.)
  - e.** Be complete and accurate to provide proper support for findings, judgments, and conclusions, and to enable demonstration of the nature and scope of work conducted.
  - f.** Be understandable without oral explanations. They should also be complete and yet concise. Anyone using them should be able to readily determine their purpose, data sources, the nature and scope of the work conducted, and the preparer's conclusions. Conciseness is important, but clarity and completeness should not be sacrificed just to save time or paper.
  - g.** Be as legible and neat as practicable. Otherwise the working papers may lose their worth as evidence.
  - h.** Be restricted to matters that are significant and relevant to the objectives of the assignment.
- 73.** There are no substitutes for a working understanding of the audit objectives, the reasons for conducting a specific task, and knowing how the task will satisfy the objectives. This understanding comes from well-planned and well-organized work programs and effective instructions by supervisors. The practice of having all working papers contain clear statements of purpose is very helpful in ensuring that information accumulated is properly related to audit objectives and reporting.

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# Reporting Standards for Performance Audits

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## Purpose

1. This chapter prescribes standards of reporting for government performance audits. The report "Contents" and "Presentation" standards may also apply for some financial audits.

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## Form

2. The first reporting standard for government performance audits is:

**Written audit reports are to be prepared communicating the results of each government audit.**

3. This standard is not intended to limit or prevent discussion of findings, judgments, conclusions, and recommendations with persons who have responsibilities involving the area being audited. On the contrary, such discussions are encouraged. However, a written report should be prepared regardless of whether such discussions are held.
4. Written reports are necessary to (a) communicate the results of audits to officials at all levels of government, (b) make the results less susceptible to misunderstanding, (c) make the results available for public inspection, and (d) facilitate follow-up to determine whether appropriate corrective actions have been taken.
5. When an audit is terminated prior to completion, the auditor should communicate the termination to the auditee and other appropriate officials, preferably in writing. The auditor should also prepare a memorandum for the record briefly summarizing the results of the work conducted and explaining why the audit was terminated.



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Timeliness

6. The second reporting standard for government performance audits is:

**Reports are to be issued promptly so as to make the information available for timely use by management and legislative officials, and by other interested parties.**

7. To be of maximum use, the report must be timely. A carefully prepared report may be of little value to decisionmakers if it arrives too late. Therefore, the audit organization should plan for the timely issuance of the audit report and conduct the audit with this goal in mind.
8. The auditors should consider interim reporting of significant matters to appropriate officials during the audit. Such communication, which may be oral or written, is not a substitute for a final written report, but it does alert officials to matters needing immediate attention and permits them to take corrective action before the final report is completed.

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Report  
Contents

9. The third reporting standard for government performance audits covers the report contents.

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Objectives,  
Scope, and  
Methodology

10. **The report should include a statement of the audit objectives and a description of the audit scope and methodology.**
11. Knowledge of the objectives of the audit, and the audit scope and methodology for achieving the objectives, is needed by readers to understand the purpose of the audit, judge the merits of the audit work and what is reported, and understand any significant limitations.

Objectives

12. The statement of objectives being reported on should explain why the audit was made and state

what the report is to accomplish. Articulating what the report is to accomplish normally involves identifying the audit subject and the aspect of performance examined, and because what is reported depends on the objectives, communicating what finding elements are discussed and whether conclusions and recommendations are being given.

13. The statement of objectives tells the reader the boundaries of the audit. To preclude misunderstanding in cases where the pursued objectives are particularly limited and broader objectives can be inferred, it may be necessary to clearly define the audit boundaries by stating objectives that were not pursued.
14. The statement of scope should describe the depth and coverage of audit work conducted to accomplish the audit's objectives. It should, as applicable, explain the relationship between the universe and what was audited, identify organizations and geographic locations at which audit work was conducted and the time period covered, cite the kinds and sources of evidence used and the techniques used to verify it, and explain any quality or other problems with the evidence. If unverified data are used, this needs to be stated. Any constraints imposed on the audit approach by data limitations or scope impairments (see chapter 3, paragraph 42) are to be disclosed.
15. The statement on methodology should clearly explain the evidence gathering and analysis techniques used to accomplish the audit's objectives. The explanation should identify any assumptions made in conducting the audit, describe any comparative techniques applied and measures and criteria used to assess performance, and if sampling is involved, describe the sample design and state why it was chosen.

Scope and  
Methodology

16. Every effort should be made to avoid any misunderstanding by the reader concerning the work that was and was not done to achieve the audit objectives, particularly when the work was limited by relying on internal controls or because of constraints on time or resources.

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Audit Findings  
and Conclusions

17. **The report should include a full discussion of the audit findings, and where applicable, the auditor's conclusions.**

Findings

18. The report should present the findings and finding elements developed in response to the audit objective.<sup>1</sup> Sufficient, competent and relevant information about findings should be included to promote adequate understanding of the matters reported and to provide convincing, but fair presentations in proper perspective. Appropriate background information that readers need to understand the findings should also be included.
19. Audit findings have often been regarded as containing the elements of criteria, condition, and effect, plus cause when problems are found. However, the elements needed for a complete finding depend entirely on the objectives of the audit. Thus, a finding or set of findings is complete to the extent that the audit objectives are satisfied and the report clearly relates those objectives to the finding's elements.

Conclusions

20. The report should contain conclusions when called for by the audit objectives. Conclusions should be

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<sup>1</sup>Any audit findings not included in the audit report, e.g., because of insignificance, should be separately communicated to management, preferably in writing. The audit report should reference findings communicated in a management letter to top management. All communications should be documented in the working papers.

specified and not left to be inferred by readers. The report should not be written on the basis that a bare recital of facts makes the conclusions inescapable.

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Cause and  
Recommendations

21. **The report should include the cause of problem areas noted in the audit, and recommendations for actions to correct the problem areas and to improve operations, when called for by the audit objectives.**

Cause

22. The report should include a discussion of cause when problems are reported and the audit objectives call for development of the reasons for the problems. In some audits, the objective may be limited to identifying whether or not a problem exists with no requirement for identifying the cause, even if a problem is found.
23. Identifying the underlying cause of problems found is helpful in making constructive recommendations to achieve corrective action. When auditors know why something happened, they can more readily determine what action is needed to prevent its recurrence.
24. Because problems can result from a number of plausible factors, auditors need to clearly demonstrate and explain with applicable evidence and reasoning the link between the problem and the factor or factors they identified as the cause. In some cases, the auditors may need to describe how they isolated the stated cause or causes from other plausible factors. This is not a requirement for proof of a causal relationship, but a requirement for reasonable persuasive argument.

Recommendations

25. The report should contain recommendations when the potential for significant improvement in operations and performance is substantiated by the reported findings and recommendations are called

for by the audit objectives. Recommendations to effect compliance with laws and regulations and improve internal controls should also be made when significant instances of noncompliance are noted or significant weaknesses in controls are found. The auditor's report should also disclose the status of known uncorrected significant findings and recommendations from prior audits that affect the objectives and findings of the current audit.

26. Reports which contain constructive recommendations can encourage improvements in the conduct of government programs and activities. Recommendations are most constructive when they are directed at resolving the cause of identified problems, are action oriented and specific, and are addressed to parties that need to act. Recommendations also need to be feasible and cost-effective.

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Statement on  
Auditing  
Standards

27. **The report should include a statement that the audit was made in accordance with generally accepted government auditing standards and disclose when applicable standards were not followed.**
28. The statement of conformity refers to the applicable standards that the auditors should have followed during the audit. The statement need not be qualified when standards that were not applicable were not followed. When applicable standards were not followed, the auditors should modify the statement to disclose in the scope section of their report the required standard that was not followed, the reasons therefor, and the known effect not following the standard had on the results of the audit.

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Internal  
Controls

29. **The report should identify the significant internal controls that were assessed, the scope of the auditor's assessment work, and any significant weaknesses found during the audit.**

30. Reporting on internal controls will vary depending on the significance of any weaknesses found and the relationship of those weaknesses to the audit objectives.<sup>2</sup>
31. In audits where the sole objective is to audit the internal controls, weaknesses found of significance to warrant reporting would be considered deficiencies and be so identified in the audit report. The internal controls that were assessed would be identified for full presentation of the findings.
32. In audits having as their objective an assessment of performance, auditors in seeking the cause of deficient performance found, may identify weaknesses in internal controls of such significance to be a key source of the deficient performance. In reporting findings, the controls would be identified and the weaknesses would be described as the "cause."

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**Compliance  
With Laws and  
Regulations**

33. **The report should include all significant instances of noncompliance and abuse and all indications or instances of illegal acts that could result in criminal prosecution that were found during or in connection with the audit.**<sup>3</sup>

Noncompliance

34. The auditors' report should include all significant instances of noncompliance found during or in connection with the audit, even those not resulting in a legal liability of the entity. All instances of illegal acts that could result in the entity, or an official or employee of the entity, being subject to criminal prosecution should also be reported. (See paragraph 42, page 7-9).

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<sup>2</sup>See footnote 1, page 7-4, for reporting internal control weaknesses not meeting the test of significance

<sup>3</sup>See footnote 1, page 7-4 for reporting on instances of noncompliance not meeting the test of significance

Abuse and Illegal  
Acts

35. In reporting significant instances of noncompliance identified in response to the audit objectives, the auditors should place their findings in proper perspective. To give the reader a basis for judging the prevalence and consequences of noncompliance, the instances of noncompliance should be related to the universe or the number of cases examined and be quantified in terms of dollar value, if appropriate.
36. If, during an audit or in connection with an audit of a government entity, external government auditors become aware of abuse or illegal acts or indications of such acts that could affect the government entity, they should promptly report to the top official of that entity. The auditor should also consider reporting to the appropriate oversight body. If the top official is believed to be a party to such acts or otherwise implicated, the auditor should in all cases report to the appropriate oversight body. If the acts involve funds received from other government entities, the auditors should also promptly report to the proper officials, including the audit officials, of those entities.
37. Internal government auditors auditing an entity that is external to the entity to which they are assigned should promptly report to officials and authorities in accordance with the preceding paragraph.
38. Internal government auditors auditing within the government entity to which they are assigned, should report to the top officials of the entity under audit (unless the official is believed to be a party to such acts) and/or the appropriate entity investigative personnel.
39. Nongovernment audit organizations conducting government audits will discharge their responsibilities for reporting abuse or illegal acts or indications of such acts found during or in connection with an audit by promptly reporting to the top official of

the entity arranging for the audit. The auditor should also consider reporting to the appropriate oversight body. If the audited entity and the top official is believed to be a party to such acts or otherwise implicated, the auditors should in all cases report to the appropriate oversight body. Also, when the acts involve funds received from other government entities, the audited entity is expected to notify the proper officials, including the audit officials, of those entities. If the entity does not do so within a reasonable time or was unable to because the top official was involved, the auditor should report to the officials of those other government entities.

40. It is the responsibility of an entity receiving the information from the various organizations, both audited entity and funding entity, to report to appropriate law enforcement authorities and other government entities whose funds are involved.
41. In the case of an audit of government funds received by a nongovernment entity, the auditors should promptly report to the appropriate government entity requiring or arranging for the audit, and such other officials designated by law or regulation to receive the audit reports.
42. Abuse or illegal acts or indications of such acts that auditors become aware of should be covered in a written report and submitted in accordance with the preceding paragraphs. Such acts may be covered in a separate report if including them in the overall report would compromise investigative or legal proceedings or otherwise preclude the report from being released to the public. Auditors generally should not release information or reports containing information on potential illegal acts that could result in the entity, or officer or employee of the entity, being subjected to criminal prosecution, or reports with references that such acts were omitted from reports, without consulting with appropriate legal counsel, since this could interfere with



legal processes or subject the implicated individuals to undue publicity, or might subject the auditor to potential legal action.

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**Views of  
Responsible  
Officials**

- 43. The report should include the pertinent views of responsible officials of the organization, program, activity, or function audited concerning the auditors' findings, conclusions, and recommendations, and what corrective action is planned.**
44. One of the most effective ways to ensure that a report is fair, complete, and objective is to obtain advance review and comments by responsible auditee officials, and others as may be appropriate. Including the views of responsible officials produces a report that shows not only what was found and what the auditors think about it, but also what the responsible persons think about it and what they plan to do about it.
45. The auditor should normally request that the responsible officials' views be submitted in writing for significant findings, conclusions, and recommendations adversely affecting the audited entity. When, in these cases, written comments are not obtained, oral comments should be requested.
46. Advance comments should be objectively evaluated and recognized, as appropriate, in the report. A promise or plan for corrective action should be noted but should not be accepted as justification for dropping a significant point or a related recommendation.
47. When the comments oppose the report's findings, conclusions, or recommendations, and are not in the auditors' opinion valid, the auditors may choose to state their reasons for rejecting them. Conversely, the auditors should modify their report if they find the comments valid.

Noteworthy  
Accomplishments

48. **The report should include a description of any significant noteworthy accomplishments, particularly when management improvements in one area may be applicable elsewhere.**
49. Significant management accomplishments identified during the audit, which were within the scope of the audit necessary to accomplish the audit objectives, should be included in the audit report, along with deficiencies. Such information is necessary to fairly present the situation the auditors find and to provide appropriate balance to the report. In addition, inclusion of such accomplishments may lead to improved performance by other government organizations that read the report.

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Issues Needing  
Further Study

50. **The report should include a listing of any significant issues needing further study and consideration.**
51. If during the audit, the auditor identifies significant issues that warrant further audit work, but the issues are not directly related to the audit objectives and the auditor does not expand the audit and pursue them, the auditor should:
- a. refer the issues to the appropriate auditors within the audit organization responsible for planning future audit work, and
  - b. disclose the issues in the report and the reasons the issues need further study.

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Privileged and  
Confidential  
Information

52. **The report should include a statement about any pertinent information that was omitted because it is deemed privileged or confidential. The nature of such information should be described, and the basis under which it is withheld should be stated.**

53. Certain information may be prohibited from general disclosure by federal, state, or local laws or regulations. Such information may be provided on a need-to-know basis only to persons authorized by law or regulation to receive it. Before omitting pertinent data from the report, the auditors should obtain assurance that a valid requirement for the omission exists, and where appropriate, consult with legal counsel.
54. Auditors should generally consult with appropriate legal counsel before releasing reports with references that illegal acts or indications of such acts were omitted from reports.<sup>1</sup>

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Report  
Presentation

55. The fourth reporting standard for government performance audits is:

**The report should be complete, accurate, objective, and convincing, and be as clear and concise as the subject matter permits.**

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Complete

56. Being complete requires that the report contain all pertinent information needed to satisfy the audit objectives, promote an adequate and correct understanding of the matters reported, and meet the applicable report content requirements. It also means including appropriate background information.
57. Giving readers an adequate and correct understanding means providing perspective on the extent and significance of reported findings, such as the frequency of occurrence relative to the number of cases or transactions tested and the relationship of the findings to the entity's operations.
58. Except as necessary to make convincing presentations, detailed supporting data need not be included.

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<sup>1</sup>See paragraph 42 on page 7-9

In most cases, a single example of a deficiency is not sufficient to support a broad conclusion or a related recommendation. All that it supports is that there was a deviation, an error, or a weakness.

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**Accurate**

59. Accuracy requires that the evidence presented be true and that findings be correctly portrayed. The need for accuracy is based on the need to assure readers that what is reported is credible and reliable. One inaccuracy in a report can cast doubt on the validity of an entire report and can divert attention from the substance of the report. Also, inaccurate reports can damage the credibility of the issuing audit organization and reduce the effectiveness of reports it issues.
60. The report should include only information, findings, and conclusions that are supported by competent and relevant evidence in the auditor's working papers. That evidence should demonstrate the correctness and reasonableness of the matters reported. Correct portrayal means describing accurately the audit scope and methodology, and presenting findings and conclusions in a manner consistent with the scope of audit work.

**Objective**

61. Objectivity requires that the presentation throughout the report be balanced in content and tone. A report's credibility is significantly enhanced when it presents evidence in an unbiased manner so that readers are persuaded by the facts.
62. The audit report should be fair and not be misleading, and should place the audit results in proper perspective. This means presenting the audit results impartially and guarding against the tendency to exaggerate or overemphasize deficient performance. In describing shortcomings in performance, auditors should present the explanation of responsible officials including the consideration of any unusual difficulties or circumstances they faced.

63. The tone of reports should encourage favorable reaction to findings and recommendations. Titles, captions, and the text of reports should be stated constructively. Although findings should be presented in clear, forthright terms, the auditors should keep in mind that one of their objectives is to be persuasive, and that this can best be done by avoiding language that unnecessarily generates defensiveness and opposition. Although criticism of past performance is often necessary, the report should emphasize needed improvements.

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**Convincing**

64. Being convincing requires that the audit results be responsive to the audit objectives, and that the findings be presented in a manner that is persuasive and that conclusions and recommendations follow logically from the facts presented. The information presented should be sufficient to persuade the readers of the validity of the findings, the reasonableness of the conclusions, and the desirability of their accepting the recommendations. Reports designed in this manner can do much to focus the attention of responsible officials on the matters in reports that warrant attention and to stimulate corrective actions.

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**Clear**

65. Clarity requires that the report be easy to read and understand. Reports should be written in language as clear and simple as the subject matter permits.
66. Use of straightforward, nontechnical language is essential to simplicity of presentation. If technical terms and unfamiliar abbreviations and acronyms are used, they should be clearly defined. Acronyms should be used sparingly.
67. Both logical organization of material, and accuracy and precision in stating facts and in drawing conclusions, are essential to clarity and understanding. Effective use of titles and captions and thesis and topic sentences make the report easier to read and

understand. Visual aids (such as pictures, charts, graphs, and maps) should be used when appropriate to clarify and summarize complex material.

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Concise

68. Being concise requires that the report be no longer than necessary to convey the message. Too much detail detracts from a report, may even conceal the real message, and may confuse or discourage readers. Needless repetition should be avoided.
69. Although room exists for considerable judgment in determining the content of reports, those that are complete, but still concise, are likely to receive greater attention.

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Report  
Distribution

70. The fifth reporting standard for government performance audits is:

**Written audit reports are to be submitted by the audit organization to the appropriate officials of the organization audited, and to the appropriate officials of the organizations requiring or arranging for the audits, including external funding organizations, unless legal restrictions, ethical considerations, or other arrangements prevent it. Copies of the reports should also be sent to other officials who may be responsible for taking action on audit findings and recommendations and to others authorized to receive such reports. Unless restricted by law or regulation, copies should be made available for public inspection.**

71. Audit reports should be distributed to as many interested officials as is practicable. In some cases, the subject of the audit may involve material that is classified for security purposes or is not releasable to particular parties or the public for other valid reasons. Generally, however, the report should be distributed to officials directly interested in the results. Such officials include those designated by

law or regulation to receive such reports, those responsible for acting on the findings and recommendations, legislators, and those of other levels of government that have provided funds to the audited entity.

72. Internal auditors auditing within their entity should follow their entity's own arrangements and statutory requirements. Usually, they report to their entity's top management and the entity is responsible for distribution of the report.
73. When nongovernment audit organizations are engaged, the engaging government organization is responsible for distributing the reports and for making reports available to the public, as appropriate. If the nongovernment audit organization is to make the distribution, the engagement agreement should indicate what officials or organizations should receive the report.

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# Summary of Statement on Government Auditing Standards

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## **I. Introduction**

### **A. Purpose**

1. This statement contains standards for audits of government organizations, programs, activities, and functions, and of government funds received by contractors, nonprofit organizations, and other nongovernment organizations
2. The standards are to be followed by auditors and audit organizations when required by law, regulation, agreement or contract, or policy

## **II. Types of Government Audits**

### **A. Purpose**

1. This chapter describes the types of audits that government and nongovernment audit organizations conduct, and that government organizations arrange to have conducted. This description is not intended to limit or require the types of audits that may be conducted or arranged
2. In conducting these types of audits, auditors should follow the applicable standards included and incorporated in this statement

### **B. Financial Audits**

1. Financial statement audits determine (a) whether the financial statements of an audited entity present fairly the financial position, results of operations, and cash flows or changes in financial position in accordance with generally accepted accounting principles, and (b) whether the entity has complied with laws and regulations for those transactions and events that may have a material effect on the financial statements.
2. Financial related audits include determining (a) whether financial reports and related items, such as elements, accounts, or funds are fairly presented, (b) whether financial information is presented in accordance with established or stated criteria, and (c) whether the entity has adhered to specific financial compliance requirements

### **C. Performance Audits**

1. Economy and efficiency audits include determining (a) whether the entity is acquiring, protecting, and using its resources (such as personnel, property, and space) economically and efficiently, (b) the causes of inefficiencies or uneconomical practices, and (c) whether the entity has complied with laws and regulations concerning matters of economy and efficiency
2. Program audits include determining (a) the extent to which the desired results or benefits established by the legislature or other authorizing body are being achieved, (b) the effectiveness of organizations, programs, activities, or functions, and (c) whether the entity has complied with laws and regulations applicable to the program

(continued)



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**Appendix A  
Summary of Statement on  
Government  
Auditing Standards**

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**D. Understanding the Audit Objectives and Scope**

1. Audits may have a combination of financial and performance audit objectives, or may have objectives limited to only some aspects of one audit type.
2. Auditors should follow the appropriate standards in this statement that are applicable to the individual objectives of the audit.

**E. Other Activities of An Audit Organization**

1. Services other than audits: The head of the audit organization should establish policy on which audit standards from this statement should be followed by the auditors in performing such services. However, as a minimum, auditors should collectively possess adequate professional proficiency and exercise due professional care for the service being performed.
2. Investigative work: The head of the audit organization should establish policy on whether the audit standards in this statement, or some other appropriate standards, are to be followed by the employees performing this work.
3. Nonaudit activities: The head of the audit organization should establish policy on what standards in this statement are to be followed, or whether some other appropriate standards are to be followed, by the employees in performing this type of work.

**III. General Standards**

- A. Qualifications:** The staff assigned to conduct the audit should collectively possess adequate professional proficiency for the tasks required.
- B. Independence:** In all matters relating to the audit work, the audit organization and the individual auditors, whether government or public, should be free from personal and external impairments to independence, should be organizationally independent, and should maintain an independent attitude and appearance.
- C. Due Professional Care:** Due professional care should be used in conducting the audit and in preparing related reports.
- D. Quality Control:** Audit organizations conducting government audits should have an appropriate internal quality control system in place and participate in an external quality control review program.

**IV. Field Work Standards for Financial Audits**

**A. Relationship to AICPA Standards**

1. The standards of field work for government financial audits incorporate the AICPA standards of field work for financial audits, and prescribes supplemental standards of field work needed to satisfy the unique needs of government financial audits.
2. The field work standards of the AICPA and the supplemental standards in chapter 4 of this statement apply to both financial statement audits and financial related audits.

(continued)

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**Appendix A  
Summary of Statement on  
Government  
Auditing Standards**

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**B. Planning**

- 1 Supplemental planning field work standards for government financial audits are:
  - a. Audit Requirements for all Government Levels: Planning should include consideration of the audit requirements of all levels of government
  - b. Legal and Regulatory Requirements A test should be made of compliance with applicable laws and regulations.
    - (1) In determining compliance with laws and regulations:
      - (a) The auditor should design audit steps and procedures to provide reasonable assurance of detecting errors, irregularities, and illegal acts that could have a direct and material effect on the financial statement amounts or the results of financial related audits.
      - (b) The auditor should also be aware of the possibility of illegal acts which could have an indirect and material effect on the financial statements or results of financial related audits.

**C. Evidence (Working papers)**

1. The AICPA field work standards and this statement require that: A record of the auditors' work be retained in the form of working papers.
2. Supplemental working paper requirements for financial audits are that working papers should:
  - a. Contain a written audit program cross-referenced to the working papers.
  - b. Contain the objective, scope, methodology and results of the audit
  - c. Contain sufficient information so that supplementary oral explanations are not required.
  - d. Be legible with adequate indexing and cross-referencing, and include summaries and lead schedules, as appropriate.
  - e. Restrict information included to matters that are materially important and relevant to the objectives of the audit.
  - f. Contain evidence of supervisory reviews of the work conducted

**D. Internal Control**

1. The AICPA field work standards and this statement require that. A sufficient understanding of the internal control structure is to be obtained to plan the audit and to determine the nature, timing, and extent of tests to be performed.

(continued)

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**Appendix A  
Summary of Statement on  
Government  
Auditing Standards**

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**V. Reporting Standards for Financial Audits**

**A. Relationship to AICPA Standards**

1. The standards of reporting for government financial audits incorporate the AICPA standards of reporting for financial audits, and prescribes supplemental standards of reporting needed to satisfy the unique needs of government financial audits
2. The reporting standards of the AICPA and the supplemental standards in chapter 5 of this statement apply to both financial statement audits and financial related audits

**B. Supplemental reporting standards for government financial audits are:**

1. **Statement on Auditing Standards:** A statement should be included in the auditors' report that the audit was made in accordance with generally accepted government auditing standards. (AICPA standards require that public accountants state that the audit was made in accordance with generally accepted auditing standards. In conducting government audits, public accountants should also state that their audit was conducted in accordance with the standards set forth in chapters 3, 4, and 5.)
2. **Report on Compliance:** The auditors should prepare a written report on their tests of compliance with applicable laws and regulations. This report, which may be included in either the report on the financial audit or a separate report, should contain a statement of positive assurance on those items which were tested for compliance and negative assurance on those items not tested. It should include all material instances of noncompliance, and all instances or indications of illegal acts which could result in criminal prosecution
3. **Report on Internal Controls:** The auditors should prepare a written report on their understanding of the entity's internal control structure and the assessment of control risk made as part of a financial statement audit, or a financial related audit. This report may be included in either the auditor's report on the financial audit or a separate report. The auditor's report should include as a minimum (a) the scope of the auditor's work in obtaining an understanding of the internal control structure and in assessing the control risk, (b) the entity's significant internal controls or control structure including the controls established to ensure compliance with laws and regulations that have a material impact on the financial statements and the results of the financial related audit, and (c) the reportable conditions, including the identification of material weaknesses, identified as a result of the auditors work in understanding and assessing the control risk
4. **Reporting on Financial Related Audits:** Written audit reports are to be prepared giving the results of each financial related audit.
5. **Privileged and Confidential Information:** If certain information is prohibited from general disclosure, the report should state the nature of the information omitted and the requirement that makes the omission necessary

(continued)

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**Appendix A  
Summary of Statement on  
Government  
Auditing Standards**

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6 Report Distribution: Written audit reports are to be submitted by the audit organization to the appropriate officials of the organization audited and to the appropriate officials of the organizations requiring or arranging for the audits, including external funding organizations, unless legal restrictions, ethical considerations, or other arrangements prevent it. Copies of the reports should also be sent to other officials who have legal oversight authority or who may be responsible for taking action and to others authorized to receive such reports. Unless restricted by law or regulation, copies should be made available for public inspection.

**VI. Field Work Standards for Performance Audits**

**A. Planning.** Work is to be adequately planned.

**B. Supervision.** Staff are to be properly supervised.

**C. Legal and Regulatory Requirements.** An assessment is to be made of compliance with applicable requirements of laws and regulations when necessary to satisfy the audit objectives.

1. Where an assessment of compliance with laws and regulations is required, auditors should design the audit to provide reasonable assurance of detecting abuse or illegal acts that could significantly affect the audit objectives.

2. In all performance audits, auditors should be alert to situations or transactions that could be indicative of abuse or illegal acts.

**D. Internal Control.** An assessment should be made of applicable internal controls when necessary to satisfy the audit objectives.

**E. Evidence.** Sufficient, competent, and relevant evidence is to be obtained to afford a reasonable basis for the auditors' judgments and conclusions regarding the organization, program, activity, or function under audit. A record of the auditors' work is to be retained in the form of working papers. Working papers may include tapes, films, and discs.

**VII. Reporting Standards for Performance Audits**

**A. Form.** Written audit reports are to be prepared communicating the results of each government audit.

**B. Timeliness.** Reports are to be issued promptly so as to make the information available for timely use by management and legislative officials, and by other interested parties.

**C. Report Contents**

1. Objectives, Scope, and Methodology: The report should include a statement of the audit objectives and a description of the audit scope and methodology.

2. Audit Findings and Conclusions: The report should include a full discussion of the audit findings, and where applicable, the auditor's conclusions.

(continued)

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**Appendix A  
Summary of Statement on  
Government  
Auditing Standards**

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3. Cause and Recommendations: The report should include the cause of problem areas noted in the audit, and recommendations for actions to correct the problem areas and to improve operations, when called for by the audit objectives.
4. Statement on Auditing Standards: The report should include a statement that the audit was made in accordance with generally accepted government auditing standards and disclose when applicable standards were not followed.
5. Internal Controls: The report should identify the significant internal controls that were assessed, the scope of the auditor's assessment work, and any significant weaknesses found during the audit.
6. Compliance With Laws and Regulations: The report should include all significant instances of noncompliance and abuse and all indications or instances of illegal acts that could result in criminal prosecution that were found during or in connection with the audit.
7. Views of Responsible Officials: The report should include the pertinent views of responsible officials of the organization, program, activity, or function audited concerning the auditors' findings, conclusions, and recommendations, and what corrective action is planned.
8. Noteworthy Accomplishments: The report should include a description of any significant noteworthy accomplishments, particularly when management improvements in one area may be applicable elsewhere.
9. Issues Needing Further Study: The report should include a listing of any significant issues needing further study and consideration.
10. Privileged and Confidential Information: The report should include a statement about any pertinent information that was omitted because it is deemed privileged or confidential. The nature of such information should be described, and the basis under which it is withheld should be stated.

**D. Report Presentation:** The report should be complete, accurate, objective, and convincing, and be as clear and concise as the subject matter permits.

**E. Report Distribution:** Written audit reports are to be submitted by the audit organization to the appropriate officials of the organization audited, and to the appropriate officials of the organizations requiring or arranging for the audits, including external funding organizations, unless legal restrictions, ethical considerations, or other arrangements prevent it. Copies of the reports should also be sent to other officials who may be responsible for taking action on audit findings and recommendations and to others authorized to receive such reports. Unless restricted by law or regulation, copies should be made available for public inspection.

### **VIII. AICPA Generally Accepted Auditing Standards**

#### **A. General Standards**

1. The examination is to be performed by a person or persons having adequate technical training and proficiency as an auditor.

(continued)

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**Appendix A  
Summary of Statement on  
Government  
Auditing Standards**

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2. In all matters relating to the assignment, an independence in mental attitude is to be maintained by the auditor or auditors.

3. Due professional care is to be exercised in the performance of the examination and the preparation of the report.

**B. Standards of Field Work**

1. The work is to be adequately planned and assistants, if any, are to be properly supervised.

2. A sufficient understanding of the internal control structure is to be obtained to plan the audit and to determine the nature, timing, and extent of tests to be performed.

3. Sufficient competent evidential matter is to be obtained through inspection, observation, inquiries, and confirmations to afford a reasonable basis for an opinion regarding the financial statements under examination

**C. Standards of Reporting**

1. The report shall state whether the financial statements are presented in accordance with generally accepted accounting principles

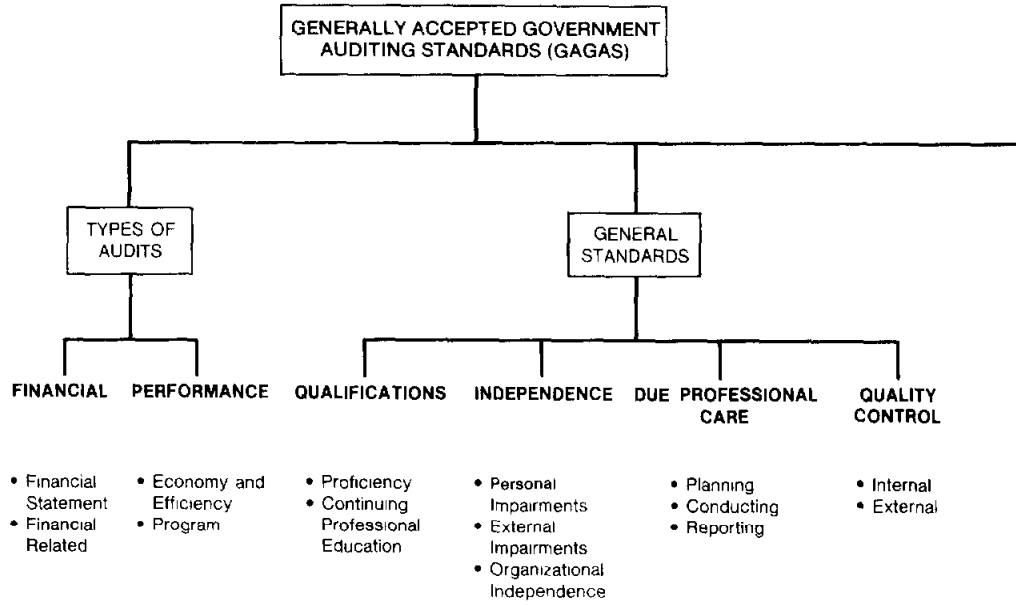
2. The report shall identify those circumstances in which such principles have not been consistently observed in the current period in relation to the preceding period.

3. Informative disclosures in the financial statements are to be regarded as reasonably adequate unless otherwise stated in the report

4. The report shall either contain an expression of opinion regarding the financial statements, taken as a whole, or an assertion to the effect that an opinion cannot be expressed. When an overall opinion cannot be expressed, the reasons therefor should be stated. In all cases where an auditor's name is associated with financial statements, the report should contain a clear-cut indication of the character of the auditor's examination, if any, and the degree of responsibility he is taking

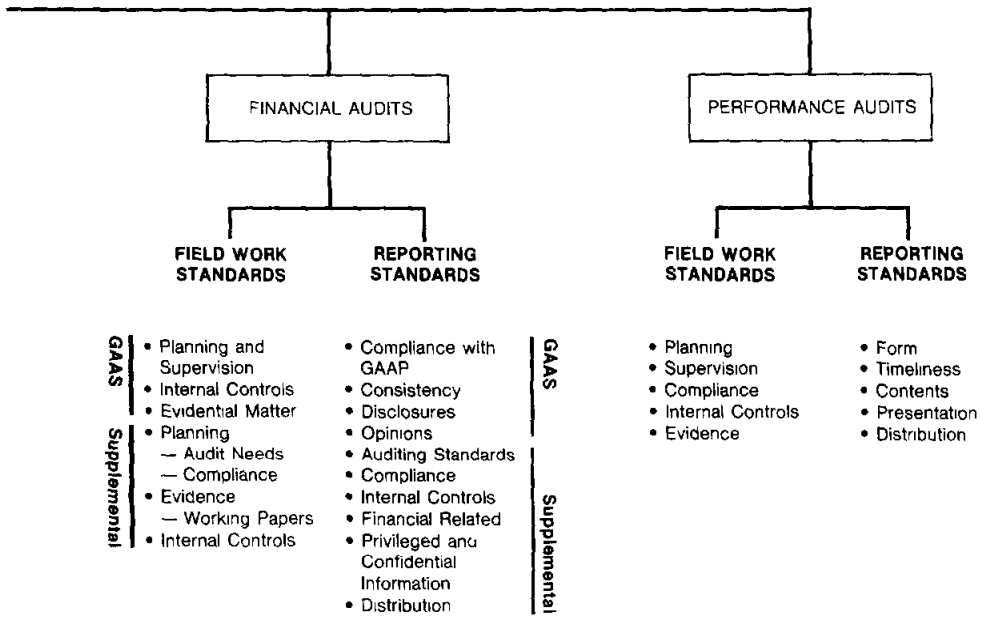
# Overview of Standards

**GENERALLY ACCEPTED GOVERNMENT AUDITING STANDARDS (GAGAS)**



**Appendix B  
Overview of Standards**

**GENERALLY ACCEPTED GOVERNMENT AUDITING STANDARDS (GAGAS) (Continued)**





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# Auditing Standards Advisory Council

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James F. Antonio  
Chairman, Governmental  
Accounting Standards Board

Robert W. Bramlett  
Project Manager, Governmental  
Accounting Standards Board

Thomas Cook  
Professor of Psychology  
Northwestern University

James H. Curry  
Assistant Inspector General  
U.S. Department of Defense

Bert T. Edwards  
Partner, Arthur Andersen & Co

Bernard P. Geizer  
First Deputy Inspector General  
Metropolitan Transportation  
Authority, New York

Frank L. Greathouse  
Director, Division of State  
Audit, Tennessee

Thomas W. Hayes  
Auditor General  
California

Edward P. Henderson  
Partner, Fleming, Reiss, Little & Co.

William R. Kinney, Jr.  
Professor of Accounting  
University of Texas

Roland M. Malan  
Assistant Deputy  
Comptroller, State of New York

John R. Miller  
Partner, Peat Marwick Main & Co.

Douglas R. Norton  
Auditor General  
Arizona

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**Appendix C**  
**Auditing Standards**  
**Advisory Council**

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Edward Renfrow  
State Auditor  
North Carolina

Lee Sechrest  
Professor of Psychology  
University of Arizona

James B. Thomas, Jr.  
Inspector General  
U.S. Department of Education

Cornelius E. Tierney  
Partner, Arthur Young & Co

Richard A. White  
Former Manager of Standards  
Institute of Internal Auditors

**GAO Project Team**

William J. Anderson, Jr.

W. A. Broadus, Jr.

Donald R. Polashuk

Ronell B. Raaum

Frederick D. Wolf

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# Glossary

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<b>Abuse</b>	Furnishing excessive services to beneficiaries; or performing what may be considered improper practices, none of which involves noncompliance with laws and regulations.
<b>Audit</b>	Refers to the type of work described in chapter 2 of this statement.
<b>Audit Methodology</b>	The methods and techniques used to gather and analyze data needed to accomplish the audit objectives.
<b>Audit Objective(s)</b>	A statement of the purpose of the audit; the question(s) the audit will answer. (Note: The AICPA refers to audit objectives as the objectives developed to achieve the financial statement assertions.)
<b>Audit Program</b>	A document listing the suggested steps and procedures to be followed in conducting the audit and preparing the report.
<b>Audit Results</b>	Include the audit findings, and as appropriate, conclusions and recommendations.
<b>Audit Scope Impairments</b>	Factors external to the audit organization which can restrict the auditors' ability to render objective opinions and conclusions.
<b>Audit Standards</b>	Pertain to the auditor's professional qualifications, the quality of audit effort, and the characteristics of professional and meaningful audit reports.
<b>Auditor</b>	The term as used in this statement refers to the auditor as well as the audit organization unless otherwise indicated in this statement.

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**Glossary**

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<b>Auditor's Opinion</b>	An expression in the audit report of the auditor's position on whether the financial information of the entity is presented fairly, in all material respects, in conformity with generally accepted accounting principles (or with other specified accounting principles applicable to the auditee).
<b>Body of Technical Knowledge</b>	Existing sources of information on types of audits, tests, procedures, and methodology. Such information is available through such organizations as the American Evaluation Association, American Institute of Certified Public Accountants, Canadian Comprehensive Auditing Foundation, Institute of Internal Auditors, Intergovernmental Audit Forums, and U.S. General Accounting Office.
<b>Competence</b>	Refers to evidence that is valid and reliable.
<b>Compliance With Laws and Regulations</b>	The term, as used in this statement, refers to following requirements or not violating prohibitions contained in statutes, regulations, contracts, and grants and in binding policies and procedures governing entity conduct.
<b>Computer-Based System</b>	That part of an overall information system which uses automated equipment and associated methods and procedures to process the data and information.
<b>Computer-Processed Data</b>	Data that are collected, processed, and stored, and subsequently compiled and produced as data or information, through use of a computer.
<b>Conclusions</b>	An expression in the audit report of the auditor's position on the audit objective(s).

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**Glossary**

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<b>Contract Audit</b>	An audit of a government contract for goods and services with profit as well as nonprofit organizations.
<b>Due Professional Care</b>	<p>The third general standard for government auditing. Conducting audits and preparing reports in accordance with generally accepted government auditing standards including:</p> <ul style="list-style-type: none"><li>• Competently and adequately carrying out the audit steps and procedures which are necessary in order to achieve the audit objectives.</li><li>• Possessing skill and knowledge appropriate for the audit.</li><li>• Using sound judgment in establishing the scope, selecting the methodology, and choosing tests and procedures for the audit, and in evaluating and reporting on the audit results.</li><li>• Exercising integrity and objectivity in conducting the audit and preparing the report.</li><li>• Follow-up on known findings and recommendations from previous audits to determine whether prompt and appropriate corrective actions have been taken by entity officials.</li></ul>
<b>Evidence</b>	The data and information an auditor obtains during audit field work to document findings and support opinions and conclusions.
<b>External Impairments</b>	These are factors external to the audit organization that may restrict the audit or interfere with an auditor's ability to form independent and objective opinions and conclusions.
<b>External Quality Control Review Program</b>	A review of an audit organization by an organization not affiliated with the audit organization being reviewed to determine that: (1) the organization's internal quality control system is in place and operating effectively and (2) established policies and

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procedures and applicable auditing standards are being followed in its audit work, including its government audits.

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**Financial Audits**

1. Financial statement audits determine (a) whether the financial statements of an audited entity present fairly the financial position, results of operations, and cash flows or changes in financial position in accordance with generally accepted accounting principles, and (b) whether the entity has complied with laws and regulations for those transactions and events that may have a material effect on the financial statements.

2. Financial related audits include determining (a) whether financial reports and related items, such as elements, accounts, or funds are fairly presented, (b) whether financial information is presented in accordance with established or stated criteria, and (c) whether the entity has adhered to specific financial compliance requirements.

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**Financial Statements**

A presentation of financial data and information, including accompanying notes, derived from accounting records to communicate at a point in time an entity's financial position, and for a period of time its results of operations and cash flows or changes in financial position.

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**Findings**

The result of information development—a logical pulling together of information to arrive at conclusions (or a response to an audit objective on the basis of the sum of the information) about an organization, program, activity, function, condition, or other matter which was analyzed or evaluated. It need not be critical or be concerned only with deficiencies or weaknesses. A finding will be the basis for conclusions and recommendations for corrective action.

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Glossary

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**Generally Accepted Accounting Principles (GAAP)**

Rules and procedures established by authoritative bodies or conventions that have evolved through custom and common usage.

The Governmental Accounting Standards Board (GASB) establishes accounting principles and financial reporting standards for state and local government entities.

The Financial Accounting Standards Board (FASB) establishes accounting principles for nongovernment entities.

The General Accounting Office (GAO) establishes accounting principles and financial reporting standards for the federal government.

Some state and local governments and regulatory bodies also have established specific accounting principles.

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**Generally Accepted Auditing Standards (GAAS)**

Those audit standards set forth in the AICPA's *Statements on Auditing Standards*.

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**Generally Accepted Government Auditing Standards (GAGAS)**

Those audit standards set forth in the Government Auditing Standards (Standards for Audit of Governmental Organizations, Programs, Activities, and Functions) issued by the Comptroller General of the United States.

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**General Standards**

A term pertaining to (1) the qualifications of the staff, (2) the audit organization's and the individual auditor's independence, (3) the exercise of due professional care in conducting the audit and in preparing related reports, and (4) the presence of quality controls.

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**Glossary**

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**Government Activity**      A specific and distinguishable line of work conducted within an organizational component of a government entity.

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**Government Entity**      Generally means a:

- State agency (e.g., department, office, commission, committee, division, bureau, or section within state government.)
- Municipality (i.e., a city or town with its own incorporated government for local affairs).
- County, independent school district, special district, or authority.
- Local agency (e.g., department, office, commission, committee, division, bureau, or section within local government).
- Nonprofit government agency.
- Government regional planning agency, commission, authority, or corporation.
- Federal department and agency.

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**Government Function**      The purpose for which a government organization is responsible.

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**Government Organization**      A government entity or component of a government entity.

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**Government Program**      Generally defined as an organized set of activities directed toward a common goal. In practice, however, the term program has many uses and thus does not have a well-defined meaning.

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**Illegal Acts**      A type of noncompliance in which the source of the requirement not followed or prohibition violated is a statute or implementing regulation.

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**Independence**

The second general standard for government auditing. In all matters relating to the audit work, the audit organization and the individual auditors, whether government or public, should be free from personal and external impairments to independence, should be organizationally independent, and should maintain an independent attitude and appearance.

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**Internal Control**

Internal control is defined as follows:

1. According to the AICPA, SAS on Consideration of the Internal Control Structure in a Financial Statement Audit. This applies to the field work and reporting standards for financial audits contained in chapters 4 and 5 of this statement.

An entity's internal control structure consists of the policies and procedures established to provide reasonable assurance that specific entity objectives will be achieved. An entity's internal control structure consists of three elements:

- **Control Environment:** The collective effect of various factors on establishing, enhancing, or mitigating the effectiveness of specific policies and procedures.
- **Accounting System:** The methods and records established to identify, assemble, analyze, classify, record, and report an entity's transactions and to maintain accountability for the related assets and liabilities.
- **Control Procedures:** The policies and procedures in addition to the control environment and accounting system that management has established to provide reasonable assurance that specific entity objectives will be achieved.

2. According to the GAO's Standards for Internal Controls in the Federal Government: This applies to the field work and reporting standards for performance audits contained in chapters 6 and 7 of this statement.

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**Glossary**

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“The plan of organization and methods and procedures adopted by management to ensure that resource use is consistent with laws, regulations, and policies; that resources are safeguarded against waste, loss, and misuse; and that reliable data are obtained, maintained, and fairly disclosed in reports.”

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**Internal Quality Control System**

Operating policies and procedures established by the audit organization to provide reasonable assurance that it: (1) has established, and is following, adequate audit policies and procedures and (2) has adopted, and is following, applicable auditing standards.

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**Materiality and/or Significance**

The weight that evidence plays in influencing the auditor’s decision concerning: the selection of issues and areas for audit; the nature, timing, and extent of audit tests and procedures (methodology); and the auditor’s audit opinion, judgment, or conclusion.

- **Materiality:** The magnitude of an omission or misstatement of accounting information that, in the light of surrounding circumstances, makes it probable that the judgment of a reasonable person relying on the information would have been changed or influenced by the omission or misstatement. Materiality judgments are made in light of surrounding circumstances and necessarily involve both quantitative and qualitative considerations.
  - **Significance:** The importance, in relation to the audit objectives, of an item, event, information, or matter, or of a problem the auditor identifies.
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**Noncompliance With Laws and Regulations**

A failure to follow requirements, or a violation of prohibitions, contained in statutes, regulations, contracts, grants, and binding policies and procedures governing entity conduct.

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<b>Organizational Independence</b>	This concerns the auditor's being sufficiently removed from pressures within the organizational structure of a government to express impartial opinions and conclusions.
<b>Performance Audits</b>	<p>1. Economy and efficiency audits include determining (a) whether the entity is acquiring, protecting, and using its resources (such as personnel, property, and space) economically and efficiently, (b) the causes of inefficiencies or uneconomical practices, and (c) whether the entity has complied with laws and regulations concerning matters of economy and efficiency.</p> <p>2. Program audits include determining (a) the extent to which the desired results or benefits established by the legislature or other authorizing body are being achieved, (b) the effectiveness of organizations, programs, activities, or functions, and (c) whether the entity is complying with requirements of laws and regulations applicable to the program.</p>
<b>Personal Impairments</b>	They involve circumstances in which auditors may not be impartial, or may not be perceived to be impartial.
<b>Planning</b>	The first field work standard for government auditing. This standard requires that the work is to be adequately planned. Adequate planning includes consideration of: audit objectives, scope, and methodology; criteria for assessing performance (where applicable); coordination with other government auditors; skill and knowledge of the staff to be used, and the use of consultants, experts, and specialists; compliance with laws and regulations and potential abuse and illegal acts; assessment of internal controls; and materiality and/or significance and audit risk.

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**Glossary**

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<b>Program Effectiveness Evaluation</b>	The application of systematic methods to estimate the extent to which observed results, intended or unintended, are caused by program activities. Cause is linked to effect through use of design and analysis methods which compare results observed after implementation to estimates of results which would have been observed in the absence of the program.
<b>Program Evaluation</b>	The application of systematic methods to the assessment of program conceptualization, implementation, and effectiveness.
<b>Qualifications</b>	The first general standard for government auditing. The staff assigned should collectively possess (1) a knowledge of the methods and techniques applicable to government auditing and be able to apply it, (2) a knowledge of government organizations, programs, activities, and functions, (3) the skills to communicate clearly and effectively, and (4) the knowledge and the skills necessary for the audit.
<b>Qualifications of Public Accountants</b>	When public accountants are engaged to conduct financial audits that lead to an expression of an opinion, public accountants should be: (1) licensed certified public accountants or persons working for a licensed certified public accounting firm or (2) public accountants licensed on or before December 31, 1970, or persons working for a public accounting firm licensed on or before December 31, 1970.
<b>Quality Control</b>	The fourth general standard for government auditing. Audit organizations conducting government audits should have an appropriate internal quality control system in place and participate in an external quality control review program.

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**Glossary**

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<b>Recommendations</b>	Actions the auditor believes are needed to correct problem areas and to improve operations.
<b>Relevance</b>	Refers to the relationship of evidence to its use.
<b>Report (Audit)</b>	<ol style="list-style-type: none"><li>1. The auditor's report in a financial audit through which an auditor expresses a conclusion or opinion or, if circumstances require, disclaims an opinion.</li><li>2. The auditor's report in a performance audit through which an auditor communicates the audit results.</li><li>3. Other special auditor's reports through which an auditor communicates information required by the audit engagement include "Report on Compliance," "Report on Internal Control," and so forth.</li></ol>
<b>Scope</b>	Refers to the depth and coverage of audit work. It concerns such questions as: Is the whole program or a part going to be audited? What period of time is to be covered? Is the audit regional or confined to particular localities? How precise must measures of performance be? What level of validity is needed in documenting the existence of a problem? What finding and reporting elements are to be developed?
<b>Should</b>	When the term "should" is used to describe the auditor's and/or audit organization's responsibility, this means that the standards that are applicable to the work and necessary to satisfy the audit objectives are to be followed. Departures from applicable standards must be disclosed in the audit report.
<b>Significance</b>	See materiality

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**Glossary**

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<b>Sufficiency</b>	The presence of enough factual and convincing evidence to support the auditors findings, conclusions, and any recommendations.
<b>Supervision</b>	This standard for government auditing requires that staff be properly supervised. Supervisors should ensure that less skilled staff members receive training and guidance in doing their work and that all staff clearly understand their tasks and what the work is expected to accomplish.
<b>Survey</b>	A process for quickly gathering information, without detailed verification, on the entity's organization, programs, activities, and functions. It is an effective method to help identify specific audit areas and to obtain information for use in planning.
<b>Timeliness</b>	This standard for government auditing states that reports are to be issued promptly so as to make the information available for timely use by management and legislative officials, and by other interested parties.
<b>Value-For-Money Audits</b>	Audits which assess whether government entities are managed with regard for economy and efficiency, and for effectiveness measurement, and in compliance with applicable laws, regulations, and directives.
<b>Working Papers</b>	Documents containing the evidence to support the auditor's findings, opinions, conclusions, and judgments. They include the collection of evidence, prepared or obtained by the auditor during the audit.

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