

**GUIDE FOR CONDUCTING EXTERNAL  
QUALITY CONTROL REVIEWS OF THE  
AUDIT OPERATIONS OF OFFICES OF  
INSPECTOR GENERAL**

**FEBRUARY 2002**

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## ACRONYMS

AICPA	American Institute of Certified Public Accountants
AT	Attestation Standards
AU	Codification of Statements on Auditing Standards
CPE	Continuing Professional Education
FIFO	First In, First Out
GAO	General Accounting Office
GAS	Government Auditing Standards
IPA	Independent Public Accountant
OIG	Office of Inspector General
OMB	Office of Management and Budget
PCIE	President's Council on Integrity and Efficiency
SAS	Statements on Auditing Standards
SFFAS	Statements of Federal Financial Accounting Standards

## **PRESIDENT'S COUNCIL ON INTEGRITY AND EFFICIENCY**

### **GUIDE FOR CONDUCTING EXTERNAL QUALITY CONTROL REVIEWS OF THE AUDIT OPERATIONS OF OFFICES OF INSPECTOR GENERAL**

#### PREFACE

This document presents the standards and detailed guidance for conducting external quality control reviews of the audit operations of Offices of Inspector General. This guide was developed to promote consistency in conducting the reviews in accordance with the February 2002 policy statement issued by the Audit Committee (see Appendix I). An external review requires the exercise of considerable professional judgment on the part of the review team. The guidance contained herein is advisory in nature and is not intended to supplant the review team's professional judgment as to what approach to take or what specific procedures need to be performed in specific reviews.

This guide has been updated for standards, laws, regulations and other directives affecting OIG audits through February 2002. The Audit Committee welcomes any suggestions for further improving the external review program, in general, or this guide, in particular.

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## **GENERAL CONSIDERATIONS**

### **DEFINITIONS**

**1. Internal Quality Control System.** Operating policies and procedures established by the OIG to provide reasonable assurance that it (1) has adopted, and is following, applicable auditing standards; and (2) has established, and is following, adequate audit policies and procedures. Internal quality control system policies and procedures encompass the elements of staff qualifications, independence, audit performance and internal review.

**2. Internal Review or Quality Assurance Program.** An internal evaluation program that is performed by OIG personnel (either within the audit office or within another component of the OIG) and is designed to assess whether the OIG carries out its work in accordance with established policies and procedures, *Government Auditing Standards*, applicable Office of Management and Budget Circulars, and appropriate statutory provisions applicable to the OIG. A quality assurance program could also have as an objective an assessment of whether the work was carried out economically, efficiently and effectively.

**3. External Quality Control Review.** A review of an OIG's audit function by a Federal audit organization not affiliated with the OIG being reviewed that satisfies the objectives specified below.

**4. Individual Audit.** Any audit for which an audit report was prepared by the OIG or by an Independent Public Accountant (IPA) under a direct procurement contract to the OIG. When an audit report is based on a series of individual audits, the consolidated audit report and each of the individual reports could be considered an "individual audit."

### **OBJECTIVE OF THE EXTERNAL QUALITY CONTROL REVIEW PROGRAM**

**5.** The objective of the PCIE external quality control review program is to foster quality audits by OIGs through an independent assessment of the effectiveness of the internal quality control system in providing reasonable assurance that applicable audit standards and requirements are being followed. The program is intended to be positive and constructive rather than negative or punitive.

### **STAFFING AND QUALIFICATIONS**

**6.** The number of staff assigned to the review team is dependent on a number of factors including, but not limited to, the size and geographic dispersion of the OIG being reviewed, the size of the audit universe, and the scope of the review. Generally, the staffing required will include a full-time team leader and the equivalent of at least three other full-time staff members. Performing and reporting on an external quality control review requires the exercise of considerable professional judgment. For this reason, the team leader should be a senior manager with appropriate audit background and experience. The rest of the team should be senior auditors or audit managers. It is recommended that the team leader be at or above the GS-15 grade level.

7. The staff assigned to conduct the review collectively should possess adequate professional proficiency for the tasks required. Reviewers should be qualified and have current knowledge of professional standards and the government environment and government auditing relative to the work being reviewed.

8. When selecting the team, consideration should be given to the types and complexity of audits that will be reviewed and to any specialized skills that may be needed (for example, EDP or financial statement auditing skills). Also, some OIGs are using electronic working papers to document their audits to varying degrees. Review teams should be capable of reviewing such work. Because of these considerations, final decisions on team make-up may be deferred until after some of the preliminary planning and presite procedures are accomplished. Nothing in this section should be construed to limit the flexibility of the team leader in planning and performing the review.

### **INDEPENDENCE**

9. The reviewing OIG and review team members should meet the independence standards of *Government Auditing Standards*. Team members should be independent of the OIG being reviewed, its staff and its auditees whose audits are selected for review. Former employees employed within the past 2 years by the OIG being reviewed should generally not be selected to be part of the review team (although review team members may want to consult with former employees about one or more aspects of the OIG's operations). To ensure that independence is maintained both in appearance and in fact, the reviewing OIG cannot review the OIG that conducted its most recent review.

### **WORKING PAPERS**

10. Working papers should be prepared to document the work performed and the conclusions reached during the course of the review. The checklists included in this guide will be available in electronic format and review teams are encouraged to keep their working papers in electronic format as much as possible.

11. The working papers should be retained by the reviewing OIG at least until the subsequent external review is completed. The external review working papers should be subject to the same custody and safeguard policies that the reviewing OIG applies to its audit working papers. At a minimum, these policies should include safeguards against unauthorized use or access to the working papers, particularly working papers that contain confidential information. As indicated below under Memorandum of Understanding (MOU), the reviewing and reviewed OIGs should discuss and reach agreement up front on how the reviewing OIG will respond to requests for copies of the report (see paragraph 60) and access to the working papers by third parties (see paragraph 14).

### **WORKING ARRANGEMENTS AND ADMINISTRATIVE RECORDS**

12. The team leader should arrange with the OIG to have adequate work space for the review team. The team leader should also request that the OIG designate a facilitator. Generally, it is contemplated that the review team will be from one OIG. To the extent that travel is necessary to accomplish the objectives of the review, the reviewing OIG should travel at its own expense. If the team is made up of members of different OIGs,

the team leader should assure that the members are aware that their own organizations are to pay for their travel unless other arrangements have been made.

**13a.** The reviewing OIG should maintain administrative records on the staff days and calendar days it takes to do the review as well as the travel and other costs incurred.

**13b.** The OIG under review will be responsible for briefing the review team on organizational issues and work practices (i.e., roles and responsibilities of the audit divisions, the use of electronic work papers, etc.).

### **MEMORANDUM OF UNDERSTANDING (MOU)**

**14.** A memorandum of understanding should be prepared to assure that there is a mutual understanding regarding the fundamental aspects of the review. The following are topics that may be covered in the agreement.

- ❖ **Scope of the Review.** Page 5 of this guide contains a discussion of the minimum scope of review that is necessary to meet the *Government Auditing Standards* external review standard and PCIE policy statement (basic review) and the possibility of expanding the review to cover additional areas of an OIG's audit operations. The agreement should specify whether the review is to be a basic review and, if not, what additional areas are to be covered by the review.
- ❖ **Staffing and Time.** If desired, the agreement could include a provision addressing the planned staffing and time frames.
- ❖ **Preliminary Findings.** If desired, the agreement could include provisions addressing the need for timely interim discussion of preliminary findings. Added consideration should be given to reaching agreement on each potential issue at the earliest point in the review process. In some cases, written statements of condition may be useful aids in discussing the results of the reviews of individual audits.
- ❖ **Reporting Results.** The MOU should include what agreements are reached regarding (1) the provision of a draft report and letter of comments, (2) the holding of an exit or closeout conference(s), (3) report review procedures, and (4) who is going to sign the report. See page 12 for a discussion of these items.
- ❖ **Requests for Reports, Letters of Comment and Working Papers.** The agreement should state how the reviewing OIG will respond to requests for access to, or copies of, the working papers from the reviewed OIG and third parties such as: Congressional committees, individual members of Congress or their staffs, the press, GAO, OMB, other organizations that may be in an adversarial relationship with the reviewed OIG (such as an auditee), members of the public, and others. The MOU should also cover the handling of requests for the final report and letter of comments (See also paragraph 60).

**15.** Other topics may be covered as needed. When preparing a memorandum of understanding, care should be taken to not limit the ability of the review team to conduct the work necessary to accomplish the objectives of the review. If a team is precluded by the MOU from performing the work necessary to gather sufficient evidence to accomplish the objectives of the review, the MOU should be revised. If it is not, the

review team should report a scope limitation. Such a scope limitation may result in the reviewed OIG not meeting the *Government Auditing Standards* quality control standard.

### **DUE PROFESSIONAL CARE**

16. The review team should exercise due professional care and sound professional judgment in all matters relating to planning, performing, and reporting the results of the external quality review.

## **PLANNING AND PERFORMING THE EXTERNAL QUALITY CONTROL REVIEW**

### **OBJECTIVES**

17. Except as described in paragraph 22, the objective of an external quality control review is to determine whether the OIG's internal quality control system is in place, and operating effectively to provide reasonable assurance that established policies, procedures, and applicable auditing standards are being followed. Specifically, the review is intended to provide the review team with a reasonable basis for expressing an opinion on whether, during the year under review:

- ❖ The OIG's internal quality control system for its audit work was designed in accordance with the PCIE quality standards for audits (see appendix I).
- ❖ The OIG's quality control policies and procedures were being complied with in order to provide the OIG with reasonable assurance of conforming with *Government Auditing Standards*.

18. The review may be expanded to address other objectives if agreed to by the review team and the OIG being reviewed.

### **SCOPE OF THE REVIEW**

19. At a minimum, the scope of the external review shall cover the elements of the OIG's internal quality control system that are designed to provide reasonable assurance that the audits it performs, or for which it directly contracts, are carried out in accordance with *Government Auditing Standards* and established policies and procedures. These elements of quality control are staff qualifications, independence, audit performance and internal review. The review should cover a one-year period. This would normally be the year comprised of the two most recent semiannual reports to Congress. However, a different period can be chosen if there is a reason to do so. The scope of the review can be expanded to other areas of the audit operations if mutually agreed upon.

### **REVIEW APPROACH**

20. The approach advocated by this guide is to:

- ❖ Gain an understanding of the reviewed OIG's audit operation and its internal quality control system.

- ❖ Gain an understanding of the OIG's internal quality assurance program, including a review of any internal reports.
- ❖ Using the knowledge obtained from the preceding steps, assess review risk and select the offices and audits to be reviewed and the nature and extent of tests to perform.
- ❖ Review functional areas and individual audits.

21. Other approaches may be taken, however, it should be kept in mind that the objectives of the review described above should be met.

### **LIMITED SCOPE REVIEWS**

22. *Government Auditing Standards* recognizes that for reviews of smaller organizations, it may be more effective or efficient to place primary emphasis on reviewing individual audits rather than the internal quality control system. In this case, the objective of the review is to determine whether the OIG followed applicable standards in the conduct of its audit work. The guidance contained herein should be modified and adapted as appropriate to meet this modified objective.

### **PRESITE REVIEW STEPS**

23. The following steps can be performed prior to going on-site. This is particularly recommended when performing the steps on-site would involve the incurring of travel costs.

**a. Audit Quality Control Policies and Procedures.** The review team should request the OIG to complete and submit the questionnaire entitled *OIG's Audit Quality Control Policies and Procedures*. This questionnaire is presented in Appendix A and asks the OIG to identify the policies and procedures relevant to the various standards. This will provide the team with relevant descriptions of the OIG's quality control policies and procedures.

**b. Semiannual Reports to Congress.** The review team should also request a copy of the two most recent semiannual reports to Congress. The semiannual reports will provide information regarding the nature and volume of audit work as well as other matters that may help the review team understand the environment in which the reviewed OIG operates. It will also assist with selecting individual audits for review.

**c. Other Information or Documentation.** The review team should also consider obtaining and reviewing the annual audit plan(s) for the period covered, a printout of the audit tracking system, an organization chart, a roster of staff (including series, grades, and other necessary information), professional designations, information about advanced degrees or special skills, information about the training budget and OIG or regionally sponsored training, and continuing education summary for all staff for the most recent two-year reporting period.

**d. Working Paper Location and Nonaudit Services.** The review team should have the reviewed organization identify the location of all the working papers for the audits

that are being considered for review. In addition, the OIG should identify any nonaudit services related to the audits considered for review.

**e. Use of Questionnaires.** The team should also consider sending questionnaires to a representative number of the reviewed organization's audit staff to obtain anonymous responses that explain the staff's understanding of the organization's office policies, procedures, and practices. The questionnaire responses could possibly provide areas for the review team to focus the review. The National Association of State Auditors, Comptrollers and Treasurers (NASACT) has a sample questionnaire that the review team may be able to use to design their questionnaire. NASACT can be contacted on the Internet at <http://nasact.org/>.

**f. Prior External Review.** The review team should request a copy of the most recent external review report and make arrangements to review the related working papers. The purpose of reviewing the prior report is to see what was covered, what was found and what may need to be followed up on. The review of the prior working papers may be helpful in meeting the objectives of the current review. The reviewers should compare what is in the prior quality control review report and related working papers to the information received on the questionnaire referenced in 23a above to (1) see if recommendations were implemented, and (2) follow up on other differences. The working papers may also provide information concerning where to concentrate the current review effort.

**g. OIG's Internal Quality Assurance Program.** The team leader should obtain a copy of the documentation of the OIG's internal quality assurance program and the most recent internal evaluation report(s). If the team is planning to make use of the internal quality assurance process in planning its review, selecting audits or sites to be reviewed, or to provide evidence as to the OIG's compliance with its internal quality control system, the team leader should consider obtaining this information so the steps described on the following pages under the headings of "Review of Internal Quality Assurance Program," "Review of Internal Quality Assurance Reports," can be performed prior to going on site.

## **UNDERSTANDING QUALITY CONTROL POLICIES AND PROCEDURES**

**24.** Appendix B contains the questionnaire to be completed by the team to help document the team's understanding and evaluation of the adequacy of the OIG's quality control policies and procedures designed to provide reasonable assurance of compliance with established policies, procedures and applicable auditing standards. The questionnaire should be completed based on the answers provided by the OIG to the questionnaire, *OIG's Audit Quality Control Policies and Procedures*, discussed in paragraph 23.a, supplemented as necessary by (1) inquiry of management and appropriate staff, and (2) review of documentation of policies and procedures and their implementation. Evaluation of compliance with policies and procedures applicable to individual audits will be performed during the review and assessment of the internal quality assurance program and individual audits.

## **REVIEW OF INTERNAL QUALITY ASSURANCE PROGRAM**

**25.** The purpose of reviewing the internal quality assurance program is to determine whether the program is adequately designed to (1) meet the objectives of quality assurance and (2) produce reports on which the external review team can rely. If it is

found during the review of the design of the quality assurance program that it contains material weaknesses, a finding to this effect should be reported. Such conditions should also be considered when deciding how much reliance can be placed on the internal review reports. Appendix C contains guidance on assessing the design of the internal quality assurance program. Steps to determine whether the program is being carried out as designed are included in the reviews of internal quality assurance reports and individual audits.

## **REVIEW OF INTERNAL QUALITY ASSURANCE REPORTS**

**26.** The purpose of reviewing the internal quality assurance reports is to gather evidence about the OIG's compliance with established policies, procedures, and audit standards. Assuming that the quality assessment program is adequately designed, the internal quality assurance reports may provide the external review team with (1) an overall picture of the OIG's compliance with relevant policies, procedures and standards, (2) evidence regarding whether any deficiencies found in the prior external review were continuing or were corrected, and (3) information regarding areas of greatest external quality control review risk. If, based on procedures performed, the review team finds that the internal review program and reports can be relied upon, the review team may be able to use the results of the internal reviews that cover the same period as the external quality control review as direct evidence to support its opinion on the operating effectiveness of the internal quality control system. While the use of the results of internal reviews as direct evidence can reduce the nature and/or extent of testing performed by the external review team, it is not intended that the external review team's opinion on the quality control system be based solely on evidence provided by the internal reviews.

**27.** The time and effort to review internal quality assurance reports will probably vary widely in practice. Some OIGs may issue organizationwide internal evaluation reports while others may issue reports on individual offices or jobs. Depending on the circumstances, it may be more efficient to not review the internal quality assurance reports but to go directly to reviewing individual audits. This may be the case when (1) the design of the quality assurance program is unlikely to produce reports that are useful to the external review team for planning purposes or for forming conclusions on the operating effectiveness of the internal quality control system, or (2) the OIG operation is small enough that a sufficient number of individual audits can be reviewed in the time allotted to obtain the needed support for the required assurances.

**28.** Appendix D contains general guidance on reviewing internal quality assurance reports.

## **ASSESSING EXTERNAL REVIEW RISK**

**29.** Based on the information obtained in the preceding steps, the team should assess the external review risk associated with the nature of the OIG's work and its quality controls. External review risk is the risk that the review team:

**a.** Will fail to identify significant weaknesses in the OIG's internal quality control system and/or compliance with that system,

- b. Will issue an inappropriate opinion on the OIG's internal quality control system and/or compliance with that system, or
- c. Will reach an inappropriate decision about the findings to be included in or excluded from the letter of comments, or whether to issue a letter of comments.

**30. External review risk consists of the following two parts:**

*Inherent risk* is the likelihood that an individual audit will fail to comply with professional standards assuming the organization does not have a quality control system. For example, inherent risk would normally be higher in OIGs (or individual offices) that conduct mostly large complex audits or many audits of a nonrecurring nature, than in OIGs (or individual offices) that conduct mostly small, routine audits or many audits with a similar scope and objectives.

*Control risk* is the risk that an organization's quality control system will not prevent the performance of an individual audit that does not comply with professional standards. It consists of two parts: the organization's control environment and its quality control policies and procedures. The control environment represents the collective effort of various factors on establishing, enhancing, or mitigating the effectiveness of specific quality control policies and procedures. The control environment reflects the overall attitude, awareness, and actions of management concerning the importance of quality work and its emphasis in the OIG.

- a. The risk, consisting of inherent risk and control risk, that an individual audit will fail to comply with professional standards and/or the OIG's quality control system will not prevent such failure.
- b. The risk (detection risk) that the review team will fail to detect the design or compliance deficiencies in the OIG's quality control system that either result in the OIG having less than reasonable assurance of conforming with professional standards or constitute conditions whereby there is more than a remote possibility that the OIG will not conform with professional standards on individual audits.

**31.** Inherent risk and control risk relate to the OIG's audit work and its quality control system and are assessed by the review team. Detection risk relates to the effectiveness and extent of the external review procedures and can be reduced by reviewing more offices or audits, and increased by reviewing less offices or audits. The lower the inherent and control risk, the higher the detection risk that the review team can tolerate, while keeping overall external review risk at an acceptably low level. Conversely, the higher the inherent and control risk, the lower the detection risk must be driven by increasing the number of offices or audits that must be reviewed, to keep overall external review risk at an acceptable level.

**32.** The team should assess inherent and control risk at the OIG audit organization-wide level and also at the office level and type of audit level. Based on this assessment, together with other factors discussed below, the review team determines the offices and audits to be selected for review to reduce overall external review risk to an acceptably low level. The assessment of these risks is qualitative and not quantitative.

## **SELECTION OF OFFICES AND INDIVIDUAL AUDITS**

**33.** The selection of offices involves the exercise of considerable professional judgment. In addition to the risk assessment discussed above, factors to consider include the following:

- ❖ Number, size, and geographical dispersion of the offices.
- ❖ Changes in organizational structure, control and leadership.
- ❖ Number, type, and importance of reports issued by location.
- ❖ Degree of centralized control over regional and branch offices.
- ❖ Coverage and results of internal evaluation reports and prior external reviews (i.e., types of opinions rendered, problems identified, implementation plans and actions taken).
- ❖ The need to verify the results of internal evaluation reports.

**34.** The review team should strive to include a sufficient number of offices that are representative of the OIG with greater weight given to offices with a higher assessed level of review risk.

**35.** The degree of centralized control over regional and branch offices and the audit reports they issue may have an impact on the number of offices and audits selected for review. If the degree of centralized control is high, fewer offices/audits may need to be visited/selected and vice versa.

**36.** Coverage, currency and results of prior external reviews and internal reviews can be considered in various ways. If prior reviews show that one or more locations had problems in the past, the team may want to review a sample of such locations to see if corrective actions have been implemented and, if so, if they were effective. For example, if training was provided to the location's staff or if new procedures were given, the review team may want to go back to see if these actions were effective. If the prior problems at a site were limited to audits under one supervisor who is no longer there, selection of that site for follow up would probably not be appropriate (although the site could be selected for other reasons). On the other hand, the team may want to select offices that haven't been covered in past reviews to see how they perform.

**37.** If the review team plans to rely on the results of the OIG's internal quality assurance reports to provide direct evidence to support its opinions and assurances (see paragraph 26), then it must select a sample of the offices (and audits) that the internal reviewers reviewed to determine if the appropriate conclusions were reached. In doing so, the team should select offices (and audits) that the internal review found to be in accordance with the standards as well as those they found to be deficient.

**38.** In determining the number of reports to review, it should be kept in mind that the objective of doing the review is to obtain evidence regarding the performance of the OIG overall, not each individual office. Therefore, team leaders should not feel that they need to select a certain number of reports at each location. The number of reports at each location should be based on consideration of all of the factors. Consideration of the types of audits includes (1) identifying the types of audit work the OIG performs and contracts for (e.g., grants, contracts, financial statements, performance, economy and efficiency, etc.) and (2) selecting audits with a higher assessed level of review risk and representative of the major types of audit work performed by the OIG staff or contracted-

out. Audit reports that are considered significant should be selected over more routine, less significant audits.

If the OIG performs and/or contracts for financial statement audit(s), at least one financial statement audit **must** be selected for review by the peer review team.

The review team will apply a **no advance notice** policy in advising the OIG of the specific individual audits selected for review. Upon commencing the review of the individual audits, the review team will advise the OIG of the specific audits selected for examination. The OIG will be directed to immediately provide all related working papers at that time to the review team. Where the review team anticipates conducting field visits (regional offices, sub-offices, etc.) in conjunction with examining individual audits, the field offices should be advised of the specific audits selected for review upon the review team's arrival.

If the OIG cannot provide the audit working papers within 2 working days of the request, they must complete the following attestation for completeness of the audit working papers upon their delivery.

<b>CERTIFICATION OF WORKING PAPERS</b>	
Agency: _____ Audit Number: _____	
Audit Title: _____ _____	
<b>Certification:</b> I certify that:	
<input type="checkbox"/>	To the best of my knowledge the audit working papers provided to the [Name of OIG Office] peer review team are complete and no changes were made since the report was issued.
<input type="checkbox"/>	Audit working papers are not complete and/or changes or additions have been made since the report was issued. Attached is an explanation as to why the audit working papers are not complete or why the changes and/or additions were made, with the effected audit working papers specifically identified.
_____ <b>Audit Leader (AIC)</b>	_____ <b>Signature/Date</b>
_____ <b>Supervisor (Program Director /Project Manager)</b>	_____ <b>Signature/Date</b>

## **NATURE AND EXTENT OF TESTS**

**39.** The nature and extent of tests of compliance should be sufficient to provide a reasonable basis for concluding whether the OIG's quality control policies and procedures were complied with to provide the OIG with reasonable assurance that its audit work was conducted in accordance with applicable professional standards. These tests should include:

- a.** Review of individual audits, including the reports and working papers for conformance with professional standards and internal quality control policies and procedures.
- b.** Interviewing appropriate professional and other staff to assess the level of understanding and compliance with the quality control policies and procedures.
- c.** Reviewing other evidential matter demonstrating compliance with quality control policies and procedures, such as accessibility of appropriate reference material and administrative, personnel and continuing professional education records.

**40.** Ordinarily, the review of individual offices' establishment of and compliance with quality control procedures is conducted on-site. However, having one or more offices send the appropriate documentation (e.g. audit working papers and reports, CPE records, etc.) for review at a central location is permitted, if (and only if) the team leader determines that the objectives of the review can be met without visiting the office(s) to be reviewed. This is more likely to be the case at OIGs where the quality control policies and procedures are established centrally and where there is centralized control and supervision. The distribution of policies and procedures through local and wide area networks, electronic bulletin boards and electronic mail as well as the use of electronic working papers may also be conducive to performing reviews of one or more offices without making a site visit.

## **REVIEW OF INDIVIDUAL OIG AUDITS**

**41.** The purpose of reviewing individual audits is to determine whether established policies, procedures, and applicable auditing standards were followed. Appendix E contains a checklist for the review of individual financial audits. Appendix F contains a checklist for the review of individual performance audits.

**42.** The review of individual audits should include a review of the auditor's reports, financial statements (when applicable), working paper files, and correspondence, as well as discussions with professional staff of the OIG.

**a.** The review of audits should ordinarily include all key areas of the audits selected to determine whether well-planned, appropriately executed, and suitably documented procedures were performed in accordance with professional standards and the OIG's quality control policies and procedures.

**b.** The review should also include any nonaudit services performed that are related to the audit to determine if personal impairments exist in accordance with Government Auditing Standards, Amendment #3. (See paragraph 38d)

**43.** For each audit reviewed, the review team should document whether anything came to its attention that caused it to believe that:

**a.** Where applicable, the financial statements were not presented in all material respects in accordance with generally accepted accounting principles (GAAP) or, if applicable, an other comprehensive basis of accounting.

**b.** The OIG did not have a reasonable basis under applicable professional standards for the report issued.

**c.** The documentation did not support the report issued.

**d.** The OIG did not comply with its quality control policies and procedures in all material respects.

### **REVIEW OF IPA MONITORING**

**44.** For audits performed by IPAs under direct contract to the OIG, the purpose of the review is to determine if the OIG has quality control policies and procedures for assuring the work meets standards and contractual requirements and whether they were followed. Appendix G contains a checklist for reviewing the OIG's monitoring of audits for which it directly contracts with IPAs.

## **REPORTING REVIEW RESULTS**

### **GENERAL**

**45.** The reporting on the results of an external review consists of the report on the external review and, when applicable, a letter of comments. The external review report contains the review team's opinion on whether the OIG's quality control system provides reasonable assurance of material compliance with professional auditing standards in the conduct of its audit. Any findings and recommendations (material weaknesses) will be an enclosure to the report and the report will refer to the enclosure. The letter of comments contains reportable conditions the reviewers identified.

**46.** The process leading to the issuance of a final report and letter of comments is something that must be discussed and agreed to prior to the start of the review. At a minimum, the process should include a procedure for the OIG to have the opportunity to comment on the report and the review team's findings and recommendations prior to the issuance of the final report. The review team must consider the comments before finalizing their report and letter of comments.

**47.** The details and mechanics of the reporting process are left up to the parties involved. Items that must be considered include the following:

- There must be on-site close out conferences with senior field office staff in each office reviewed and/or exit conference with senior audit management.
- Informal draft findings and preliminary conclusions should be presented during the review to the official(s) designated by the reviewed OIG. Providing informal findings and preliminary conclusions during the review process will

help to avoid any misunderstandings and help insure that all material facts are considered before a formal report is prepared. This will speed up the report finalization process.

- What internal review process should take place within the reviewing OIG and who will sign the draft report. The Inspector General must sign the final report.
- How long the reviewed OIG should have to provide written comments to the draft report and who in the OIG should provide them.

**48.** To minimize the time that elapses between the end of fieldwork and the issuance of the final report and letter of comments, the review team should promptly prepare the draft and final reports and letters and the reviewed OIG should promptly prepare its response to the draft.

### **REPORTS ON EXTERNAL REVIEWS**

**49. Report Content.** A final written report should be prepared and addressed to the Inspector General. The report should contain the following information:

- Scope of the review, including any limitations thereon, and any expansion beyond the basic review.
- A description of the objectives and characteristics of an internal quality control system.
- An opinion on whether the OIG's internal quality control system was designed in accordance with the quality standards established by the PCIE and was being complied with during the year under review to provide reasonable assurance of material compliance with professional auditing standards in the conduct of its audits (paragraph 50).
- If a qualified or adverse opinion is issued, the report must include an enclosure that describes the findings and recommendations related to the material weaknesses identified during the peer review (paragraphs 51-54). In addition, the report should identify, where applicable, material weaknesses that are repeated from the OIG's previous external review. When used, the letter of comments should only identify findings or issues that did not result in a qualified or adverse opinion, i.e., reportable conditions (paragraph 55-58).
- An enclosure that describes the peer review methodology, including a list of the audit reports reviewed and the OIG offices visited.
- The opinion report should refer to the letter of comments when a letter of comments is issued. The reference to the letter of comments will indicate that the other matters discussed therein do not affect the overall opinion.

Appendix H contains illustrative reports and defines the types of findings that should be included in the Opinion Report and Letter of Comments.

**50. Considerations Regarding the Type of Opinion to Issue.** The decision as to what type of opinion to provide is the most important and sensitive issue to be decided during the review. Any decision to issue a qualified or adverse opinion must be supported by strong and convincing evidence of systematic material noncompliance with professional auditing standards that materially affected a significant number of audit reports issued. In forming its opinion, the review team should consider whether it was able to perform all necessary procedures to accomplish the objectives of the review and the nature, significance and pervasiveness of deficiencies found.

**a. Scope Limitations.** A qualified report should be issued when the scope of the review is limited by conditions that preclude the application of one or more review procedures considered necessary in the circumstances and the review team cannot accomplish the objectives of those procedures through alternate procedures. For example, a review team may be able to apply appropriate alternate procedures (e.g., select another audit) when the working papers for one or more audits selected for review are unavailable for legitimate reasons (e.g., being held by a U.S. attorney to support litigation). On the other hand, if the unavailable audit was the only one performed during the year by an office for which the team assessed review risk as high, the team ordinarily would be unable to apply alternate procedures.

**b. Nature, Significance and Pervasiveness of Deficiencies.** The overriding objective of a system of quality control is to provide the OIG with reasonable assurance of materially conforming with professional standards in the conduct of its audits. When a review team encounters material failures to conform to professional standards, considerable professional judgment is required to determine whether an unqualified, qualified, or adverse opinion is appropriate. The review team should first try to determine the cause of the failure. The failure to conform with professional standards on an audit may be the result of an isolated human error and, therefore, does not necessarily mean that the review report should be qualified or adverse. However, when the review team determines that the cause of a significant failure to conform with professional standards is both systemic in nature and materially affected a significant number of audit reports issued, the review team should issue a qualified or adverse opinion report. For a failure to conform with professional standards to be considered systematic it must have occurred in at least one-fourth of the audits reviewed and must have occurred in two or more of the reviewed OIG's organizational units (i.e., audit divisions, audit directorates, audit field offices, etc.). Systematic failures that affect between one-fourth and one-half of the audit reports reviewed and that occurred in two or more of the OIG's organizational units should result in a qualified opinion. Systematic failures that affected more than one-half of the audit reports reviewed and a majority of the OIG's organization units reviewed should result in an adverse opinion.

- i. Causes that might be systemic in nature and might, therefore, affect the review team's opinion, include the following (not all-inclusive):
  - The failure is related to a type of audit in which the OIG or audit team had little or no experience and did not have appropriate training or outside assistance.

- The failure is related to a matter covered by a professional pronouncement that the OIG had failed to identify as being relevant to its audits.
  - The failure should have been detected if the OIG's quality control policies and procedures had been followed.
  - The failure should have been detected by the application of quality control policies and procedures commonly found in other similar OIGs.
- ii. The review team must consider the pattern and pervasiveness of the deficiencies found and their implications for compliance with the OIG's system of quality control as a whole, in addition to their nature and significance in the specific circumstances in which they were observed. In some cases, the design of the OIG's system of quality control may be deficient. In other cases, there may be a pattern of noncompliance with a quality control policy or procedure. On the other hand, the types of deficiencies noted may be individually different, not individually significant, and not directly traceable to the design of or compliance with a particular quality control policy or procedure.
- iii. In order to give appropriate consideration to the evidence obtained and to form appropriate conclusions, the review team must understand the elements of quality control and exercise professional judgment. The exercise of professional judgment is essential because the significance of the evidence obtained cannot be evaluated primarily on a quantitative basis. In assessing whether deficiencies found with the design of internal quality control policies and procedures are significant, the question should be asked, "Does the OIG have reasonable assurance that the objective of internal quality control (i.e., compliance with applicable standards, etc.) in the deficient area is met?" In assessing whether the system of internal quality control is functioning as prescribed, the team should consider the degree to which it found such policies and procedures were not being followed.
- c. Design Deficiencies. There may be circumstances when the reviewer finds few deficiencies in the work performed by the OIG and yet may conclude that the design of the OIG's quality control system needs to be improved. For example, an OIG that is growing rapidly and adding personnel and perhaps new responsibilities may not be giving appropriate attention to necessary policies and procedures in areas such as personnel management (hiring, assigning personnel to audits, and advancement). A reviewer might conclude that these conditions could create a situation in which the OIG would not have reasonable assurance of conforming with professional standards in one or more important respects. However, in the absence of deficiencies in the audits reviewed, the reviewer would ordinarily conclude that the matter should be addressed in either the letter of comments or through procedures less formal such as exit conferences. Under no circumstances will a qualified or adverse opinion be provided based on potential future problems, even if such problems could become material and systematic in nature if the reviewed OIG does not take appropriate preventive action.

**51.** When presenting findings of weaknesses in the design of the internal quality control system, the team should describe (1) the condition (what controls are lacking) and (2) the effect (e.g. the actual instances of nonconformance with professional standards found).

**52.** When presenting findings of noncompliance with internal quality control policies and procedures the team should put the findings in proper perspective by relating the extent of the noncompliance to the number of cases examined. When the team finds instances of nonconformity with professional standards that are related to noncompliance with quality control policies and procedures this information should be included in the finding.

**53.** Finding presentation should be both complete and fair. Exaggeration of a finding's significance or the extent of noncompliance found should be avoided. If deficiencies were found at only one of several sites reviewed, they would not be considered systematic and the report should so indicate so as not to infer that the deficiencies were organizationwide and systematic. The tone of the report should be positive and constructive rather than overly negative. The report should stress the opportunity for improvement in the future rather than criticism of the past. Recommendations should be made where improvements are needed or should be considered. Recommendations should be for improvements in the internal quality control system's policies and procedures and should take into account cost versus benefit considerations.

**54. Views of Responsible Officials.** One of the best ways to assure the objectiveness, accuracy, and completeness of the findings is to obtain the views of responsible officials. When apparent deficiencies are found during the course of the review, the team must discuss the situation with the appropriate responsible official(s) designated by the reviewed OIG. All preliminary draft findings and conclusions must be presented during the review to the official(s) designated by the reviewed OIG. This action will help to avoid any misunderstandings and help assure that all material facts are considered before a formal draft report is prepared. If these officials have additional facts or explanations that bear on the matter but do not change the team's mind concerning the occurrence of noncompliance and its materiality, the officials' views must be incorporated into the draft report. The review team must carefully analyze the responding official's comments to the draft report to determine whether the initial comments included in the draft report should be revised. A full explanation needs to be included in the final report as to what actions were taken in response to the reviewed OIG's official comments to the draft report.

### **LETTER OF COMMENTS**

**55.** A letter of comments may be used to address reportable conditions in either the unqualified, qualified, or adverse opinion reports (See Appendix H). The letter should include a detailed description of each reportable condition. The letter should also provide reasonably detailed summaries of the findings and recommendations so that the OIG can determine what actions it should take. Finally, the letter should list the audit reports and OIG organizational entities where the reportable conditions were found.

**56.** The letter of comments should be addressed, dated, and signed in the same manner as the report on the external review, and should include the following:

- a. A reference to the report on the external review, indicating the opinion rendered.

- b. A description of the purpose of the external review.
- c. A statement that the review was performed in accordance with standards and guidelines established by the PCIE.
- d. A description of the limitations of a system of quality control.
- e. A definition of a reportable condition and a description of the reportable conditions found. In addition, the letter should identify, where applicable, reportable conditions that are repeated from the OIG's previous external review.
- f. A statement that the matters discussed in the letter was considered in determining the opinion on the system of quality control.
- g. The reportable conditions should be described fairly (See paragraph 53), and include the views of responsible officials (See paragraph 54).

**57.** Although isolated instances of noncompliance with the OIG's quality control policies and procedures ordinarily would not be included in a letter of comments, their nature, importance, causes (if determinable), and implications for the OIG's quality control system as a whole should be evaluated in conjunction with the review team's other findings before making a final determination.

**58. Noteworthy Accomplishments.** In keeping with the constructive nature of the external review program, the team should report any particularly noteworthy accomplishments found during the review. Examples of such items would be particularly creative and effective audit approaches or procedures or particularly efficient and effective quality control procedures. Other OIGs may benefit from this information. This may be done through a formal letter of comments or through other appropriate means such as exit conferences and informal letters of noteworthy accomplishments.

#### **REPORT DISTRIBUTION AND FOLLOW-UP**

**59.** Upon completion, the final report on the external review and, if applicable, the letter of comments should be addressed to the Inspector General. Any decisions concerning implementation of any recommendations in the report rest solely with the reviewed OIG. Subsequent external reviews should look at areas where problems were found in the past to determine if the same problems exist during the subsequent period.

**60.** Upon receipt of the final Opinion Report to the Inspector General, the reviewed OIG will provide a copy of the report to the head of the Agency and advise the Vice Chair, PCIE of the date of report.

(The Vice Chair, PCIE will prepare a schedule of completed peer reviews, and advise the appropriate congressional committees that the Opinion Reports are available on request from the reviewed OIGs.)

## REFERENCES

References are provided to enable the auditor to refer to relevant requirements and standards. The auditor should be familiar with the requirements and standards and have them available when performing the audit. Below are the abbreviations used to reference the requirements and standards contained in this document.

AU	<i>Codification of Statements on Auditing Standards</i> , promulgated by the American Institute of Certified Public Accountants (AICPA).
GAS	Government Auditing Standards. The financial audit standards contained in <i>Government Auditing Standards</i> (1994 Revision), published by the General Accounting Office (GAO). These standards are broad statements of the auditors' responsibilities, promulgated by the Comptroller General of the United States.
GAS3	Government Auditing Standards, Amendment #3, "Independence," dated January 25, 2002. [ <b>Note:</b> The paragraph references from Amendment #3 have not been incorporated into the overall GAS document. The current version of GAS addresses independence in paragraphs 3.11 through 3.25. Paragraphs 3.26 – 3.30 address different standards. Amendment #3 addresses this standard in paragraphs 3.11 through 3.30.10. Therefore, to minimize confusion, we use "GAS3" to reference the independence standard under Amendment #3.]
AT	<i>Attestation Standards</i>
AU	<i>U.S. Auditing Standards</i>
SAS	<i>Statements on Auditing Standards</i>
OMB 01-02	Office of Management and Budget Bulletin 01-02, "Audit Requirements for Federal Financial Statements"
OMB 97-01	Office of Management and Budget Bulletin 97-01, "Form and Content"
SFFAS	Statements of Federal Financial Accounting Standards, developed by the Federal Accounting Standards Advisory Board and issued by the Office of Management and Budget.