July 2004

Dear Colleague:

The U.S. Government Accountability Office (GAO) and the President's Council on Integrity and Efficiency (PCIE) maintain the GAO/PCIE *Financial Audit Manual* (FAM). The FAM provides guidance for performing financial statement audits of federal entities. The FAM is a key tool for enhancing accountability over taxpayer-provided resources.

GAO and the PCIE are committed to keeping the FAM current. With this goal in mind, a GAO/PCIE task force prepared the attached update of the FAM, primarily to incorporate the provisions of Statement on Auditing Standards 99, *Consideration of Fraud in a Financial Statement Audit*. The updated sections are highlighted in the table of contents. This update was issued as an exposure draft on the internet in April 2004 and includes changes based on comments received. The FAM, as amended for this and other updates, is available on the internet at either the GAO web site (www.gao.gov) or the PCIE web site (www.ignet.gov/pande/audit1.html#guide).

If you have comments or suggestions for future FAM updates, please send an email to FAM_Comments@oig.doi.gov.

We thank the individuals and organizations that provided comments and insights to enhance the FAM. The task force assembled by GAO and the PCIE also deserves much credit for its dedication to completing this project.

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The Honorable Everett L. Mosley
Chair
President's Council on Integrity
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Attachment

United States Government Accountability Office
President's Council on Integrity and Efficiency

GAO/PCIE

Financial Audit Manual

Update

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225 - PERFORM PRELIMINARY ANALYTICAL PROCEDURES

.01 During the planning phase, preliminary analytical procedures are performed to help the auditor

- understand the entity's business, including current-year transactions and events;
- identify account balances, transactions, ratios, or trends that may signal inherent or control risks, including any risks related to fraud (see section 260);
- identify and understand the significant accounting policies;
- determine planning, design, and test materiality (see section 230); and
- determine the nature, timing, and extent of audit procedures to be performed.

.02 GAAS requires the auditor to perform preliminary analytical procedures (AU 329). The resources spent in performing these procedures should be commensurate with the expected reliability of comparative information. For example, in a first-year audit, comparative information might be unreliable; therefore, preliminary analytical procedures generally should be limited.

.03 The auditor generally should perform the following steps to achieve the objectives of preliminary analytical procedures:

a. **Compare current-year amounts with relevant comparative financial information:** The financial data used in preliminary analytical procedures generally are summarized at a high level, such as the level of financial statements. If financial statements are not available, the budget or financial summaries that show the entity's financial position and results of operations may be used.

The auditor compares current-year amounts with relevant comparative financial information. Use of unaudited comparative data might not allow the auditor to identify significant fluctuations, particularly if an item consistently has been treated incorrectly. Also, the auditor may identify fluctuations that are not really fluctuations due to errors in the unaudited comparative data.

A key to effective preliminary analytical procedures is to use information that is comparable in terms of the time period presented and the presentation (i.e., same level of detail and consistent grouping of detail accounts into summarized amounts used for comparison).

The auditor may perform ratio analysis on current-year data and compare the current year's ratios with those derived from prior periods or budgets. The

auditor does this to study the relationships among components of the financial statements and to increase knowledge of the entity's activities. The auditor uses ratios that are relevant indicators or measures for the entity. Also, the auditor should consider any trends in the performance indicators prepared by the entity.

b. **Identify significant fluctuations:** Fluctuations are differences between the recorded amounts and the amounts expected by the auditor, based on comparative financial information and the auditor's knowledge of the entity. Fluctuations refer to both unexpected differences between current-year amounts and comparative financial information as well as the absence of expected differences. The identification of fluctuations is a matter of the auditor's judgment.

   The auditor establishes parameters for identifying significant fluctuations. When setting these parameters, the auditor generally considers the amount of the fluctuation in terms of absolute size and/or the percentage difference. The amount and percentage used are left to the auditor's judgment. An example of a parameter is "All fluctuations in excess of $10 million and/or 15 percent of the prior-year balance or other unusual fluctuations will be considered significant."

c. **Inquire about significant fluctuations:** The auditor discusses the identified fluctuations with appropriate entity personnel. The focus of the discussion is to achieve the purposes of the procedures described in paragraph 225.01. For preliminary analytical procedures, the auditor does not need to corroborate the explanations since they will be tested later. However, the explanations should appear reasonable and consistent to the auditor. The inability of entity personnel to explain the cause of a fluctuation may indicate the existence of control, fraud, and/or inherent risks.

.04 In performing preliminary analytical procedures, the auditor develops expectations about plausible relationships that are expected to exist. Because these procedures generally use data aggregated at a high level, their results typically provide only a broad initial indication about a potential misstatement. The auditor should consider any unusual relationships, together with other information gathered, in identifying the risk of material misstatement due to fraud (see section 260).

260 – IDENTIFY RISK FACTORS

.01 The auditor's consideration of inherent risk, fraud risk, control environment, risk assessment, communication, and monitoring (parts of internal control) affects the nature, timing, and extent of substantive and control tests. This section describes (1) the impact of risk factors identified during this consideration on substantive and control tests, (2) the process for identifying these risk factors, and (3) the auditor's consideration of the entity's process for reporting under FMFIA (both for internal control (section 2 of FMFIA) and for financial management systems' conformance with system requirements (section 4 of FMFIA) and for formulating the budget.

IMPACT ON SUBSTANTIVE TESTING

.02 AU 312 provides guidance on the consideration of audit risk and defines "audit risk" as the risk that the auditor may unknowingly fail to appropriately modify an opinion on financial statements that are materially misstated. Audit risk can be thought of in terms of the following three component risks:

- **Inherent risk** is the susceptibility of an assertion to a material misstatement, assuming that there are no related internal controls.

- **Control risk** is the risk that a material misstatement that could occur in an assertion will not be prevented or detected and corrected on a timely basis by the entity's internal control. Internal control consists of five components: (1) the control environment, (2) risk assessment, (3) monitoring, (4) information and communication, and (5) control activities (defined in paragraph 260.08 below). This section will discuss the first three of the components and communication, which is part of the fourth component. Section 300 (Internal Control Phase) will discuss the information systems and control activities.

- **Detection risk** is the risk that the auditor will not detect a material misstatement that exists in an assertion.

AU 316 requires the auditor to consider fraud risk, which is a part of audit risk, making up a portion of inherent and control risk. Fraud risk consists of the risk of fraudulent financial reporting and the risk of misappropriation of assets that cause a material misstatement of the

[Pages 260-2 to 260-8 remain unchanged. Revised pages follow.]

generated may be too voluminous to allow effective manual review. For example, one posting to the general ledger may result from the computer summarization of information from hundreds of locations.

e. **Nature of the hardware and software used in IS:** The nature of the hardware and software can affect inherent risk, as illustrated below:

- The type of computer processing (on-line, batch-oriented, or distributed) presents different levels of inherent risk. For example, the inherent risk of unauthorized transactions and data entry errors may be greater for on-line processing than for batch-oriented processing.

- Peripheral access devices or system interfaces can increase inherent risk. For example, Internet and dial-up access to a system increases the system's accessibility to additional persons and therefore increases the risk of unauthorized access to computer resources.

- Distributed networks enable multiple computer processing units to communicate with each other, increasing the risk of unauthorized access to computer resources and possible data alteration. On the other hand, distributed networks may decrease the risk of conflicting computerized data between multiple processing units.

- Applications software developed in-house may have higher inherent risk than vendor-supplied software that has been thoroughly tested and is in general commercial use.

f. **Unusual or nonroutine transactions:** As with manual systems, unusual or nonroutine transactions increase inherent risk. Programs developed to process such transactions may not be subject to the same procedures as programs developed to process routine transactions. For example, the entity may use a utility program to extract specified information in support of a nonroutine management decision.

FRAUD RISKS

.18 The auditor has a responsibility to plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether caused by error or fraud. Accordingly, the auditor is concerned with the **risk of material misstatement due to fraud (fraud risk)**. The primary factor that distinguishes fraud from error is that the action causing the misstatement in fraud is intentional. (See section 230 related to materiality, including quantitative and qualitative considerations.)

.19 Two types of misstatements are relevant to the auditor's consideration of fraud in an audit of financial statements—misstatements arising from fraudulent financial reporting and misstatements arising from misappropriation of assets. **Misstatements arising from fraudulent financial reporting** are intentional misstatements or omissions of amounts or disclosures in financial statements to deceive financial statement users. They could involve intentional alteration of accounting records, misrepresentation of transactions, intentional misapplication of accounting principles, or other means. **Misstatements arising from misappropriation of assets** involve theft of an entity's assets that result in misstatements in the financial statements. They could involve theft of property, embezzlement of receipts, fraudulent payments, or other means. (See section 310 for internal control over safeguarding assets. Safeguarding controls relate to protecting assets against loss from unauthorized acquisition, use, or disposition.)

.20 In considering misstatements arising from misappropriation of assets, the auditor should consider fraud risks associated with improper payments. Some of the improper payments made by federal government entities could involve fraud. The Improper Payments Information Act of 2002 (P.L. 107-300) defines improper payments as any payment that should not have been made or that was made in an incorrect amount (including overpayments and underpayments) under statutory, contractual, administrative, or other legally applicable requirements. The act requires agency heads to annually review all programs and activities that they administer, identify those that might be susceptible to significant improper payments,[1] estimate annual improper payments for those identified programs, and—for programs for which estimated improper payments exceed $10 million—report certain information to the Congress. Although the act has this reporting threshold, the auditor might consider improper payments amounting to $10 million or less quantitatively or qualitatively material.

.21 As discussed in paragraph .18, the auditor is responsible for obtaining reasonable, but not absolute, assurance about whether the financial statements are free of material misstatement. Absolute assurance cannot be attained, and the auditor's report does not provide absolute assurance. A properly planned and performed audit might not detect a material misstatement, and the subsequent discovery of a material misstatement does not, in and of itself, provide evidence that the auditor did not conform with auditing standards.

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[1] Agencies first need to determine which programs and activities are susceptible (at high risk) to improper payments. In determining this, OMB has issued guidance defining significant improper payments as those that exceed both 2.5 percent of program payments and $10 million. See OMB Memorandum M-03-13, *Improper Payments Information Act of 2002*, *Public Law 107-300* (May 21, 2003).

.22 In addition, the auditor should be alert to situations or transactions that could be indicative of abuse. Abuse is distinct from fraud and illegal acts. Abuse involves behavior that is deficient or improper (but not necessarily fraudulent or illegal) when compared with behavior that a prudent person would consider reasonable and necessary business practice given the facts and circumstances. The auditor is not required to detect abuse. However, if indications of abuse that could result in material misstatement of the financial statements or other financial data come to the auditor's attention, the auditor should apply audit procedures specifically directed to determine whether abuse has occurred and the effect, if any, on the financial statements. The auditor should consider both quantitative and qualitative factors in making judgments about the materiality of possible abuse and about related audit procedures. The determination of abuse is subjective, and the auditor does not provide reasonable assurance of detecting abuse. (See GAGAS, paragraphs 4.19-.20.)

Characteristics of Fraud

.23 Three conditions generally are present when fraud occurs:

- **Incentive/Pressure**—Management, other employees, or external parties (for example, for some improper payments) have an incentive or are under pressure, which provides a motive to commit fraud.

- **Opportunity**—Circumstances exist, such as the absence of controls, ineffective controls, or the ability of management to override controls, that provide an opportunity to commit fraud.

- **Attitude/Rationalization**—Individuals involved are able to rationalize committing fraud. Some individuals possess an attitude, character, or ethical values that allow them to knowingly and intentionally commit a dishonest act.

Generally, the greater the incentive or pressure, the more likely an individual will be able to rationalize the acceptability of committing fraud.

.24 Management is in a position that could permit it to perpetrate fraud by directly or indirectly manipulating accounting records; overriding controls, sometimes in unpredictable ways; or committing other fraudulent or improper acts.

Fraud Risk Factors

.25 Although fraud is usually concealed, the presence of **fraud risk factors** that indicate incentive/pressure, opportunity, or attitude/rationalization might alert the auditor to a significant risk of fraud. However, fraud risk factors do not necessarily indicate that fraud exists. Examples of fraud risk factors, classified by the two types of fraudulent misstatements and then by these three conditions, include the following:

a. **Examples** related to misstatements arising from fraudulent financial reporting:

- Incentive/Pressure—Incentive exists for management to report reduced program costs or costs that are consistent with budgeted amounts, or excessive pressure exists to meet unrealistic deadlines or other requirements.

- Opportunity—Key financial statement amounts are based on significant estimates that involve subjective judgments or uncertainties that are difficult to corroborate, or management is in a position to override controls for processing adjustments or unusual transactions.

- Attitude/Rationalization— Employees perceive that penalties exist for reporting honest results, or employees consider requirements such as performance targets unrealistic.

b. **Examples** related to misstatements arising from misappropriation of assets:

- Incentive/Pressure—Employees who are disgruntled because of impending layoffs have an incentive to misappropriate assets, or pressure to meet programmatic objectives such as for rapid benefit payments increases the risk of fraudulent improper payments.

- Opportunity—Employees have access to assets that are small in size and valuable or the authority to disburse funds, or a program has weaknesses in internal control related to fraudulent improper payments.

- Attitude/Rationalization—Employees believe that management is unethical, or individuals believe they are entitled to the entity's assets.

Fraud risk factors represent inherent or control risk factors. As discussed in paragraph .02, the auditor should consider fraud risk factors in assessing inherent and control risk. Sections 295A and 295B include additional examples of fraud risk factors.

Professional Skepticism

.26 The auditor should exercise professional skepticism—an attitude that includes a questioning mind and a critical assessment of audit evidence—throughout the audit. The auditor should maintain a mindset that recognizes the possibility that a material misstatement due to fraud might be present, regardless of any past experience with the entity and regardless of the auditor's belief about management's honesty and integrity.

Brainstorming Meeting(s) about Potential Fraud Risks

.27 Audit team members should exchange ideas in one or more "brainstorming" meeting(s) to identify potential fraud risks. They should discuss how and where the financial statements could be susceptible to material fraudulent misstatement, how management could perpetrate and conceal fraudulent financial reporting, how assets could be misappropriated (including through fraudulent improper payments), how management could override controls, and how the auditor might respond to these risks. They also should consider known internal and external fraud risk factors (including any related to fraudulent improper payments) and categorize these factors by type of misstatement and by incentive/pressure, opportunity, and attitude/rationalization. The brainstorming discussion should emphasize the need to exercise professional skepticism in gathering and evaluating evidence throughout the audit.

.28 The Audit Director, Assistant Director, and all other team members who have significant responsibilities in planning and performing the audit should participate in brainstorming, which may be performed in a single meeting or in multiple meetings. While different members may participate in different meetings, each brainstorming meeting should include at least one experienced team member, and all team members should be familiar with the collective results of the brainstorming meeting(s). Determining the brainstorming participants (for example, it might be useful to include stakeholders and specialists, such as IS auditors) and the number of brainstorming meeting(s) are matters of auditor judgment.

.29 The auditor's consideration of fraud risks should be ongoing throughout the audit. Near the completion of fieldwork, the auditor should evaluate whether the audit test results indicate the need for a change in the assessment of the fraud risks made earlier or the need for additional or different audit procedures (see paragraphs 540.18-.19). Accordingly, communications with the audit team members about fraud should occur as needed throughout the audit, and the auditor may hold multiple, periodic brainstorming meetings.

Information to Identify Fraud Risks

.30 Fraud risks might be identified as a result of replies to inquiries. To obtain information about fraud risks, the auditor should inquire of management about:

- any knowledge of fraud or suspected fraud (including fraudulent improper payments), or related allegations;
- management's understanding of fraud risks, including any specific risks the entity has identified and any account balances or classes of transactions having likely fraud risks (including information about any fraudulent improper payments that the agency identified in making assessments related to the Improper Payments Information Act of 2002);
- any antifraud programs and controls the entity has established;[2]
- the nature and extent that locations or business segments, if any, are monitored, and whether there are particular locations or segments for which fraud risks might be more likely;
- whether and how management communicates to employees its views on business practices and ethical behavior; and
- whether management has reported to the audit committee (referred to as "financial management advisory committee" in some federal entities) or others with equivalent authority and responsibility on how the entity's internal control prevents, deters, or detects fraud.

.31 In addition to inquiring of management, inquiring of others might provide a different perspective or provide other important information. Accordingly, the auditor should perform the following inquiries and related procedures:

a. Obtain information about instances of fraud (including any related to fraudulent improper payments) reported by the inspector general, ordinarily by asking the Special Investigator Unit to summarize how cases of reported fraud were committed, and then ask management or the Office of Inspector General whether related controls have been strengthened.

b. Inquire of the audit committee or others with equivalent authority and responsibility about fraud risks and any fraud or suspected fraud, and obtain an understanding of how they exercise oversight.

[2] An example document, *Management Antifraud Programs and Controls*, commissioned by the Fraud Task Force of the Auditing Standards Board of the AICPA, is available at the AICPA's web site, www.aicpa.org.

c. Inquire of internal audit personnel about fraud risks, any procedures to detect fraud during the reporting period, management's response to any such findings, and any fraud or suspected fraud.

d. Inquire of other personnel about fraud or suspected fraud. The auditor should use judgment to determine whom to ask and the extent of inquiries. For example, the auditor may make inquiries of employees with varying levels of authority, operating personnel not directly involved in the financial reporting process, employees familiar with complex or unusual transactions or with improper payments, and in-house legal counsel.

e. If inconsistencies arise from the auditor's inquiries of management and others, obtain additional evidence to resolve the inconsistencies.

.32 The auditor also should perform the following procedures:

a. Obtain and review the agency's (1) plan to identify improper payments and (2) report, if any, on improper payments (or information about any findings) that resulted from the agency's review under the Improper Payments Information Act of 2002.

b. Determine whether preliminary analytical procedures disclosed any unusual or unexpected relationships that might indicate fraud risks. Where revenue is (or is expected to be) material, analytical procedures should include those related to revenue—for example, trend analysis—to identify unusual or unexpected relationships that might indicate fraudulent financial reporting of revenue (see section 225 related to preliminary analytical procedures).

c. Consider whether any fraud risk factors exist (see paragraph .25).

d. Consider other information that might help identify fraud risks, such as information that resulted from previous audits, the brainstorming meeting(s), procedures related to accepting and continuing engagements, any reports on interim financial statements, and inherent risks identified at the account or transaction level.

Identification and Assessment of Fraud Risks

.33 To identify fraud risks (including any related to fraudulent improper payments), the auditor should perform the following procedures:

a. Evaluate the information obtained in the procedures described in paragraphs .28-.32, in the context of the three conditions that generally are present when fraud occurs— incentive/pressure, opportunity, and attitude/rationalization. While fraud risk might be greatest when all three of these conditions are evident, observation of one or more of these conditions might indicate a fraud risk.

b. Where revenue is (or is expected to be) material, evaluate whether there are fraud risks related to revenue recognition (for example, through premature recognition or fictitious revenue). If the auditor concludes that improper revenue recognition does not represent a fraud risk, the auditor should document the reasons supporting that conclusion (see paragraph 290.04 h).

c. Evaluate the possibility that management could override controls, even if specific fraud risks have not been identified.

.34 For each identified fraud risk, the auditor should determine whether it relates to (1) specific financial statement account balances or classes of transactions and related assertions or (2) more pervasively to the financial statements as a whole. Generally, relating fraud risks to the individual accounts, classes of transactions, and assertions helps in designing audit procedures in response to these risks.

.35 As part of understanding internal control sufficient to plan the audit, the auditor should (1) evaluate whether programs and controls that address identified fraud risks have been suitably designed and placed in operation and (2) determine whether these programs and controls mitigate these risks or whether specific control deficiencies exacerbate these risks. See section 350 regarding testing the operating effectiveness of controls that are determined to mitigate these risks.

.36 The auditor should assess the identified fraud risks, taking into consideration the results of the procedures described in the preceding paragraph. In making this assessment, using professional judgment, the auditor should consider all significant aspects of each of these risks , including the type of misstatement, the significance and pervasiveness of the risk, and the likelihood that it could result in a material misstatement.

Response to Assessed Fraud Risks

.37 The auditor must respond to the assessed risks of material misstatement due to fraud. The nature and significance of these fraud risks, as well as programs and controls that address identified fraud risks, influence the auditor's response. The auditor should use professional judgment in determining the appropriate

response for the circumstances and exercise professional skepticism in gathering and evaluating audit evidence. The response should (1) have an overall effect on the conduct of the audit (see paragraph .39), (2) address fraud risks that relate to management override of controls (see paragraph .40), and, (3) for any of these risks that relate to specific financial statement account balances or classes of transactions and related assertions, involve the nature, timing, and extent of audit procedures (see paragraph .41). If it is not practicable, as part of a financial statement audit, to design audit procedures that sufficiently respond to the fraud risks, the auditor should consider requesting assistance from the Special Investigator Unit.

.38 In some instances, the audit plan could, for reasons other than responding to fraud risk, include procedures and personnel and supervisory assignments that are sufficient to respond to a fraud risk. In these instances, the auditor may conclude that no further response is required. For example, with respect to timing, audit procedures could be planned as of the date that the reporting period ends, both as a response to a fraud risk and for other reasons.

.39 The auditor should respond to the fraud risks in ways that have an overall effect on the conduct of the audit, as follows:

a. **Assignment of personnel and supervision**—Assign audit team staffing and/or supervision so that the knowledge, skill, and ability of personnel assigned significant responsibilities are commensurate with the auditor's assessment of the fraud risks—for example, the auditor may assign a fraud specialist or more experienced personnel or may increase supervision in response to identified fraud risks (also see section 270 related to IS auditors).

b. **Review of accounting principles**—Review management's selection and collective application of significant accounting principles, particularly those related to subjective measurements and complex transactions.

c. **Unpredictability of audit procedures**—Incorporate an element of unpredictability in the selection of audit procedures from reporting period to reporting period—for example, perform substantive tests of selected account balances and assertions not otherwise tested due to their materiality and risk, adjust the timing of audit tests, use a different method to select items for testing, or perform procedures at different locations or at locations on an unannounced basis. Statistical sampling selection usually provides an element of unpredictability as to the specific items tested (see section 480). Generally, the auditor should not inform entity personnel of specific audit procedures prior to performing them.

.40 The auditor should perform the following procedures to specifically address the risk that management can perpetrate fraud by overriding controls:

a. **Examination of journal entries and other adjustments**—Examine journal entries and other adjustments for evidence of possible material misstatement due to fraud. These include reclassifications, consolidating entries, and other routine and nonroutine journal entries and adjustments. The auditor should obtain an understanding of the financial reporting process and the controls over journal entries and other adjustments; identify and select journal entries and other adjustments for testing; determine the nature, timing, and extent of the testing (ordinarily including tests of journal entries and other adjustments at the end of the reporting period); and inquire of individuals involved in the financial reporting process about inappropriate or unusual activity related to the processing of journal entries and other adjustments.

b. **Review of accounting estimates**—Review accounting estimates for biases that could result in material misstatement due to fraud. In preparing financial statements, management is responsible for making judgments or assumptions that affect significant accounting estimates and for monitoring the reasonableness of these estimates on an ongoing basis. The auditor should consider whether differences between (1) estimates best supported by the evidence and (2) the estimates included in the financial statements, even if the estimates are individually reasonable, indicate possible bias by management, in which case the auditor should reconsider the estimates taken as a whole. The auditor also should perform a retrospective review of significant accounting estimates used in the prior year's financial statements, focusing on sensitive or subjective aspects, to determine whether they indicate possible bias by management. Further, the auditor should be alert for aggressive or inconsistently applied estimates.

c. **Evaluation of business rationale for significant unusual transactions**—Evaluate the business rationale for any significant unusual transactions, considering whether (1) the form of these transactions is overly complex, (2) management has discussed the nature of and accounting for these transactions with the audit committee or others with equivalent authority and responsibility or the board of directors, if any, (3) management is placing more emphasis on particular accounting treatments than on the underlying economics of the transactions, (4) transactions that involve related parties have been properly reviewed and approved by the audit committee or others with equivalent authority and responsibility or the board of directors, if any, and (5) the transactions involve previously unidentified related parties (see

section 902) or related parties that do not have the substance or financial strength to support the transaction without assistance from the entity.

.41 For fraud risks related to specific financial statement account balances or classes of transactions and related assertions, the specific response will depend on the types of risks and the specific balances or classes and assertions, but it generally should involve both substantive and control tests. The response should involve the following:

a. **Nature** of audit procedures—for example, obtaining related evidence from independent external sources rather than internal sources;

b. **Timing** of audit procedures—for example, performing substantive testing at or near the end of the reporting period rather than at an interim date; and

c. **Extent** of audit procedures—for example, increasing audit sample sizes.

Section 295 I provides additional examples of responses.

[Subsequent sections of FAM 260, beginning at "Control Environment Factors," remain unchanged, and the numbering of paragraphs and pages will be conformed.}

280 - PLAN OTHER AUDIT PROCEDURES

.01 The auditor should consider the following areas during the planning phase, even though many related audit procedures will be applied during the other phases.

INQUIRIES OF LEGAL COUNSEL

.02 As discussed in AU 337 and section 550, the auditor should make inquiries of the entity's counsel and perform other audit procedures regarding litigation, claims, and assessments. Because of the amount of the time needed by management and the legal counsel to gather and report the necessary information (including the potential need for management to inquire of Department of Justice legal counsel on a case-specific basis), the auditor should plan the following procedures (which are described in more detail in AU 337) for an appropriate time in the audit:

- making inquiries of management regarding their policies and procedures used for identifying, evaluating, and accounting for litigation, claims, and assessment;

- obtaining a description and evaluation of all such matters existing as of the balance sheet date and through the date of management's response (which should be near the end of fieldwork);

- obtaining evidence regarding legal counsel used by the entity and matters handled; and

- sending letters of audit inquiry to legal counsel (the auditor may limit the inquiry to matters that are considered individually or collectively material to the financial statements, provided the entity and the auditor have reached an understanding and agreement on the materiality level).

MANAGEMENT REPRESENTATIONS

.03 As discussed in section 550, the auditor is required to obtain a representation letter from management on specific matters prior to completion of the audit. Particularly during first year audits and when standards change, the auditor may want to discuss these required representations with management early in the audit to identify and resolve any difficulties related to obtaining these representations. Note that for federal government auditors, these representations include (1) the effectiveness of internal control, (2) compliance with laws and regulations, and, (3) for CFO Act agencies, financial management systems' substantial compliance with FFMIA requirements. Additional guidance on management representations is provided in AU 333, AU 801, AT 101, AT 201, AT

501, AT 601, and section 1001 (Part II). Also, a summary of uncorrected misstatements aggregated by the auditor is to be included or attached to the letter, which should state management's belief that the effects of the misstatements are immaterial to the financial statements taken as a whole, both individually and in the aggregate. (See section 595 D for an example summary of uncorrected misstatements.)

RELATED PARTY TRANSACTIONS

.04 AU 334 and sections 550 and 902 provide guidance on audit procedures that should be performed to identify related parties and related party transactions as well as examining these transactions for appropriate disclosure in the financial statements. During the planning phase, the auditor should perform procedures to identify and document related parties and the nature of related party transactions that might need to be disclosed in the financial statements and related notes. Such information should be distributed to all members of the audit team for use in summarizing and testing related party transactions and identifying any additional related parties.

SENSITIVE PAYMENTS

.05 In the planning phase, the auditor should consider the audit procedures that will be applied to sensitive payments. Sensitive payments encompass a wide range of functions, including executive compensation, travel, official entertainment funds, unvouchered expenditures, consulting services, speaking honoraria and gifts, and executive perquisites. See GAO's *Guide for Evaluating and Testing Controls Over Sensitive Payments*, GAO/AFMD-8.1.2, Washington, D.C.: May 1993.

REACHING AN UNDERSTANDING WITH OFFICIALS OF THE ENTITY AND REQUESTERS

.06 During planning, the auditor should reach an understanding with officials of the entity, including management and individuals contracting for or requesting the audit, about the work to be performed, as required by AU 310 and GAGAS (chapter 4). If the audit is done based on the request of a committee or member of Congress, the auditor should communicate with that committee or member as well as management. If the audit is required by law or is self-initiated, the auditor should communicate with the committee members or staff who have oversight of the auditee as well as management.

.07 The auditor should communicate with officials of the entity and the committee or member in writing (preferred) or orally and document the understanding reached. "Commitment" letters may be used to communicate with Congress about the

auditor's planned work. In drafting commitment letters, the auditor should consider the matters required to be communicated by the auditing standards. If the audit organization has a general ongoing working relationship with Congress and prior audit reports, there may already be an understanding with the applicable committee or other requester.

.08 Because of an ongoing working relationship with either a requester or management, the auditor may affirm the contents of the prior audit report, since the types of information included in the understanding are generally included in the objectives, scope, and methodology section of the audit report.

.09 Examples of the matters that are generally included in the understanding are the objectives and limitations of the audit and management's and the auditor's responsibilities. These are described in AU 310. GAGAS also require the understanding to relate to the auditor's responsibility for testing and reporting on compliance and internal control.

OTHER AUDIT REQUIREMENTS

.10 Under GAGAS, chapter 4, the auditor should consider the results of previous audits and attestation engagements and follow up on known significant findings and recommendations that relate directly to the objectives of the current audit. Generally, a financial audit should cover areas that had findings and recommendations in previous audits. However, the auditor should consider whether any findings and recommendations from the prior year financial audit need follow-up that would not otherwise be covered (for example, findings at locations that would not otherwise be revisited).

.11 During planning, the auditor also should consider the additional requirements in OMB audit guidance for legal letters, management representation letters, and certain agreed-upon procedures. OMB audit guidance has specific dates by which interim and updated legal letters for CFO Act agencies and covered executive agencies subject to the Accountability of Tax Dollars Act of 2002[1] are to be requested and received, specific formats for summarizing the information in the letters, and a list of specific officials to whom copies of the letters and summaries should be forwarded. The guidance also has an example of a management representation letter. In addition, the guidance requires that certain agreed-upon procedures be applied to agency payroll offices and requires that reports be submitted to OPM by a specific date.

[1] OMB issued guidance implementing the act by applying its guidance for CFO Act agencies to covered executive agencies.

290 – DOCUMENTATION

[Pages 290-1 to 290-2 remain unchanged. Revised pages follow.]

associates them with significant financial statement line items and assertions. For each risk identified, the auditor documents the (1) nature and extent of the risk, (2) condition(s) that gave rise to that risk, and (3) specific cycles, accounts, line items, and related assertions affected (if not pervasive). The auditor also documents conclusions on the overall effectiveness of the control environment, risk assessment, communication, and monitoring. In addition, the auditor generally should document the entity's basis for its determination of substantial compliance of its systems with FFMIA requirements.

h. **Fraud risks (section 260)**. The auditor should document (also see paragraph 290.07):

- specific fraud risks (categorized by type of misstatement and by incentive/pressure, opportunity, and attitude/rationalization) that were identified and the assessment of those risks;
- if the auditor did not consider improper revenue recognition to represent a fraud risk, the reasons supporting that conclusion;
- consideration of the risk of management override of controls; and
- the auditor's response to the assessed fraud risks. (Also see section 590.)

i. **Effects of IS (section 270):** The auditor should document

- a basic understanding of the IS aspects of the financial management system, including the significance of IS to the entity (section 220);
- the inherent risks arising from IS (paragraph 260.17);
- the impact of IS on the control environment, risk assessment, communication, and monitoring (paragraphs 260.41-.42); and
- tentative conclusions on the likelihood that IS controls are operating effectively (section 270).

When the auditor prepares documentation of the above information, the IS auditor generally should review and agree with the content. Tentative conclusions on the likelihood that IS controls are operating effectively should also be reviewed and concurred to by the Audit Director and Assistant Director as part of their reviews of the General Risk Analysis or equivalent. If IS controls are not likely to be effective, the auditor should document supporting evidence and generally should report such findings as discussed in section 580.

j. **Operations controls to be tested, if any (section 275).**

k. **Other planned audit procedures (section 280).**

l. **Locations to be visited (section 285):** This information includes

- the locations selected,
- the basis for selections,
- the general nature of procedures planned for each location,
- the determination of the number of items for testing,
- the allocation of those items among the selected locations, and
- other procedures applied.

m. **Staffing requirements.**

n. **Audit timing, including milestones.**

o. **Assistance from entity personnel.**

.05 The **Cycle Matrix** or equivalent links each of the entity's accounts (in the chart of accounts) to a cycle, an accounting application, and a financial statement line item or RSSI (paragraph 240.06). This information may instead be incorporated into the Account Risk Analysis or equivalent.

.06 The **Account Risk Analysis** or equivalent contains the audit plan for each significant line item and account and should identify significant line items, accounts, assertions, and cycles/accounting applications (sections 235 and 240, respectively). The auditor also summarizes and documents the specific risks, other than pervasive risks, as well as the inherent, fraud, and control risk factors, for use in determining the nature, timing, and extent of the audit procedures. The auditor may also include insignificant accounts in each line item ARA or equivalent, indicating their insignificance and the consequent lack of audit procedures applied to them. In such instances, the cycle matrix or equivalent need not be prepared.

.07 The auditor also should document (section 260):

- the brainstorming meeting(s) about potential fraud risks, including how and when the discussion(s) occurred, the audit team members who participated, and the general matters discussed;
- the procedures performed to obtain information about, identify, and assess fraud risks; and
- any other significant procedures performed or other significant matters related to the auditor's consideration of fraud (and any significant abuse).

.08 The auditor should document the understanding reached with officials of the entity and requesters about the work to be performed, as described in section 280.

.09 The auditor also should consider the needs of, and consult in a timely manner with, other auditors who plan to use the work being performed, especially in areas where the auditor makes decisions requiring significant auditor judgment. Where the auditor deviates from a policy or procedure expressed by use of the term "must" or "should" in the FAM, he or she should provide an opportunity for the other auditors to review the documentation of the reasons explaining these deviation decisions.

295 I - EXAMPLES OF AUDITOR RESPONSES TO FRAUD RISKS INVOLVING THE NATURE, TIMING, AND EXTENT OF AUDIT PROCEDURES

.01 As discussed in section 260, the auditor's response to assessed fraud risks should (1) have an overall effect on the conduct of the audit, (2) address fraud risks that relate to management override of controls, and (3)—for any fraud risks that relate to specific financial statement account balances or classes of transactions and related assertions—involve the nature, timing, and extent of audit procedures. This section provides examples of auditor responses in this third category—changing the nature, timing, and extent of audit procedures.

EXAMPLES OF AUDITOR RESPONSES TO FRAUD RISKS INVOLVING THE NATURE, TIMING, AND EXTENT OF AUDIT PROCEDURES

.02 Examples of auditor responses to fraud risks involving the nature, timing, and extent of audit procedures include the following:

- Inquire of management and other personnel involved in areas having fraud risks, such as risks related to any improper payments, to obtain their insights about those risks and whether and how controls mitigate those risks.

- Inquire of additional members of management, such as program directors or center directors, or other nonaccounting personnel to assist in identifying issues and corroborating other evidential matter.

- Use data mining or other computer-assisted audit techniques (such as Interactive Data Extraction and Analysis) to gather more extensive evidence about data contained in significant accounts. Such techniques can be used to select audit sample items from electronic files, sort items with specific characteristics (to perform substantive analytical procedures or make a nonrepresentative selection), or test an entire population.

- Inspect, or observe physical counts of, tangible assets, such as property, plant, and equipment and certain inventories, for which other procedures might otherwise have been sufficient.

- Conduct surprise or unannounced procedures, such as inventory observations or cash counts on unexpected dates or at unexpected locations.

- Make inquiries of major suppliers or customers in addition to obtaining written confirmations, request confirmations of a specific individual within an organization, or request confirmation of additional or different information.

- Where a specialist's (see section 650 and AU 336) work is particularly significant, perform additional procedures related to some or all of the specialist's methods, assumptions, or findings to evaluate whether the findings are unreasonable, or engage another specialist to do that.

- Perform additional or more focused tests of budget to actual variances and their underlying causes.

- Perform targeted tests of the timing of cost/expense recognition.

- Request that physical inventory counts be made on, or closer to, the date that the reporting period ends.

- If fraud risks relate to an interim period, perform audit tests that are focused on transactions that occurred in that interim period (or throughout the reporting period).

- Test a larger sample of disbursement transactions for validity.

- Perform substantive analytical procedures that are more detailed by location, program, month, or other category (for example, analyzing specific credit lines in an allowance for loan losses, rather than the portfolio as a whole) or that use more precise techniques (for example, regression analysis).

- Discuss with other auditors who are auditing the financial statements of one or more agency components the extent of work necessary to address fraud risks resulting from intragovernmental transactions and activity among those components.

ADDITIONAL EXAMPLES OF AUDITOR RESPONSES TO FRAUD RISKS RELATED TO MISSTATEMENTS ARISING FROM FRAUDULENT FINANCIAL REPORTING

.03 The following paragraphs provide additional examples of auditor responses to fraud risks related to misstatements arising from fraudulent financial reporting in the areas of (1) management's estimates, (2) revenue recognition, and (3) inventory quantities. These example responses involve the nature, timing, and extent of audit procedures.

Management's Estimates

.04 Fraud risks might relate to management's development of accounting estimates. These risks might affect various accounts and assertions, such as valuation and completeness of liabilities related to insurance and credit programs, pensions, postretirement benefits, and environmental cleanup. These risks might also relate to significant changes in assumptions for recurring estimates. Further, because estimates are based on both subjective and objective factors, bias might exist in the subjective factors.

.05 Examples of procedures that the auditor might perform in response to fraud risks related to management estimates include the following:

- Gather additional information about the entity and its environment to assist in evaluating more extensively the reasonableness of management's estimates and underlying judgments and assumptions, focusing on more sensitive or subjective aspects.

- Perform a more extensive retrospective review of management judgments and assumptions applied in estimates made for prior periods, such as analyzing each significant judgment and assumption in light of the events that occurred subsequently and identifying reasons for any differences. Consider whether these reasons should affect the current period's estimates.

- Use the work of a specialist to evaluate management's estimate, or develop an independent estimate to compare to management's estimate.

Revenue Recognition

.06 Revenue recognition is affected by the particular facts and circumstances and sometimes—for example, for certain government corporations—by accounting principles that can vary by type of operations. Hence, where revenue is (or is expected to be) material, the auditor should be familiar with the applicable criteria for revenue recognition by a federal government entity, and the audit procedures should reflect the auditor's understanding of the entity and its environment, including the composition of revenue, specific attributes of the revenue transactions, and specific entity considerations.

.07 Examples of procedures that the auditor might perform in response to fraud risks related to improper revenue recognition include the following:

- Perform substantive analytical procedures related to revenue that are based on more precisely developed expectations, such as comparing revenue between the current year and expectations based on prior fiscal years, by location, program, and month, or that establish the limit (see paragraphs 475.04-.05) at a lower percent of test materiality. Audit techniques such as regression analysis might be helpful in performing these procedures.

- Inquire of the entity's personnel, including its general counsel, about any revenue-related transactions near the end of the reporting period and their knowledge of any unusual terms or conditions that might be related to those transactions.

- Confirm with customers and other appropriate parties the relevant contract terms and the absence of side agreements that might influence the appropriate accounting.

- Physically observe goods being shipped or readied for shipment (or returns awaiting processing) at one or more locations at the end of the reporting period and perform appropriate sales and inventory cutoff procedures.

- Where revenue transactions are electronically initiated, processed, and recorded, expand control tests related to these transactions.

Inventories

.08 Examples of procedures that the auditor might perform in response to fraud risks related to inventories include the following:

- Review the entity's inventory records to identify locations, items, or issues that warrant specific attention during or after the physical inventory count. As a result, the auditor might decide to observe inventory counts at some locations on an unannounced basis or to request that physical inventory counts be made at all locations on the same date and on a date that is on, or closer to, the date that the reporting period ends.

- Perform additional inventory observation procedures, such as more rigorously examining the contents of boxed items, the manner in which the inventory is stacked (to identify hollow squares or other issues) or labeled, and—using the work of a specialist, if needed—the purity, grade, and concentration of inventory substances such as specialty chemicals.

- Perform additional tests of physical inventory count sheets or tags, and retain copies of these documents to minimize the risk of subsequent alteration or inappropriate extension and summarization of the inventory.

- Perform additional procedures focused on the quantities included in the priced inventory to further test the count quantities—such as comparing quantities for the current period with those for prior periods by inventory category, location, or other criteria, or comparing count quantities with perpetual records.

- Use computer-assisted audit techniques (such as Interactive Data Extraction and Analysis) to test the extension and summarization of the physical inventory counts—such as sorting by tag number to test tag controls or by item number to test for item omission or duplication—and to test for unusual quantities and cost amounts.

- When performing substantive analytical procedures related to inventories, establish the limit (see paragraphs 475.04-.05) at a lower percent of test materiality.

ADDITIONAL EXAMPLES OF AUDITOR RESPONSES TO FRAUD RISKS RELATED TO MISSTATEMENTS ARISING FROM MISAPPROPRIATION OF ASSETS

.09 Additional examples of auditor responses to fraud risks related to misstatements arising from misappropriation of assets involving the nature, timing, and extent of audit procedures include the following:

- Use information on any improper payments, including information resulting from the agency's review of programs and activities under the Improper Payments Information Act of 2002, to develop and perform audit procedures that are focused on specific vulnerable areas.

- For benefit programs, expand the extent of participant eligibility testing, including unannounced visits to intake centers or work sites to test the existence and identity of participants, or observe benefit payment distribution to identify "ghost" participants or use confirmation requests to test the existence of program participants. Data mining can be used to search for duplicate payments, ineligible or ghost participants, and other issues.

- For particular assets that are highly susceptible to misappropriation, obtain a more comprehensive understanding of internal controls related to preventing

and detecting such a misappropriation and expand the tests of those controls, and physically inspect those assets at or near the end of the reporting period.

- Assign higher levels of control risk to specific locations that have higher fraud risks (such as when large quantities of assets that are particularly susceptible to such risks are present at some locations) and modify audit procedures at those locations.

- When performing substantive analytical procedures related to assets that are particularly susceptible to misappropriation, establish the limit (see paragraphs 475.04-.05) at a lower percent of test materiality.

540 – EVALUATE MISSTATEMENTS

[Pages 540-1 to 540-6 remain unchanged. Revised pages follow.]

- The auditor may believe that sufficient evidence has already been obtained and may form his/her opinion on the financial statements based on his/her estimate.

- The auditor may want to increase assurance in the likely misstatements in order to convince entity management of the amount or to support the report on the financial statements. For example, the auditor may choose to increase his/her assurance in the likely misstatement by testing additional items. These additional procedures will most likely increase the auditor's assurance in the previous findings but generally will not materially affect the amount of the likely misstatement. Before deciding to perform additional procedures, the auditor should obtain agreement from entity management on the extent of additional evidence needed to be persuasive to them. The auditor also should consult with the Reviewer before beginning any of these additional procedures.

- The Audit Director may decide not to expend additional resources to resolve the disagreement, for example, because additional testing is unlikely to provide different conclusions. If the auditor believes the estimate is sufficiently accurate, he or she would express a qualified or adverse opinion, depending on the materiality of the item to the financial statements taken as a whole. If the auditor believes the estimate is not sufficiently accurate, he or she would qualify or disclaim an opinion for a scope limitation, depending on the materiality of the item to the financial statements taken as a whole.

RECONSIDERATION OF FRAUD RISK

.18 The auditor's consideration of fraud risks should be ongoing throughout the audit, and evidence gathered during fieldwork could change or support an earlier judgment about fraud risks. For example, during fieldwork, the auditor might identify discrepancies in the accounting records or conflicting or missing evidence.

.19 Near the completion of fieldwork, the auditor should evaluate whether the audit test results indicate the need for a change in the assessment of the fraud risks made earlier or the need for additional or different audit procedures. The auditor should (1) perform overall analytical procedures related to revenue, if revenue is (or is expected to be) material, (2) consider whether substantive or overall analytical procedures indicate a previously unrecognized fraud risk, (3) consider whether responses to inquiries during the audit have been vague, implausible, or inconsistent with other evidence, and (4) consider other evidence gathered during the audit. Further, the Audit Director should determine that appropriate

communications have occurred among the audit team members regarding fraud risks.

.20 When audit test results identify misstatements, the auditor should consider whether these might be indicative of fraud. If, preliminarily, the auditor believes that a misstatement is or might be the result of fraud, the auditor should (1) consult with the Audit Director and the Reviewer, who will determine whether to seek assistance from the Special Investigator Unit or OGC, and, (2) if performing the audit under contract, consult with the Assistant Inspector General for Audit, or the GAO Managing Director, having responsibility for the audit. Then, if, on the basis of evidence obtained, the auditor believes that an instance of fraud (or significant abuse) has occurred or is likely to have occurred, the auditor should (1) consult with the Special Investigator Unit and OGC, (2) include relevant information in the audit report unless the instance is clearly inconsequential, and (3) determine that the audit committee or others with equivalent authority and responsibility are adequately informed. In some circumstances, the auditor may be required by law or regulation to report directly to outside parties about fraud (or significant abuse). However, the auditor should limit public reporting to matters that would not compromise any related investigative or legal proceedings. (See GAGAS, paragraphs 5.12 and 5.17-.25.)

.21 If a misstatement is or might be the result of fraud and the effect is not material to the financial statements, the auditor should evaluate the implications, especially those regarding the organizational position and responsibilities of the individual involved. If the matter involves a relatively low-level employee who is not responsible for significant activities (for example, a misappropriation from a small petty cash fund by a nonmanagement employee), the auditor may conclude that the matter has little significance to the audit. However, if the matter involves higher-level management, even though the amount of misstatement is not material to the financial statements, the auditor should consider whether (1) it is qualitatively material and (2) it might indicate a more pervasive problem. Accordingly, the auditor should reevaluate the assessment of fraud risk, as well as the assessment of inherent and control risk, and the resulting effects on the nature, timing, and extent of substantive testing. Regardless of the level of the employee, the auditor should report the misstatement to at least the next level of management. In addition, the auditor should reach an understanding with the audit committee or others with equivalent authority and responsibility regarding the nature and extent of communications with them about misappropriations perpetrated by lower-level employees.

.22 If a misstatement is or might be the result of fraud and either the effect could be material or the auditor is unable to determine whether the effect is material, the

auditor should, (1) if applicable, attempt to obtain additional evidential matter to demonstrate whether material fraud has occurred or is likely to have occurred and its effect on the financial statements and the related audit report, (2) consider the implications for other aspects of the audit, including reevaluating the assessment of risks and the resulting effects on testing as described in the preceding paragraph, (3) discuss the matter and the approach for further investigation with at least the next higher level of entity management and with senior management and the audit committee or others with equivalent authority and responsibility, and (4) consider whether to advise entity management to consult with its general counsel.

.23 **Fraud involving senior management and fraud that causes a material misstatement** of the financial statements should be discussed in the audit report. Depending on circumstances, it could affect the report on compliance with laws and regulations, the report on the financial statements, and/or the significant matters section. The auditor should consult with the Audit Director and the Reviewer and should report the matter to the audit committee or others with equivalent authority and responsibility.

.24 If the auditor has identified fraud risk factors that have control implications, the auditor should consider whether these risk factors represent reportable conditions that should be included in the audit report in the internal control section. Further, the auditor should consider whether the absence of, or deficiencies in, antifraud programs and controls also represent reportable conditions.

FINANCIAL MANAGEMENT SYSTEMS

.25 For audits of the CFO Act agencies and components identified by OMB in its audit guidance, the auditor should determine whether the entity's financial management systems substantially comply with the three requirements of FFMIA. Federal financial management systems requirements and the SGL at the transaction level were considered in sections 350 and 360. At this point, the auditor should reassess those preliminary conclusions and conclude on the federal accounting standards based on the results of control, compliance, and substantive testing and evaluation of misstatements found. If the auditor concludes that the systems do not substantially comply with the requirements, he or she should report the noncompliance. In addition, if the auditor concluded the systems were not in substantial compliance with FFMIA based on limited testing, he or she should report that the work on FFMIA would not necessarily disclose all instances of lack of substantial compliance with FFMIA requirements. (See section 580.)

590 – DOCUMENTATION

.01 The auditor should document the nature and extent of work performed in the reporting phase and the related conclusions. Such documentation should include

- evaluation of misstatements,
- inquiries of legal counsel,
- subsequent events,
- management representations,
- related party transactions, and
- procedures performed to determine consistency of the other information in the Accountability Report with the financial statements and on conformity with OMB guidelines on form and content of financial statements.

SPECIFIC DOCUMENTATION CONSIDERATIONS

Audit Summary Memorandum

.02 At the completion of the audit, an audit summary memorandum should be prepared that summarizes the audit results and demonstrates the adequacy of the audit procedures and the reasonableness of the conclusions on the financial statements, internal control, substantial compliance of the financial management systems with the FFMIA requirements, the entity's compliance with laws and regulations, MD&A (the overview of the entity), required supplementary information (including RSSI), and other accompanying information.

.03 The audit summary memorandum generally should refer to other documentation where this information is described in more detail. The memorandum should briefly summarize and allow the reader to easily refer in the documentation to:

- any significant changes from the auditor's original assessment of the control environment, risk assessment, communication, and monitoring or inherent or control risk and significant revisions of audit procedures;

- any additional fraud risks or other conditions beyond those considered in planning (section 260), including analytical relationships, identified during the audit that caused the auditor to believe additional audit procedures or any other response was required, as well as any further response the auditor concluded was appropriate;

- the results of the procedures performed to specifically address the risk of management override of controls;

- the auditor's considerations about any misstatement that the auditor believes is or might be the result of fraud;

- the nature of any communications about fraud or possible fraud (and any significant abuse) made to management, the audit committee or others with equivalent authority and responsibility, the Special Investigator Unit or others in the Office of Inspector General, and others;

- the auditor's summary conclusions related to the consideration of fraud;

- significant accounting, auditing, or reporting issues;

- any limitations on the audit scope and the auditor's assessment of whether the audit procedures were adequate to support conclusions on the financial statements, internal control, the systems' substantial compliance with FFMIA requirements, compliance with laws and regulations, MD&A, required supplementary information (including RSSI), and other accompanying information;

- the auditor's conclusions on whether the audit evidence obtained supports the conclusions on the financial statements, internal control, the systems' substantial compliance with FFMIA requirements, compliance with laws and regulations, MD&A, required supplementary information (including RSSI), and other accompanying information;

- the auditor's conclusion on whether the audit was done in compliance with GAGAS, OMB audit guidance, and the GAO/PCIE *Financial Audit Manual* and whether the report is appropriate;

- the auditor's conclusion on whether the entity's financial statements comply with U.S. generally accepted accounting principles;

- significant subsequent events, if any;

- the Summary of Unadjusted Misstatements;

- a summary of internal control weaknesses and a comparison of those the auditor found to the weaknesses reported in management's assertion about the effectiveness of internal control;

- a summary of instances of the systems' lack of substantial compliance with FFMIA requirements, including areas in which there is substantial but not full compliance;

- a summary of instances of noncompliance with laws and regulations; and

- the documentation of overall analytical procedures.

Overall Analytical Procedures

.04 The following items should be documented for overall analytical procedures:

- **Data used and sources of data:** The documentation on the specific financial data used for the current-year amounts and the data used for comparison should include the amounts of the financial items; the dates or periods covered by the data; whether the data were audited or unaudited; the persons from whom the data were obtained, if applicable; and the source of the information (e.g., the general ledger trial balance, prior-year audit documentation, or prior-year financial statements).

- **Parameters for identifying significant fluctuations:** These parameters are left to the auditor's judgment.

- **Explanations for significant fluctuations and sources of these explanations:** Explanations obtained should be consistent with corroborating evidence in the documentation and should be referenced to this work.

- **Auditor's conclusions on the results of the procedures:** The auditor's conclusions on the results of overall analytical procedures should be documented.

Considering Weaknesses in Internal Control

.05 The basis for considering internal control weaknesses as material weaknesses, other reportable conditions, or as not reportable, should be documented. Any oral communications of control weaknesses that are not included in a written report should be documented. Procedures performed to determine the effects of misstatements and weaknesses in internal control on other reports prepared and used by the entity also should be documented.

Reporting Lack of Systems' Substantial Compliance With FFMIA Requirements

.06 The basis for considering whether systems' noncompliances with FFMIA requirements represent lack of substantial compliance should be documented.

Reporting Instances of Noncompliance

.07 The basis for classification of instances of noncompliance as material noncompliance, other reportable noncompliance, or not reportable should be documented. Any oral communications of noncompliance that are not included in a written report should be documented.

Appendix B

INSTANCES WHERE THE AUDITOR "MUST" COMPLY WITH THE FAM

.01 In the paragraphs listed below the word "must" is used to indicate a situation in which the auditor is required to comply with the FAM:

100.04 (footnote)	In opining on internal control, the opinion must be on internal control and not management's assertion if material weaknesses are present.
100.17	The audit must be designed to achieve the objectives of OMB audit guidance.
100.23	The auditor must exercise judgment properly, assuring that, at a minimum, the work meets professional standards.
260.37	The auditor must respond to the assessed fraud risks.
295 C.07	The auditor must apply analytical or other substantive procedures to locations not tested in using nonrepresentative sample selection, unless immaterial.
310.06	The auditor must evaluate and test certain controls.
310.08	The auditor must test the effectiveness of controls if the controls have been determined to be effective in design.
340.09	The auditor must test controls that are likely to be effective.
395 G.02	In using rotation testing of controls, the auditor must annually perform some work in areas not selected for testing.
475.07	In order to rely on a substantive analytical procedure, a difference that exceeds the limit must be explained.
475.12	In performing a substantive analytical procedure, if the explanation is not adequate to explain the difference, the auditor must do additional substantive testing.

475.13 Additional procedures must provide adequate assurance that misstatements that exceed test materiality are identified.

475.15 The auditor must obtain an overall understanding of current-year financial statements in using overall analytical procedures at the financial statement level.

480.06 When using nonrepresentative selection, the auditor must not project results to the portion of the population not tested and must apply other procedures to the remaining items unless immaterial.

480.07 In representative sampling, each item in the population must have the opportunity to be selected.

480.14 In sampling, sample items must be selected from all items so that each item has an opportunity to be selected.

480.47 The auditor must evaluate the quantitative and qualitative effects of known and projected misstatements in relation to the financial statements as a whole.

490.03 The auditor must consider the implications of misstatements detected in applying supplemental analytical procedures.

495 A.11 In using analytical procedures, if an account is compared with another current year amount, that amount must be audited by means other than an analytical procedure using its relationship to this account.

495 A.12 In analytical procedures, the auditor must document why a prior year amount has a plausible and predictable relationship with the current year amount, and adjustments must be supported by reliable data and corroborated. (Four "musts" in paragraph.)

495 A.21 In using computer-produced data in performing analytical procedures, the auditor must either test the IS controls in the system or test the reliability of the data produced. (Two "musts" in paragraph.)

495 C.04 The auditor must perform additional procedures to extend the results of interim testing to year-end.

510.01	The auditor must conclude on the financial statements, internal control, FFMIA requirements, compliance, and other information included.
520.01	The auditor must perform overall analytical procedures.
520.07	(First bullet.) In overall analytical procedures, the auditor must use audited, final current-year amounts.
540.07	The auditor must bring all misstatements found to management's attention (except those below the auditor-designated amount at which misstatements need not be accumulated).
570.01, 580.14	The auditor must determine whether the audit was conducted in accordance with GAGAS, OMB audit guidance, and the GAO/PCIE financial audit methodology, and document the conclusion on compliance.
580.22	The auditor must consider whether the financial statements are materially affected by a departure from U.S. generally accepted accounting principles.
580.39	In order to express an opinion on internal control, the auditor must have a management assertion about the effectiveness of internal control and must be able to perform all the procedures considered necessary. (Two “musts” in paragraph.)

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650 - USING THE WORK OF OTHERS

[Pages 650-1 to 650-7 remain unchanged. Revised pages follow.]

Type of reporting	Evaluate the other auditors' independence and objectivity (paragraphs 650.11-.24)	Evaluate the other auditors' qualifications (paragraphs 650.25-.35)	Level of Review (paragraphs 650.36-.42)	Hold discussions and/or perform supplemental tests (paragraphs 650.43-.47)
Report concurs with the other auditors' report or does not mention the other auditors' work (paragraph 650.09 d and e)	Yes	Yes	High, moderate, or low	Yes for internal auditors' work (should include supplemental tests). Yes for auditors' work for high level of review. No for auditor's work for moderate or low level of review

EVALUATING THE OTHER AUDITORS' OR SPECIALISTS' INDEPENDENCE AND OBJECTIVITY

.11 Unless the auditor has no association with the report, the auditor should evaluate the other auditors' or specialists' independence and objectivity. Where the auditor has previously used the work of the same other auditors, the auditor generally should update the previous evaluation. Under GAGAS, chapter 3, audit organizations and individual auditors should be free both in fact and appearance from personal, external, and organizational impairments to independence. The auditor should first evaluate organizational independence. Different standards apply to CPA firms, other organizationally independent auditors, internal auditors, and specialists.

.12 For CPA firms and specialists, the contracting process is designed to select a firm that is independent and objective. The statement of work or request for proposal should ask the firms to represent that they are independent and objective with respect to the auditee and should request the firms to describe in their proposals all work, including nonaudit services, they have done for the auditee in the last several years (see GAGAS, chapter 3, and *Government Auditing Standards: Answers to Independence Questions* (GAO-02-870G, July 2002)). The technical

evaluation panel should evaluate whether the nature and extent of this work or other factors cause an independence or objectivity issue. In this evaluation, the panel may consider, for example, whether (1) the other auditors will need to audit their own work or (2) whether the other auditors made management decisions or performed management functions.

.13 If possible,[1] the auditor should have a role in contracting for the CPA firm or specialist. When the auditor does not participate in contracting for the CPA firm or specialist, the auditor generally should obtain an overview of the contracting process; this generally should include reading the statement of work or request for proposal and the proposal of the firm selected, and understanding the evaluations of the panel selecting the firm. The auditor should determine whether the firm provided a representation as to independence and objectivity (usually in its proposal). If the firm has not provided a representation as to independence and objectivity, the auditor should obtain a representation from the firm. If the auditor is not familiar with the firm, the auditor should inquire of professional organizations (such as the American Institute of Certified Public Accountants or the Public Company Accounting Oversight Board established by the Sarbanes-Oxley Act of 2002) as to the firm's professional reputation and standing.

.14 For government auditors, the auditor should decide whether the other audit organization is organizationally independent to report externally or whether it should be considered an internal audit organization. The auditor may refer to the work of organizationally independent government auditors but should not refer to the work of internal audit organizations in the audit report; generally more extensive review and supervision are necessary when dealing with internal auditors. The auditor should obtain written representations from the head of the government audit organization that to the best of his or her knowledge, the organization and the individual auditors doing the work are independent of the entity being audited. This means that the individual auditors are free of personal impairments to independence and maintain an independent attitude and appearance; it also means that the organization is free from external impairments and is organizationally independent (see GAGAS, chapter 3). The representation letter may indicate the general criteria for determining independence, such as "under the criteria in GAGAS." The representations should be for the period of the financial statements to the date of the other auditors' report. Since the decision on the independence and objectivity of the other auditors is needed to

[1] Under the CFO Act, if the IG is not doing the audit, he or she is required to determine the independent external auditor (CPA firm) that will do the work.

plan the auditor's work, the auditor generally should obtain oral representations early in the audit, with written representations at the end of the audit.[2]

.15 Government auditors may be presumed to be free from organizational impairments to independence when reporting externally to third parties if their audit organization is organizationally independent of the audited entity. Government audit organizations may meet the requirement for organizational independence in a number of ways. There is a presumption that a government audit organization is organizationally independent (GAGAS, chapter 3) if the audit organization is

a. assigned to a level of government other than the one to which the audited entity is assigned (federal, state, or local), for example, a federal auditor auditing a state government program, or

b. assigned to a different branch of government within the same level of government as the audited entity, for example, a legislative auditor auditing an executive branch program.

.16 There is also a presumption of organizational independence if the head of the audit organization (GAGAS, chapter 3) meets one of the following:

a. directly elected by voters of the jurisdiction being audited,

b. elected or appointed by a legislative body, subject to removal by a legislative body, and reports the results of audits to and is accountable to a legislative body,

c. appointed by someone other than a legislative body, so long as the appointment is confirmed by a legislative body and removal from the position is subject to oversight or approval by a legislative body, and reports the results of audits to and is accountable to a legislative body, or

d. appointed by, accountable to, reports to, and can only be removed by a statutorily created governing body, the majority of whose members are independently elected or appointed and come from outside the organization being audited.

.17 If the other audit organization or its head meets one of the above criteria, the auditor need not perform any procedures concerning organizational

[2] Obtaining a representation from the head of the audit organization is similar to the procedure for CPA firms under AU 543.10b.

independence other than to obtain a representation letter from the head of the audit organization as noted in paragraph 650.14 (see paragraph 650.23 for tests of personal independence). However, if the auditor encounters evidence that the audit organization might not be organizationally independent, the auditor should consider the need for inquiries and other procedures; the auditor should then evaluate the results of these procedures.

.18 In addition to the presumptive criteria, GAGAS recognize that there may be other organizational structures under which a government audit organization could be free from organizational impairments. These other structures should provide sufficient safeguards to prevent the audited entity from interfering with the audit organization's ability to perform the work and report the results impartially. For the audit organization to be considered free from organizational impairments to report externally under a structure different from the ones listed above, the audit organization (GAGAS, chapter 3) should have **all** of the following safeguards:

a. statutory protections that prevent the abolishment of the audit organization by the audited entity,

b. statutory protections that require that if the head of the audit organization is removed from office, the head of the agency should report this fact and the reasons for the removal to the legislative body,

c. statutory protections that prevent the audited entity from interfering with the initiation, scope, timing, and completion of any audit,

d. statutory protections that prevent the audited entity from interfering with the reporting on any audit, including the findings, conclusions, and recommendations, or the manner, means, or timing of the audit organization's reports,

e. statutory protections that require the audit organization to report to a legislative body or other independent governing body on a recurring basis,

f. statutory protections that give the audit organization sole authority over the selection, retention, and dismissal of its staff, and

g. statutory access to records and documents that relate to the agency, program, or function being audited.

.19 If the head of the audit organization concludes that the organization has all the safeguards listed above, the audit organization may be considered free from organizational impairments to independence when reporting externally. The

audit organization should document the statutory provisions in place that provide these safeguards. The external quality assurance reviewer will review these provisions to determine whether the necessary safeguards are present.

.20 When using the work of other auditors who meet these requirements, the auditor should request a representation letter (see paragraph 650.14) from the head of the audit organization. The auditor should review the above documentation and discuss it with the head of the audit organization. He or she also may discuss the matter with the external quality assurance reviewer, legal counsel for the audit organization, and his or her own legal counsel.

.21 If the auditor decides that the government audit organization is not organizationally independent to report externally (either because it does not meet the criteria in GAGAS or for another reason), the auditor should determine whether the other auditors are organizationally independent to report internally. These auditors are internal auditors. The Institute of Internal Auditors' (IIA) *International Standards for the Professional Practice of Internal Auditing* defines internal auditing as "an independent, objective assurance and consulting activity designed to add value and improve an organization's operations. It helps an organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes." GAGAS contain guidance on organizational independence for government internal auditors. For example, internal auditors should be outside the staff or line management function of the unit under audit. They should report their results and be accountable to the head or deputy of their agency. IIA standards require internal auditors to be objective for the activities they audit. These GAGAS and IIA standards of independence for internal auditors differ from independence under the AICPA Code of Professional Conduct or independence for external auditors under GAGAS. The auditor generally should determine whether the internal auditors whose work is to be used are independent of the activities they audit. The auditor also should consider the organizational status of the head of the audit organization. For the audit organization to be considered free from organizational impairments to report internally to management, the head of the audit organization (GAGAS, chapter 3) should meet **all** of the following criteria:

a. accountable to the head or deputy head of the government entity,

b. required to report the results of the audit organization's work to the head or deputy head of the government entity, and

c. located organizationally outside the staff or line management function of the unit under audit.

[Subsequent sections of FAM 650, beginning at paragraph .22, remain unchanged.}

660 C - AGREED-UPON PROCEDURES COMPLETION CHECKLIST

Entity:_____

Job code:_____

Principal report:_____

.01 This checklist is a tool to help auditors comply with the requirements for agreed-upon procedures engagements. No specific signatures are required on the checklist in the planning phase.

.02 Several of the last questions include steps in GAO's quality control process, including the GAO Audit Documentation Set, second partner review, and review by the Technical Accounting and Auditing Expert (Chief Accountant at GAO) when that person is not the second partner. GAO auditors should complete these questions and forms. IG auditors and other auditors may use these questions and forms or may substitute questions and forms that consider their reporting style and quality control.

Step	N/A	Yes	No	Ref.
1. Has the audit team documented an understanding with the individuals requesting the audit and officials of the entity?				
2. Does the documentation cover the following? • The nature of the engagement. • Identification of the subject matter, the responsible entity, and the criteria. • Identification of the users of the report. • Auditor's responsibilities. • Reference to GAGAS and the attestation standards. • Agreement on the nature, timing, and extent of procedures. • Anticipated reporting, including disclaimers. • Any involvement of a specialist. • Materiality limits.				

Step	N/A	Yes	No	Ref.
3. Was an entrance conference held with the responsible entity?				
4. Has the auditor determined whether a letter of representation from the responsible entity is necessary? (Note: This is not a requirement.)				
5. Were applicable laws and regulations documented if part of the procedures?				
6. Were review responsibilities communicated to individuals on the assignment?				
7. Does the documentation contain the following? a. The scope and methodology, including any sampling criteria used and consideration of the results of any previous agreed-upon procedures and follow up on any known significant findings that directly relate to the agreed-upon procedures engagement. b. Any indication of fraud, illegal acts, violations of provisions of contracts or grant agreements, or abuse, and—if there was such indication—the directed procedures performed, results obtained, and related communications. c. Descriptions of transactions and records examined. d. Documentation of the work performed to support reported results. e. Evidence of supervisory review.				

Step	N/A	Yes	No	Ref.
8. Does the documentation record that the applicable standards were followed (AT 101, AT 201, and GAGAS, chapter 6)?				
9. Does the documentation record a reasonable basis for the results of the agreed-upon procedures?				
10. Does the summary memorandum summarize the results of the procedures and refer to the documentation?				
11. Were any deviations from the standard reporting elements documented and the basis approved by the assistant director with copies of the documentation sent to the audit director and Reviewer (AT 201.31)?				
12. Was the report referenced?				

Step	N/A	Yes	No	Ref.
13. Did the assistant director review the following? a. Documentation of the understanding with the individuals requesting the audit and officials of the entity. b. Memorandum of entrance conference with the responsible entity. c. Completed work programs. d. Memorandums on key engagement issues. e. Summary of the results of the procedures. f. Memorandum of exit conference with the responsible entity. g. Deviations from standard reporting language. h. Financial schedules/statements. i. Agreed-upon procedures report. j. GAO Audit Documentation Set (or equivalent).				

Step	N/A	Yes	No	Ref.
14. Did the audit director review the following? a. Documentation of the understanding with the individuals requesting the audit and officials of the entity. b. Summary of results of the procedures. c. Memorandum of exit conference with responsible entity. d. Deviations from standard reporting language. e. Agreed-upon procedures report. f. GAO Audit Documentation Set (or equivalent).				
15. Did the assistant director or the auditor in charge determine that all significant review notes were resolved appropriately?				
16. Did the assistant director initial all documentation bundle covers to indicate that all documentation was sufficiently reviewed?				
17. Is the report appropriate as to the following? a. Wording. b. Scope of work. c. GAGAS. d. Explanatory paragraphs.				

Step	N/A	Yes	No	Ref.
18. Was the report reviewed by the following? a. Office of the General Counsel. b. Technical Accounting and Auditing Expert. c. Second partner (or equivalent), if not Technical Accounting and Auditing Expert.				
19. Is the agreed-upon procedures report dated appropriately or does the report indicate when the auditor completed fieldwork? (AT 201)				

Note: All "No" answers should be discussed in attached documentation. If the reason that a question is "Not Applicable" is not obvious, the auditor should document the reason on the checklist or in an attachment.

Date of completion of fieldwork _____

Audit Manager _____ Date _____

Assistant Director _____ Date _____

Audit Director _____ Date _____

SECOND PARTNER'S (OR EQUIVALENT) CONCURRENCE ON AGREED-UPON PROCEDURES WORK

Objective of second partner (or equivalent) review: To objectively review significant engagement matters to conclude, based on all facts the second partner (or equivalent) has knowledge of, that no matters were found that caused the second partner (or equivalent) to believe that (1) the procedures were not performed in accordance with GAGAS, which incorporate financial audit and attestation standards established by the American Institute of Certified Public Accountants (AICPA), and (2) the report does not meet professional standards and audit organization policies.

Procedures: Before the report was issued, I performed the following procedures:

- as necessary, discussed significant engagement issues with the audit director;
- read documentation of key decisions and consultations;
- read the agreed-upon procedures report; and
- confirmed with the audit director that there are no unresolved issues.

Conclusions: Based on all the relevant facts of which I have knowledge, I found no matters that caused me to believe that (1) the agreed-upon procedures were not performed in accordance with GAGAS and the AICPA's attestation standards related to agreed-upon procedures engagements and (2) the report is not in accordance with professional standards and audit organization policies.

In signing this form, I acknowledge that there have been no personal or external impairments to independence regarding my work on this engagement.

Title	**Signature**	**Date**

TECHNICAL ACCOUNTING AND AUDITING EXPERT'S CONCURRENCE ON AGREED-UPON PROCEDURES WORK

Objective of review: When the Technical Accounting and Auditing Expert is not the second partner (or equivalent), the Technical Accounting and Auditing Expert should read the report. The Technical Accounting and Auditing Expert should then sign the conclusions below.

Conclusions: Based on my reading of the report, I found no matters that caused me to believe that (1) the agreed-upon procedures were not performed in accordance with GAGAS and the AICPA's attestation standards related to agreed-upon procedures engagements and (2) the report is not in accordance with professional standards and audit organization policies.

In signing this form, I acknowledge that there have been no personal or external impairments to independence regarding my work on this engagement.

_____

Title **Signature** **Date**

1001 – MANAGEMENT REPRESENTATIONS

.01 This section deals with the management representations that the auditor is required to obtain from current management as part of the audit, as described in sections 280 and 550. It covers the four general areas of representations: representations about the financial statements, internal control, financial management systems' substantial compliance with the requirements of the Federal Financial Management Improvement Act of 1996 (FFMIA), and compliance with laws and regulations. In the AICPA standards, these representations are discussed in sections AU 333, AT 501, and AU 801. OMB audit guidance also contains guidance on management representations letters.

.02 Written representations from management ordinarily confirm oral representations given to the auditor, indicate and document the continuing appropriateness of those representations, and reduce the possibility of misunderstanding. Management representations are not a substitute for audit procedures. If a representation is contradicted by other audit evidence, the auditor should investigate the circumstances and consider the reliability of the representation. Also, the auditor should then consider whether it is appropriate to rely on other management representations. Management's refusal to furnish written representations is a scope limitation sufficient to preclude an unqualified opinion.

.03 The specific representations obtained will depend on the circumstances of the engagement and the nature and basis of presentation of the financial statements. These representations apply to all the financial statements and all periods covered by the audit report. In addition to the representations given in the AICPA standards, the auditor generally should consider the need to obtain representations on other matters based on the circumstances of the audited entity. Also, the representations given in the example representation letter in section 1001 A should be deleted if inapplicable or customized to the situation of the entity being audited.

.04 The management representation letter should be obtained from the highest level of the audited entity. The officials who sign the management representation letter should be those who, in the auditor's view, are responsible for and knowledgeable, directly or through others, about the matters in the representation letter. These officials generally should be the head of the entity and the CFO, or equivalent. Additional management representation letters should be obtained from any component units for which separate reports are to be issued.

.05 The management representation letter should be on the audited entity's letterhead. The representations should be as of a date no earlier than the date of

the auditor's report—the end of fieldwork. To ensure the letter is ready in time, a draft letter generally should be provided to and discussed with management early in the audit and updated for circumstances found throughout the audit. Where management signs the letter after the end of fieldwork, the letter should state that the representations are as of the date of the audit report. If management signs the letter before the end of fieldwork, the auditor generally should obtain a separate letter to update the representations to the end of fieldwork. However, where the time difference is short, the auditor may update the representations orally and document the update.

.06 Although the management representation letter generally should be addressed to the Comptroller General (at GAO) or the agency IG (and also to the independent external auditor, when appropriate), the audit team should consider having the entity deliver it directly to a member of the team to avoid any delays in receiving the letter.

.07 Especially for large audited entities, management may need to specify a materiality threshold in the management representation letter, below which items would not be considered exceptions. The auditor should be satisfied that such a materiality threshold is so far below design materiality that even many items below this level would not, in the aggregate, approach design materiality. For example, a threshold that is 5 percent (or less) of design materiality may be sufficiently low. The materiality level may be different for different representations and would not apply to those representations not directly related to amounts in the financial statements (such as responsibility for the statements).

REPRESENTATIONS RELATING TO THE FINANCIAL STATEMENTS

.08 Paragraph AU 333.06 lists management representations that are ordinarily included in a GAAS audit if applicable. These generally relate to management acknowledging its responsibility for the financial statements and its belief that the financial statements are fairly presented in conformity with U.S. generally accepted accounting principles; completeness of financial information; recognition, measurement, and disclosure; and subsequent events. Examples of additional representations that may be appropriate depending on an entity's business or industry are given in appendix B to AU 333. The auditor may review section AU 333 for items that could be added to the representations, many of which would have to be modified in the federal government environment. (OMB has added a representation dealing with intragovernmental transactions and their reconciliations for intragovernmental transactions and their reconciliations for agencies and components that are covered under the OMB audit requirements for federal agencies.)

.09 Appendix B of AU 333 gives example language for the following situations (note: tailor for the circumstances applicable to the federal audit entity, as appropriate):

General
- Unaudited interim information accompanies the financial statements.
- The impact of a new accounting principle is not known.
- There is justification for a change in accounting principles.
- Financial circumstances are strained, with disclosure of management's intentions and the entity's ability to continue as a going concern.
- The possibility exists that the value of specific significant long-lived assets or certain identifiable intangibles may be impaired.
- The entity engages in transactions with special purpose entities.
- The work of a specialist has been used by the entity.

Cash
- Disclosure is required of compensating balances or other arrangements involving restrictions on cash balances, line of credit, or similar arrangements.

Financial instruments
- The value of debt or equity securities has declined.
- Management has determined the fair value of significant financial instruments that do not have readily determinable market values.
- There are financial instruments with off-balance-sheet risk and financial instruments with concentrations of credit risk.

Receivables
- Receivables have been properly stated in the financial statements (for example, at estimated net realizable value).

Inventories
- Excess or obsolete inventories exist.

Deferred charges
- Material expenditures have been deferred.

Debt
- Short-term debt could be refinanced on a long-term basis, and management intends to do so.

Contingencies
- Estimates and disclosures have been made of environmental remediation liabilities and related loss contingencies.
- Agreements may exist to repurchase assets previously sold.

Pension and postretirement benefits

- An actuary has been used to measure pension liabilities and costs.
- There is involvement with a multiemployer plan.
- Postretirement benefits have been eliminated.
- Employee layoffs that would otherwise lead to a curtailment of a benefit plan are intended to be temporary.
- Management intends to either continue to make or not make frequent amendments to its pension or other postretirement benefit plans, which may affect the amortization period of prior service cost, or management has expressed a substantive commitment to increase benefit obligations.

Sales

- There may be losses from sales commitments.
- There may be losses from purchase commitments.
- Nature of the product or industry indicates the possibility of undisclosed sales terms.

.10 The auditor generally should consider the need for additional customizing of the example representation letter given in section 1001 A and for the additional representations in paragraph 1001.09. Many of the representations may have to be qualified, especially in an initial audit or in later audits where significant problems remain. For instance, where the example representation letter states that there are no violations of laws or regulations, the entity may need to add at the end of the statement, "except as follows:" and describe the violations.

.11 In addition, the auditor generally should consider whether circumstances may require that additional descriptive items be included in the representation letter, especially as support for conclusions the auditor makes in the audit. This is important where the corroborating information that can be obtained by procedures other than inquiry is limited. For example, the letter should include descriptions of (1) the reasons for audited-entity-imposed scope limitations, such as lack of availability of certain records, (2) the basis for material liability estimates, key asset valuations, or the probability of contingencies, and (3) significant plans or intentions for the entity. For example, if the entity has a pension plan outside of the Civil Service Retirement System or the Federal Employees' Retirement System, an item should state that the entity does not plan to terminate the plan and that management believes the actuarial assumptions and methods used to measure pension liabilities and costs for financial reporting purposes are appropriate in the circumstances.

REPRESENTATIONS RELATING TO INTERNAL CONTROL

.12 Internal control representations, when the auditor opines on internal control, are found in AT 501.44 and, for those related to fraud, in AU 316. These representations, where applicable, relate to management's (1) acknowledging its responsibility for internal control, (2) stating that management has assessed the effectiveness of its internal control and specifying the control criteria used, (3) stating management's assertion about the effectiveness of its internal control based on the control criteria, (4) stating that management has disclosed to the auditor all significant deficiencies in the design or operation of internal control that could adversely affect the entity's ability to meet the internal control objectives and pointing out those that are material weaknesses (using the definition in the representation letter, which is the definition in AU 325), (5) stating whether there were any changes to internal control subsequent to the end of the reporting period, (6) acknowledging its responsibility for the design and implementation of programs and controls to prevent and detect fraud, (7) knowledge of any fraud or suspected fraud affecting the entity involving management, employees who have significant roles in internal control, or others where the fraud could have a material effect on the financial statements, and (8) knowledge of any allegations of fraud or suspected fraud affecting the entity received in communications from employees, former employees, analysts, regulators, or others.

.13 For items 2 and 3, entities may use criteria established under FMFIA and OMB Circular A-123 in their FMFIA internal control assessment. Standards in GAO's green book *Standards for Internal Control in the Federal Government* were established as standards for federal entities to follow. The November 1999 update to these standards (GAO/AIMD-00-21.3.1) incorporates concepts from the private sector guidance *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations (COSO) of the Treadway Commission. Entities should summarize in the representation letter any material weaknesses relating to financial reporting (including safeguarding), compliance (including budget), and performance measures controls. Example wording for the representations is given in section 1001 A for the case where management asserts that its internal control as of the date of the financial statements provided reasonable assurance that misstatements, losses, or noncompliance material in relation to the financial statements or required supplementary stewardship information would be prevented or detected on a timely basis. If there are material weaknesses, management should include a brief description of them in its representation letter and modify its assertion accordingly.

REPRESENTATIONS RELATING TO FINANCIAL MANAGEMENT SYSTEMS' SUBSTANTIAL COMPLIANCE WITH FFMIA REQUIREMENTS

.14 FFMIA requires the auditor who audits a CFO Act agency to report whether the entity's financial management systems substantially comply with (1) federal financial management systems requirements, (2) applicable federal accounting standards (U.S. generally accepted accounting principles), and (3) the SGL at the transaction level. In order to report in accordance with FFMIA, the auditor should obtain representations from management as to the entity's systems' substantial compliance with these requirements.

.15 The auditor should obtain representations that management takes responsibility for having its systems substantially comply with the FFMIA requirements, stating that it has assessed the systems' compliance, stating the criteria used, and asserting the systems' substantial compliance (or lack thereof). The criteria should be the requirements in OMB Circular A-127, Financial Management Systems (which incorporates the SGL, the JFMIP Federal Financial Management Systems Requirements documents, and other OMB circulars). These requirements are further described, including indicators of substantial compliance, in OMB's FFMIA implementation guidance for CFOs and IGs, referenced in OMB's audit guidance.

REPRESENTATIONS RELATING TO COMPLIANCE WITH LAWS AND REGULATIONS

.16 AU 801.07 suggests that a representation relating to compliance with laws and regulations state that management has identified and disclosed to the auditor all laws and regulations that have a direct and material effect on the financial statements.

.17 In addition, AT 601 deals with compliance attestation. The auditor is not required to follow AT 601 because it does not apply to an audit of financial statements. However, in situations in which the auditor believes additional representations regarding compliance may be needed, examples are given in AT 601.68.

EFFECT OF CHANGE IN MANAGEMENT ON REPRESENTATION LETTER

.18 Sometimes management is reluctant to sign representations for periods when it did not manage the entity. The auditor should explain to management that by issuing the financial statements, it is making the assertions implicit in the financial statements. Management may wish to understand the transactions and controls

supporting the financial statements, and the auditor should help it do so. Where a change in management is expected, the auditor may advise the new management to obtain representations from the old management about the period prior to the change.

1001 A EXAMPLE MANAGEMENT REPRESENTATION LETTER

[Entity Letterhead]

[Date of auditor's report and completion of fieldwork]

The Honorable [name of Inspector General or Comptroller General]
[Inspector or Comptroller] General [of the United States]
[Name of agency] [or U.S. General Accounting Office]
Washington, D.C.

[Also, include the independent external auditor as an addressee, when appropriate.]

Dear [name(s)]:

This letter is in connection with your audits of the [entity's] balance sheet as of September 30, 20X2 and 20X1, [or dates of audited financial statements] and the related statements of net costs, changes in net position, budgetary resources, financing, and custodial activity [if applicable], for the years then ended for the purposes of (1) expressing an opinion as to whether the financial statements are presented fairly, in all material respects, in conformity with U.S. generally accepted accounting principles, (2) reporting [or expressing an opinion] on the entity's internal control as of September 30, 20X2 [or date of latest audited financial statements], (3) reporting whether the [entity's] financial management systems substantially comply with federal financial management systems requirements, applicable federal accounting standards (U.S. generally accepted accounting principles), and the U.S. Government Standard General Ledger at the transaction level as of September 30, 20X2, and (4) testing for compliance with applicable laws and regulations.

Certain representations in this letter are described as being limited to matters that are material. For purposes of this letter, matters are considered material if they involve $X or more. Items also are considered material, regardless of size, if they involve 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 be changed or influenced by the omission or misstatement.

We confirm, to the best of our knowledge and belief, the following representations made to you during the audits (these representations are as of [date of completion of fieldwork], pertain to both years' financial statements, and update the representations we provided in the prior year):

1. We are responsible for the fair presentation of the financial statements and stewardship information in conformity with U.S. generally accepted accounting principles.

2. The financial statements are fairly presented in conformity with U.S. generally accepted accounting principles.

3. We have made available to you all

   a. financial records and related data;

   b. where applicable, minutes of meetings of the Board of Directors [or other similar bodies, such as congressional oversight committees] or summaries of actions of recent meetings for which minutes have not been prepared; and

   c. communications from the Office of Management and Budget (OMB) concerning noncompliance with or deficiencies in financial reporting practices.

4. There are no material transactions that have not been properly recorded in the accounting records underlying the financial statements or disclosed in the notes to the financial statements.

5. We believe that the effects of the uncorrected financial statement misstatements summarized in the accompanying schedule are immaterial, both individually and in the aggregate, to the financial statements taken as a whole. [An example accompanying schedule is included in section 595 C.] [If management believes that certain of the identified items are not misstatements, management's belief may be acknowledged by adding to the representation, for example, "We believe that items XX and XX do not constitute misstatements because [description of reason]."]

6. The [entity] has satisfactory title to all owned assets, including stewardship property, plant, and equipment; such assets have no liens or encumbrances; and no assets have been pledged.

7. We have no plans or intentions that may materially affect the carrying value or classification of assets and liabilities.

8. Guarantees under which the [entity] is contingently liable have been properly reported or disclosed.

9. Related party transactions and related accounts receivable or payable, including assessments, loans, and guarantees, have been properly recorded and disclosed.

10. All intraentity transactions and balances have been appropriately identified and eliminated for financial reporting purposes, unless otherwise noted. All intragovernmental transactions and balances have been appropriately recorded, reported, and disclosed. We have reconciled intragovernmental transactions and balances with the appropriate trading partners for the four fiduciary transactions identified in Treasury's *Intra-governmental Fiduciary Transactions Accounting Guide*, and other intragovernmental asset, liability, and revenue amounts as required by the applicable OMB Bulletin.

11. There are no

    a. possible violations of laws or regulations whose effects should be considered for disclosure in the financial statements or as a basis for recording a loss contingency,

    b. material liabilities or gain or loss contingencies that are required to be accrued or disclosed that have not been accrued or disclosed, or

    c. unasserted claims or assessments that are probable of assertion and must be disclosed that have not been disclosed.

12. We have complied with all aspects of contractual agreements that would have a material effect on the financial statements in the event of noncompliance.

13. No material events or transactions have occurred subsequent to September 30, 20X2 [or date of latest audited financial statements], that have not been properly recorded in the financial statements and stewardship information or disclosed in the notes.

14. We are responsible for establishing and maintaining internal control.

15. We acknowledge our responsibility for the design and implementation of programs and controls to prevent and detect fraud (intentional misstatements or omissions of amounts or disclosures in financial statements and misappropriation of assets that could have a material effect on the financial statements).

16. We have no knowledge of any fraud or suspected fraud affecting the [entity] involving:
    a. management,
    b. employees who have significant roles in internal control, or
    c. others where the fraud could have a material effect on the financial statements.

    [If there is knowledge of any such instances, they should be described.]

17. We have no knowledge of any allegations of fraud or suspected fraud affecting the [entity] received in communications from employees, former employees, or others. [If there is knowledge of any such allegations, they should be described.]

18. Pursuant to 31 U.S.C. 3512(c), (d) (commonly known as the Federal Managers' Financial Integrity Act), we have assessed the effectiveness of the [entity's] internal control in achieving the following objectives:

    a. reliability of financial reporting—transactions are properly recorded, processed, and summarized to permit the preparation of financial statements and stewardship information in accordance with U.S. generally accepted accounting principles, and assets are safeguarded against loss from unauthorized acquisition, use or disposition;

    b. compliance with applicable laws and regulations—transactions are executed in accordance with (i) laws governing the use of budget authority and with other laws and regulations that could have a direct and material effect on the financial statements and (ii) any other laws, regulations, and governmentwide policies identified by OMB in its audit guidance; and

    c. reliability of performance reporting—transactions and other data that support reported performance measures are properly recorded, processed, and summarized to permit the preparation of performance information in accordance with criteria stated by management.

    [This item is not required if the auditor is not opining on internal control. Also, if the entity bases its internal control assessment on suitable criteria

other than 31 U.S.C. 3512(c), (d), this item should cite the criteria used (for example, *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations (COSO) of the Treadway Commission).]

19. Those controls in place on September 30, 20X2 [or date of latest audited financial statements], and during the years ended 20X2 and 20X1, provided reasonable assurance that the foregoing objectives are met. [This item is not required if the auditor is not opining on internal control.]

    [If there are material weaknesses, the foregoing representation should be modified to read:

    > Those controls in place on September 30, 20X2, and during the years ended 20X2 and 20X1, provided reasonable assurance that the foregoing objectives are met except for the effects of the material weaknesses discussed below or in the attachment.
    >
    > or: Internal controls are not effective.
    >
    > or: Internal controls do not meet the foregoing objectives.]

20. We have disclosed to you all significant deficiencies in the design or operation of internal control that could adversely affect the entity's ability to meet the internal control objectives and identified those we believe to be material weaknesses. [This item is not required if the auditor is not opining on internal control.]

21. There have been no changes to internal control subsequent to September 30, 20X2 [or date of latest audited financial statements], or other factors that might significantly affect it. [If there were changes, describe them, including any corrective actions taken with regard to any significant deficiencies or material weaknesses.] [This item is not required if the auditor is not opining on internal control.]

22. We are responsible for implementing and maintaining financial management systems that substantially comply with federal financial management systems requirements, federal accounting standards (U.S. generally accepted accounting principles), and the U.S. Government Standard General Ledger at the transaction level. [This item is not required if the entity is not subject to the Federal Financial Management Improvement Act of 1996.]

23. We have assessed the financial management systems to determine whether they substantially comply with these federal financial management systems requirements. Our assessment was based on guidance issued by OMB. [This item is not required if the entity is not subject to the Federal Financial Management Improvement Act of 1996.]

24. The financial management systems substantially complied with federal financial management systems requirements, federal accounting standards, and the U.S. Government Standard General Ledger at the transaction level as of [date of the latest financial statements]. [This item is not required if the entity is not subject to the Federal Financial Management Improvement Act of 1996.]

    [If the financial management systems substantially comply with only one or two of the above elements, this representation should be modified as follows:

    As of [date of financial statements], the [entity's] financial management systems substantially comply with [specify which of the three elements for which there is substantial compliance (e.g., federal accounting standards and the SGL at the transaction level)], but did not substantially comply with [specify which of the elements for which there was a lack of substantial compliance (e.g., federal financial management systems requirements)], as described below (or in an attachment).]

    [If the financial management systems do not substantially comply with any of thee three elements, the following paragraph should be used instead:

    As of [date of financial statements], the [entity's] financial management systems do not substantially comply with the federal financial management systems requirements.]

    [If there is a lack of substantial compliance with one or more of the three requirements, identify herein or in an attachment all the facts pertaining to the noncompliance, including the nature and extent of the noncompliance and the primary reason or cause of the noncompliance.]

25. We are responsible for the [entity's] compliance with applicable laws and regulations.

26. We have identified and disclosed to you all laws and regulations that have a direct and material effect on the determination of financial statement amounts.

27. We have disclosed to you all known instances of noncompliance with laws and regulations.

_____
[Name of Head of Entity]
[Title]

_____
[Name of Chief Financial Officer]
[Title]

1003 - FINANCIAL STATEMENT AUDIT COMPLETION CHECKLIST

Entity: _____

Job Code: _____

Principal Report: _____

_____

Other Reports (including management letters and testimonies): _____

_____

INSTRUCTIONS

.01 This checklist is a tool to help auditors of financial statements conform with U.S. generally accepted government auditing standards (GAGAS), OMB audit guidance, and provisions of the FAM. This checklist should be completed before the report is issued and should be prepared by the audit manager and reviewed by the assistant director and audit director. If the audit is conducted at multiple sites, the site supervisor may complete parts of the checklist for each site (with the audit manager completing an overall checklist). While parts of the checklist are useful in audit planning, no specific signatures are required on the checklist in the planning phase.

.02 The detailed questions in this checklist are to be answered “no,” "N/A" (not applicable), or “yes.” For some questions, “no” answers might indicate departures from professional standards or from policies. The auditor should explain all “no” answers at the end of this checklist and should consider the effects and significance of “no” answers, including any effect on the auditor’s report. Check “N/A” when the item does not exist or when the item exists but is judged to be not material. Because the checklist is designed for the wide range of financial statement audits, there sometimes might be many "N/A" answers. If the reason why a question is not applicable is not obvious, the auditor should document the reason on the checklist or in an attachment. It is not necessary to create additional documentation to support the “yes” answers, but a column is provided to insert a reference to related documentation ("ref."). The questions are summarized; for most questions, there is a reference to professional literature that provides more detail.

.03 Section V has questions on GAO's report considerations; section VI has questions on GAO's quality control. GAO auditors should complete these sections. IG auditors and other auditors may use these sections or may substitute forms that consider their reporting style and quality controls.

.04 See section 650 related to reviewing this checklist (or equivalent) when using the work of others.

.05 The FAM includes a separate "Checklist for Federal Accounting, Reporting, and Disclosures" (section 1050) that covers accounting, financial reporting, and disclosure requirements related to financial statements prepared using U.S. generally accepted accounting principles promulgated by FASAB. The AICPA has published a disclosure checklist for requirements related to financial statements prepared using U.S. generally accepted accounting principles promulgated by FASB. The auditor should prepare (or review, if prepared by the entity) either the Checklist for Federal Accounting, Reporting, and Disclosures or the AICPA disclosure checklist, as applicable, or an equivalent checklist that addresses the applicable accounting, financial reporting, and disclosure requirements. These checklists may be tailored for the needs of the individual agency financial statements.

.06 GAO auditors should prepare the "GAO Audit Documentation Set" that provides guidance on documentation. IG and other auditors may develop similar tools.

.07 For GAO's financial audits, a second partner review should be performed and the Chief Accountant should read the report. These reviews by the second partner and/or Chief Accountant are documented on the last two pages of this checklist. IG auditors and other auditors should consider the need for similar reviews.

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References:

AICPA *Professional Standards* (vol. 1) ..... AU

GAO/PCIE *Financial Audit Manual* ..... FAM

Government Auditing Standards ..... GAGAS

Section I: Planning and Concluding the Audit	N/A	Yes	No*	Ref.
1. Has the audit team documented that it has established an understanding with the individuals requesting the audit and officials of the entity as to the objectives of the work; management's responsibilities; auditors' responsibilities; the nature, timing, and extent of planned testing and reporting; the planned level of assurance; and any limitations of the work? (FAM 280 and GAGAS, par. 4.06)	___	___	___	___
2. Were entrance conferences held?	___	___	___	___
3. Does the entity profile (or equivalent) document an understanding of the entity sufficient to plan the audit? (FAM 290.03)	___	___	___	___
4. Does the documentation contain an adequate general risk analysis or the equivalent? (FAM 290.04)	___	___	___	___
5. Did the audit team adequately perform and document the following planning steps? (FAM 290.04)				
a. Perform preliminary analytical procedures (FAM 225)	___	___	___	___
b. Determine planning, design, and test materiality (FAM 230)	___	___	___	___
c. Identify significant laws and regulations (FAM 245)	___	___	___	___
d. Identify relevant budget restrictions (FAM 250)	___	___	___	___
e. Understand the budget formulation process (FAM 260.51)	___	___	___	___

(continued on next page)

Section I: Planning and Concluding the Audit	N/A	Yes	No*	Ref.
5. (continued)				
f. Assess inherent risk and the overall effectiveness of the control environment, risk assessment, communication, and monitoring, including whether weaknesses in the control environment, risk assessment, communication, and monitoring preclude the effectiveness of specific control activities (FAM 260)	___	___	___	___
g. Conduct brainstorming meeting(s), obtain information to identify fraud risks, and identify and assess fraud risks (FAM 260)	___	___	___	___
h. Respond to fraud risks, including any related to revenue and to management override of controls, and exercise professional skepticism throughout the audit (FAM 260)	___	___	___	___
i. Design the audit to achieve an acceptable level of audit assurance that the financial statements are not materially misstated (GAO uses 95 percent) (FAM 260.04)	___	___	___	___
j. Consider the effects of information technology, including service centers (FAM 220, 260.17, 260.41-42, and 270)	___	___	___	___
k. Assess the FMFIA process (FAM 260.43)	___	___	___	___
l. Consider operations controls to be tested (FAM 275)	___	___	___	___
m. Understand performance measures controls (FAM 275)	___	___	___	___
n. Plan other procedures (representation letters, related party transactions, sensitive payments) (FAM 280)	___	___	___	___
(continued on next page)				

Section I: Planning and Concluding the Audit	N/A	Yes	No*	Ref.
5. (continued)				
o. Consider locations to be visited (FAM 285)	___	___	___	___
p. Plan procedures to test whether the entity's financial management systems substantially comply with the requirements of FFMIA (FAM 350.02)	___	___	___	___
q. Consider staffing requirements	___	___	___	___
r. Consider timing of procedures and milestones (FAM 295 D)	___	___	___	___
s. Consider assistance from entity personnel	___	___	___	___
6. Does the general risk analysis or the equivalent reflect appropriate consideration of findings and recommendations from previous audits that could affect the current audit objectives? (GAGAS, par. 4.14)	___	___	___	___
7. Did the audit team identify budget controls for each relevant budget restriction and perform sufficient work to support the conclusions on internal control? (FAM 250, 310.05, 330.09)	___	___	___	___
8. Did the audit team identify compliance controls and perform sufficient work to support the conclusions on internal control? (FAM 245, 310.05, 330.09)	___	___	___	___
9. If the audit team used the work of others (CPA firms, IGs, internal auditors, or specialists), did the audit team meet the requirements of FAM 650?	___	___	___	___

Section I: Planning and Concluding the Audit	N/A	Yes	No*	Ref.
10. Did the audit team perform overall analytical procedures, including documentation of the following?				
a. Expectations	___	___	___	___
b. Data/sources	___	___	___	___
c. Parameters	___	___	___	___
d. Explanations/corroboration	___	___	___	___
e. Conclusions (FAM 590.04)	___	___	___	___
11. Does the documentation indicate that the audit team properly performed the following procedures in the reporting phase of the audit? (FAM 590.01)				
a. Evaluate misstatements, including considering whether any misstatements are indicative of fraud (FAM 540)	___	___	___	___
b. Bring all misstatements to the attention of entity management (FAM 540.07)	___	___	___	___
c Obtain attorneys' representations (FAM 550.02)	___	___	___	___
d. Review subsequent events (FAM 550.04 and 1005)	___	___	___	___
e. Obtain management representations (FAM 550.08 and 1001)	___	___	___	___
f. Identify and test related party transactions (FAM 550.12 and 1006)	___	___	___	___
g. Review the consistency of other information accompanying the financial statements (FAM 580.76)	___	___	___	___

Section I: Planning and Concluding the Audit	N/A	Yes	No*	Ref.
12. Does the audit summary memorandum or equivalent properly summarize or refer to documentation addressing the following? (FAM 590.02-.03)				
a. Changes from original risk assessments	___	___	___	___
b. Additional fraud risks or other conditions identified during the audit calling for an additional response and the additional response	___	___	___	___
c. The basis for conclusions on significant auditing, accounting, and reporting issues	___	___	___	___
d. Conclusions on adequacy of procedures	___	___	___	___
e. Unadjusted misstatements	___	___	___	___
f. Conclusions on financial statements	___	___	___	___
g. Conclusions on internal control	___	___	___	___
h. Conclusions on whether the entity's financial management systems meet the requirements of FFMIA	___	___	___	___
i. Conclusions on compliance with laws and regulations	___	___	___	___
j. Conclusions on the consistency of accompanying information with the principal statements	___	___	___	___
13. Has the Audit Director determined that appropriate communications have occurred among the audit team members regarding fraud risks? (FAM 540.19)	___	___	___	___

Section I: Planning and Concluding the Audit	N/A	Yes	No*	Ref.
14. Is there documentation that the following occurred?				
a. Deviations from the "should" procedures in the FAM and the basis therefor were approved by the assistant director with copies of the documentation sent to the audit director and the Reviewer	___	___	___	___
b. Deviations from the "must" procedures in the FAM were approved by the Reviewer (FAM 100.28)	___	___	___	___

Section II: Key Audit Areas	N/A	Yes	No*	Ref.
Answer these questions for each key audit area or cycle. Indicate the key audit areas and cycles to which these questions: _____				
1. Did the audit team prepare the following documentation summarizing considerations in planning and performing the work in the key audit areas and cycles?				
a. Cycle Matrix or an equivalent (or documentation in Account Risk Analysis or an equivalent) showing links between accounts, cycles, applications and line items (FAM 290.05)	___	___	___	___
b. Account Risk Analysis or an equivalent (FAM 290.06)	___	___	___	___
c. Cycle Memorandum and/or flowchart or equivalents (FAM 390.04-.05)	___	___	___	___
d. Specific Control Evaluation or an equivalent (FAM 390.06)	___	___	___	___
e. Written audit program (AU 311.05)	___	___	___	___
2. If conditions changed during the course of the audit, was the audit program modified as appropriate in the circumstances? (AU 311.05)	___	___	___	___

Section II: Key Audit Areas	N/A	Yes	No*	Ref.
3. When the audit team performed sampling, did it properly determine and document the following?				
a. The method used in relation to test objectives	___	___	___	___
b. Sample size and the method of determining it	___	___	___	___
c. Tests performed	___	___	___	___
d. Results (misstatements and deviations found)	___	___	___	___
e. Evaluation (including projection to the population)	___	___	___	___
f. Conclusions (FAM 490.07)	___	___	___	___
4. When the audit team performed substantive analytical procedures, did it properly document the following?				
a. Expectations and the method used to develop them	___	___	___	___
b. Data sources/reliability	___	___	___	___
c. Limit/criteria	___	___	___	___
d. Client explanations and corroborating evidence	___	___	___	___
e. Additional steps needed	___	___	___	___
f. Conclusions (FAM 490.07)	___	___	___	___

Section II: Key Audit Areas	N/A	Yes	No*	Ref.
5. When the audit team performed interim testing, did it do the following?				
a. Test the rollforward period	___	___	___	___
b. Properly document:				
i. The basis for using interim testing	___	___	___	___
ii. The procedures performed	___	___	___	___
iii. The effects of any misstatements found (FAM 495C.06)	___	___	___	___
6. Did the audit team evaluate the reasonableness of significant accounting estimates made by management? (AU 342)	___	___	___	___
7. Were known and likely misstatements identified in the testing of the key area carried forward to the summary of possible adjustments? (FAM 540.04)	___	___	___	___
8. Did an information systems auditor review the specific control evaluation to evaluate the audit team's decision on which controls are computer-related (including controls relating to service-center-produced records)? (FAM 350.10)	___	___	___	___

Section II: Key Audit Areas	N/A	Yes	No*	Ref.
9. Based on the inherent and control risk, did the audit team perform adequate substantive tests of the following? (If not a key area, check the N/A box.)				
Fund Balance with Treasury (FBWT)	___	___	___	___
Consider these issues:				
• Did the audit team test the agency's year-end reconciliation of Fund Balances with Treasury to Treasury account ledgers and trial balance reports (Financial Management Service (FMS) Forms 6653, 6655)?				
• Did the audit team determine whether the auditee did the following?				
a. Researched and resolved differences before making adjustments				
b. Recorded any necessary adjustments in the agency's FBWT accounts				
c. Reported the adjustments to Treasury				
d. Disclosed in the notes to the financial statements material unreconciled differences and budget clearing account differences at year-end, and material unreconciled differences written off by the agency during the year?				
(continued on next page)				

Section II: Key Audit Areas	N/A	Yes	No*	Ref.
Fund Balance with Treasury (continued) • Did the audit team assess (at absolute value) the materiality of unreconciled differences, such as those reported on the Statement of Differences (FMS form 6652) and those included in budget clearing accounts (such as budget accounts F3875, F3878, F3879)? (GAO/AIMD-97-104R)				
Receivables Consider these issues: • Where practical, were accounts receivable confirmed and appropriate follow-up steps taken, including second requests and alternate procedures? (AU 330.30-.31) • If substantive test were performed prior to year-end, was there an adequate review of transactions from the interim date to the balance sheet date? (AU 313.08-.09) • If a significant number and amount of accounts receivable were not confirmed, were other appropriate auditing procedures performed? (AU 330.31-.32)	___	___	___	___

Section II: Key Audit Areas	N/A	Yes	No*	Ref.
Inventories Consider these issues: • Were physical inventories observed at all locations where material amounts were located? (AU 331) • If perpetual inventory records are maintained, does the documentation indicate that differences disclosed by the physical inventory (or cycle counts) are properly reflected in the financial statements? (AU 331) • When the physical inventory is taken at a date other than the balance sheet date (or where rotating procedures are used), did the auditor consider inventory transactions between the inventory date(s) and the balance sheet date? (AU 313.08-.09) • Does the documentation contain evidence that counts were correctly made and recorded (was control over inventory tags or count sheets maintained) and test count quantities were reconciled with the counts reflected in the final inventory? (AU 331.09) (continued on next page)	___	___	___	___

Section II: Key Audit Areas	N/A	Yes	No*	Ref.
Inventories (continued) • Were there adequate tests of the following? a. Clerical accuracy of the inventory b. Costing methods and substantiation of costs used in pricing all elements of the inventory c. Cutoff • Were analytical procedures used to test the overall valuation of inventories?				
Investments Consider these issues: • Was a summary schedule prepared (or obtained) and details tested with respect to the description, purchase price and date, changes during the period, income, market value, etc. of investments? • Were securities either examined or confirmed? (AU 332.04)	___	___	___	___

Section II: Key Audit Areas	N/A	Yes	No*	Ref.
Property, Plant, and Equipment Consider these issues: • Was a summary schedule prepared (or obtained) to show beginning balances, changes during the period, and ending balances for the following? a. Property, plant, and equipment b. Accumulated depreciation • If samples were used to determine opening balances, were the samples appropriate? • Did the audit team perform tests of completeness, such as by testing from disbursements to property records? • Do the tests appear adequate and were proper conclusions drawn?	____	___	___	___
Liabilities Consider these issues: • Did the audit team perform an adequate search for unrecorded liabilities? • Did the audit team consider expenses that might require accrual (e.g., pensions, compensated absences, other postretirement benefits, or postemployment benefits provided to former or inactive employees prior to retirement), and whether accrued expenses were reasonably stated?	___	___	___	___

Section II: Key Audit Areas	N/A	Yes	No*	Ref.
Revenue and Expenses Consider these issues: • Did the audit team compare revenue and expenses for the period to expectations, based on the budget and the results of the preceding period? (AU 329) • Were significant variances and fluctuations from expectations explained? (AU 329) • Did the audit team consider the following? a. The entity's revenue recognition policy b. Unusual transactions c. Fraud risks • Do tests appear adequate and were proper conclusions drawn?	___	___	___	___
Statement of Budgetary Resources Consider these issues: • Were appropriate procedures applied, such as the following? a. Understanding and testing the budget execution controls b. Tests of the process of preparing the statement c. Tests of undelivered orders d. Review of reconciliation to the President's Budget	___	___	___	___

Section III: Consultation	N/A	Yes	No*	Ref.
1. Where warranted by the complexity or unusual nature of an issue (for example, issues where the FAM requires consultation, issues not discussed in FAM or professional standards, going concern issues, economic dependency issues, issues arising after report issuance), was there appropriate consultation with specialists, including the following?				
• The Reviewer (FAM Appendix A)	___	___	___	___
• The Statistician (FAM Appendix A)	___	___	___	___
• The Office of General Counsel (FAM Appendix A)	___	___	___	___
• The Technical Accounting and Auditing Expert? (FAM 100.25)	___	___	___	___
2. Were significant consultations appropriately documented? (FAM 100.24)	___	___	___	___
3. Were the persons consulted made aware of all relevant facts and circumstances?	___	___	___	___

Section IV: Report	N/A	Yes	No*	Ref.
1. Does the auditor's report include the following?				
a. Introduction	___	___	___	___
b. Significant matters (if applicable)	___	___	___	___
c. Conclusions on:				
i. Financial statements	___	___	___	___
ii. Internal control	___	___	___	___
iii. Whether the entity's financial management systems substantially complied with the requirements of the Federal Financial Management Improvement Act of 1996 (FFMIA)	___	___	___	___
iv. Compliance with laws and regulations	___	___	___	___
v. Consistency of other information with financial statements	___	___	___	___
d. Objectives, scope, and methodology, including description of all instances where GAGAS and OMB audit guidance were not followed	___	___	___	___
e. Agency comments (FAM 580.04, 580.81)	___	___	___	___

Section IV: Report	N/A	Yes	No*	Ref.
2. Is the auditor's report appropriate as to the following?				
a. Wording	___	___	___	___
b. Scope of work	___	___	___	___
c. U.S. generally accepted accounting principles	___	___	___	___
d. Explanatory paragraphs	___	___	___	___
e. Opinion on financial statements	___	___	___	___
f. Conclusions on internal control	___	___	___	___
g. Conclusions on whether the entity's financial management systems substantially comply with the requirements of FFMIA	___	___	___	___
h. Reporting on compliance with laws and regulations (FAM 580)	___	___	___	___
3. Is background material (purpose, authority, and functions of programs/activities) limited to what is necessary?	___	___	___	___
4. Is the auditor's report dated in conformity with professional standards? (AU 530, FAM 1601)	___	___	___	___
5. Does the auditor's report cover all periods for which financial statements are presented? (AU 508.65)	___	___	___	___
6. If the financial statements of a prior period are presented and have been audited by a predecessor auditor whose report is not presented, does the auditor's report refer to the predecessor auditor's report? (AU 508.74)	___	___	___	___

Section IV: Report	N/A	Yes	No*	Ref.
7. Does the auditor's report describe the responsibility the auditor is taking for supplementary information, including stewardship information? (AU 551; FAM 580.76-.79)	___	___	___	___
8. a. When illegal acts involve funds received from other governmental entities, did the audit team satisfy itself that the audited entity notified the proper officials of those entities within a reasonable time?	___	___	___	___
b. If the entity did not, or was unable to do so because the top official was involved, did the audit team report these acts to the officials of those other governmental entities? (GAGAS, par. 5.23)	___	___	___	___
9. Does the auditor's report include the following?				
a. Identification of which matters are reportable conditions and which of the reportable conditions are material weaknesses (GAGAS, par. 5.14)	___	___	___	___
b. Reference to a separate letter, if applicable, describing nonreportable conditions (GAGAS, par. 5.16)	___	___	___	___
c. Presentation of all identified (1) instances of fraud and illegal acts unless clearly inconsequential, (2) significant violations of provisions of contracts or grant agreements, and (3) significant abuse (GAGAS, par. 5.12)	___	___	___	___
10. When appropriate, did the audit team report directly to outside parties on fraud, illegal acts, violations of provisions of contracts or grant agreements, or significant abuse? (GAGAS, par. 5.21)	___	___	___	___

Section IV: Report	N/A	Yes	No*	Ref.
11. Did the auditor consider the status of all known significant findings and recommendations from prior audits that affect current audit objectives, including whether any failure to follow up and correct previously identified deficiencies in internal control represent reportable conditions? (GAGAS pars. 4.16, 5.12, and 5.13j.)	___	___	___	___
12. Is a reasonable basis documented for the following?				
a. The opinion about whether the financial statements and disclosures comply in all material respects with U.S. generally accepted accounting principles (FAM 560)	___	___	___	___
b. The conclusions on internal control	___	___	___	___
c. The conclusions on whether the entity's financial management systems substantially comply with the requirements of FFMIA	___	___	___	___
d. The conclusions about compliance with laws and regulations	___	___	___	___
13. Is a reasonable basis documented for reported findings, including the following? (FAM 590.05-.06)				
a. Internal control weaknesses	___	___	___	___
b. Instances of the entity's financial management systems lack of substantial compliance with the requirements of FFMIA	___	___	___	___
c. Instances of noncompliance with laws and regulations	___	___	___	___

Section IV: Report	N/A	Yes	No*	Ref.
14. Do the findings include (where appropriate) the following?				
a. Condition (describe the existing situation)	___	___	___	___
b. Criteria (state what we are comparing to)	___	___	___	___
c. Cause (reflect reason or reasons why the condition and criteria differ)	___	___	___	___
d. Effect (describe the result of the difference between the condition and criteria)	___	___	___	___
15. Are recommendations and suggestions reasonable, doable, and cost-effective?	___	___	___	___
16. Does the presentation of agency comments include the following?				
a. Type of comments obtained (oral, written)	___	___	___	___
b. Title of the most senior official(s) involved	___	___	___	___
c. Accurate characterization of general agreement or disagreement with the report	___	___	___	___
d. Description of the substance of the comments	___	___	___	___
e. Resolution of all substantive comments	___	___	___	___

Section V: GAO's Report Considerations	Yes
1. Overall, does the report have the following characteristics?	
a. Professional (the work reflects an understanding of the issues, an awareness of the external environment, including sensitivity to relevant trends, and a practical approach to what can be done to deal with the problems noted)	_____
b. Accurate (presents information or findings accurately; contains no notable errors in logic or reasoning)	_____
c. Objective (presentation is fair and impartial; tone is constructive and objective)	_____
d. Fact-based (states information and findings completely, includes all necessary facts and/or explanations, distinguishes between fact and unproven or uncorroborated material, and resolves conflicting evidence)	_____
e. Balanced (presents sound and logical evidence to support conclusions, does not use adjectives or adverbs to characterize evidence in a way that implies criticism or conclusions by innuendo, and appropriately recognizes positive aspects of the programs or issues reviewed)	_____
f. Timely and useful (provides relevant and timely information)	_____
g. Clear and concise (presentation is clear, concise, and well organized; message is presented logically; and writing style is adapted to the audience)	_____

Section VI: GAO's Quality Control	N/A	Yes	No*	Ref.
1. Was the report reviewed by the following?				
a. Audit Director	___	___	___	___
b. Office of the General Counsel	___	___	___	___
c. Chief Accountant	___	___	___	___
d. Second Partner	___	___	___	___

Section VI: GAO's Quality Control	N/A	Yes	No*	Ref.
2. Did the audit director review the following? (FAM 1301.17)				
a. General risk analysis or equivalent, including sampling approach	___	___	___	___
b. Account risk analyses or equivalent for material areas with high or moderate combined risk	___	___	___	___
c. Memoranda on key accounting and auditing issues	___	___	___	___
d. Summary memoranda for material areas with high or moderate combined risk	___	___	___	___
e. Management representation letter	___	___	___	___
f. Legal representation letter	___	___	___	___
g. Summary of unadjusted misstatements	___	___	___	___
h. Exit conference summary memorandum	___	___	___	___
i. Audit summary memorandum	___	___	___	___
j. Financial statements	___	___	___	___
k. Referencing/Quality Assurance Review Sheet	___	___	___	___
l. GAO Audit Documentation Set	___	___	___	___

Section VI: GAO's Quality Control	N/A	Yes	No*	Ref.
3. Did the assistant director review the following? (FAM 1301.17)				
a. Entity profile or equivalent	___	___	___	___
b. General risk analysis or equivalent, including sampling approach	___	___	___	___
c. Account risk analyses or equivalent	___	___	___	___
d. Initial audit programs	___	___	___	___
e. Lead schedules	___	___	___	___
f. Completed audit programs	___	___	___	___
g. Memoranda on key accounting and auditing issues	___	___	___	___
h. Summary memoranda	___	___	___	___
i. Checklist for Federal Accounting Reporting, and Disclosures (for statements using GAAP promulgated by FASAB)	___	___	___	___
j. Financial reporting and disclosure checklist (for statements using GAAP promulgated by FASB)	___	___	___	___
k. Management representation letter	___	___	___	___
l. Legal representation letter	___	___	___	___
m. Summary of unadjusted misstatements	___	___	___	___
n. Exit conference memorandum	___	___	___	___
o. Audit summary memorandum	___	___	___	___
(continued on next page)				

Section VI: GAO's Quality Control	N/A	Yes	No*	Ref.
3. (continued)				
p. Financial statements	___	___	___	___
q. Referencing/Quality Assurance Review Sheet	___	___	___	___
r. GAO Audit Documentation Set	___	___	___	___
4. Did the assistant director or audit manager determine that all significant review notes were resolved appropriately? (FAM 1301.28)	___	___	___	___
5. Did an assistant director initial all bundle covers to indicate that all documentation was sufficiently reviewed? (FAM 1301.05)	___	___	___	___
6. Were review notes, superseded versions of documentation , and draft reports (except the referenced draft and the draft sent to the agency for comment), including review notes and superseded versions in electronic form, placed in a separate folder to be retained until the report is issued (unless the audit director decides to retain them until the next audit)? (FAM 1301.28)	___	___	___	___
7. Were review responsibilities communicated to all individuals on the assignment? (FAM 1301.23)	___	___	___	___
8. Was documentation prepared by an information systems auditor reviewed by an information systems auditor for technical content and by a member of the audit team to determine that related audit objectives were achieved? (FAM 1301.24)	___	___	___	___
9. For areas that are both material and have high combined risk, did the audit director or assistant director perform secondary reviews of the documentation? (FAM 1301.12)	___	___	___	___

Section VI: GAO's Quality Control	N/A	Yes	No*	Ref.
10. Was all documentation prepared by the audit director or assistant directors read by audit managers or auditors in charge to determine its consistency with any related documentation? (FAM 1301.15)	___	___	___	___
11. If the documentation indicated a difference of opinion between engagement personnel or between engagement personnel and a specialist or other person consulted, was the difference resolved appropriately and was the basis of the resolution documented? (FAM 1302)	___	___	___	___

Section VII: Explanation of "NO" Answers* and Other Comments

The following pages are provided for comments on all "no" answers* or to expand upon any of the "yes" and "N/A" answers.

* For some questions, "no" answers might indicate departures from professional standards or from policies. The auditor should explain all "no" answers below and should consider the effects and significance of "no" answers, including any effect on the auditor's report.

Page no.	Question no.	Explanatory comments	Disposition of comments

Section VIII: Conclusions: Based on your review and knowledge, do you believe the following?	Yes	No**
1. The audit team performed the engagement, in all material respects, in accordance with U.S. generally accepted government auditing standards (which include U.S. generally accepted auditing standards) and applicable OMB guidance, or the auditor's report was appropriately modified	___	___
2. The financial statements conformed, in all material respects, with U.S. generally accepted accounting principles, or the auditor's report was appropriately modified	___	___
3. The auditor's report was appropriate in the circumstances	___	___
4. The documentation on this engagement supports:		
The auditor's opinion on the financial statements	___	___
The auditor's conclusions on internal control	___	___
The auditor's conclusions on whether the entity's financial management systems substantially comply with the requirements of FFMIA	___	___
The auditor's conclusions on compliance with laws and regulations	___	___
5. The audit team complied, in all material respects, with the audit organization's policies and procedures	___	___

** If any of the above 5 statements have "no" responses, please describe the response in a memorandum to the Reviewer.

Date of completion of fieldwork _____

Audit Manager _____ Date _____

Assistant Director _____ Date _____

Audit Director _____ Date _____

Section IX: Second Partner's Concurrence

Objective of second partner review: To objectively review significant auditing, accounting, and reporting matters and to conclude, based on all facts the second partner has knowledge of, that, except as discussed in the report, no matters were found that caused the second partner to believe that (1) the audit was not performed in accordance with GAGAS and OMB audit guidance (if applicable), (2) the financial statements are not, in all material respects, in conformity with U.S. generally accepted accounting principles, and (3) the report does not meet professional standards and GAO's policies and core values.

Procedures: Before the report was issued, I performed the following procedures.

- Discussed significant auditing, accounting, and reporting issues with the Audit Director;
- Discussed the audit team's identification of high-risk balances and transactions and the audit of those balances and transactions;
- Reviewed documentation on the resolution of significant auditing, accounting, and reporting issues, including documentation of consultation with specialists such as the Chief Accountant, Chief Statistician, and IS professionals;
- Reviewed the summary of unadjusted misstatements;
- Read the audit summary memorandum;
- Read the financial statements and audit report; and
- Confirmed with the Audit Director that there are no unresolved issues.

Conclusion:

Based on all the relevant facts of which I have knowledge, I found no matters, except as discussed in the report, that cause me to believe that (1) the audit was not performed in accordance with GAGAS and OMB audit guidance (if applicable), (2) the financial statements are not, in all material respects, in conformity with U.S. generally accepted accounting principles, and (3) the report is not in accordance with professional standards and GAO's policies and core values.

In signing this form, I acknowledge that there have been no personal or external impairments to independence regarding my work on this engagement.

_____

Second Partner Name and Title Signature Date

Section X: Chief Accountant's Concurrence
When the Chief Accountant is not the second partner, the Chief Accountant should read the report. The Chief Accountant should then sign the conclusion below. Conclusion: Based on my reading of the report, I found no matters, except as discussed in the report, that cause me to believe that (1) the audit was not performed in accordance with GAGAS and OMB audit guidance (if applicable), (2) the financial statements are not, in all material respects, in conformity with U.S. generally accepted accounting principles, and (3) the report is not in accordance with professional standards and GAO policies and core values. In signing this form, I acknowledge that there have been no personal or external impairments to independence regarding my work on this engagement. _____ Chief Accountant's Signature Date