

Procuring Audit Services in Government:

**A Practical Guide
to Making the
Right Decision**

**AGA CPAG Research Series:
Report No. 19
February 2009**

ACKNOWLEDGEMENTS

About the Author

The author and researcher, **Jeffrey C. Steinhoff, CGFM, CPA, CFE**, retired from government in January 2008 after 40 years of federal service. He is a past National President of AGA and prior to his retirement was the managing director for Financial Management and Assurance at the U.S. Government Accountability Office (GAO). As managing director he headed up GAO's largest audit unit, with responsibility for oversight of financial management and auditing issues across the federal government. Included in his duties were the audit of the government's consolidated financial statements, the establishment of Government Auditing Standards and internal control standards, reviews of internal control, forensic auditing, financial management systems reviews, cost management, improper payments, and the full range of accountability and corporate governance issues. As of January 2009, he is a Director in KPMG's Federal Advisory Services practice. Views expressed in this report are those of the author and are not necessarily the views of AGA or his current employer, KPMG LLP.

AGA wishes to thank the Advisory Group members listed in Appendix B for their invaluable help and contributions to this research study.

Corporate Partner Advisory Group Leadership

Chairman

Hank Steininger, CGFM, CPA

Managing Partner, Global Public Sector,
Grant Thornton LLP

Vice Chairman

John Cherbini, CGFM, CPA

Partner, KPMG LLP

AGA Professional Staff

Relmond Van Daniker, DBA, CPA

Executive Director

Anna D. Gowans Miller, MBA, CPA

Director of Research

Susan Fritzen

Director of Corporate Partner Program

Marie Force

Director of Communications

Christina Camara

Publications Manager

**AGA is Proud to Recognize the Firm
Supporting this Effort:**



*Certified Public Accountants
and Consultants*

AGA's Corporate Partner Advisory Group Research Program: Building the Bridge Between Government and Industry

AGA's Corporate Partner Advisory Group (CPAG), executive director and director of research are creating research projects of value to governments, industry and the entire AGA membership. These studies are expected to result in reports assessing current and/or best practices and make recommendations for future improvements in federal, state and local governmental accounting, auditing and financial management. CPAG members support AGA research through either cooperative or sponsored research projects. "By undertaking research, AGA is fulfilling its mission as a thought leader in advancing government accountability," said AGA Executive Director Relmond Van Daniker, DBA, CPA. "This is one of numerous research initiatives that will benefit government and bridge the gap between the public and private sectors."

The CPAG was organized in 2001 as a business element within AGA. The mission of the CPAG is to bring industry and government executives together to exchange information, support professional development, improve communications and understanding, solve issues and build partnership and trust, thereby enhancing AGA's focus on advancing government accountability. Corporate member involvement in the CPAG is limited to organizations that sign up for the AGA Corporate Partner membership program. For more information on the research program, please visit www.agacgfm.org/research/default.aspx or contact Anna Miller at amiller@agacgfm.org.

TABLE OF CONTENTS

Preface	4
Why Would You Want an Audit?—A Decision Model for Procuring Audit Services	5
What are the Standards that Govern Government Audits?	7
What are the Different Types of Audit and Attest Engagements Covered By GAGAS?	9
How Do Audit and Attest Engagements Differ from Other Professional Services of an Evaluative Nature?	14
Can Government Audit Organizations and CPA Firms Perform Non-Audit or Advisory Services?	16
Ten Basic Principles to Consider if You Need Audit or Evaluative Services	17
Final Thoughts	18
Appendix A: Ten Basic Principles to Consider If You Need Audit or Evaluative Services	19
Appendix B: Advisory Group Members	19

PROCURING AUDIT SERVICES IN GOVERNMENT:

Preface

Government program and procurement officials routinely procure services to support agency missions and operations. In the case of audits, it is important that acquisition decisions be informed by a clear understanding of the distinction between audits and other evaluative services. This research paper, which is written as a guide, seeks to clarify for the non-auditor exactly what an audit entails, the professional standards followed, who can perform an audit, the value derived from an audit, and the standards and oversight to which government auditors and independent public accountants (hereafter referred to as CPA firms) are subject to when performing government audits.

Many decisions must be made in procuring professional services, such as audits and attestation engagements, internal control reviews, computer security assessments, cost-benefit studies, alternatives analysis, actuarial studies, forensic reviews, cost estimating and investigations. In some cases, the distinctions among these services are evident. But that is not always the case, and the term audit is sometimes used to describe evaluative services that may not in fact be an audit. The term audit is so widely used in our society that assessing whether your home or business is energy efficient is commonly called an energy audit. This can make it difficult for non-auditors to understand the differences.

While the term “audit” has broad meaning, in this research paper the term audit is used in the manner intended in *Government Auditing Standards* (commonly referred to as GAGAS), which is issued by the U.S. Government Accountability Office (GAO). In short, in government an audit is an engagement performed by an independent auditor that adheres to all the requirements of GAGAS. These standards include (1) ethical principles, (2) general standards, such as auditor independence, competence, and quality control and assurance, and (3) field work and reporting standards, such as the standards of the American Institute of Certified Public Accountants (AICPA) for financial audits and attestation engagements and the requirement to obtain sufficient, appropriate evidence. GAGAS covers a broad range of engagements from the audit of the financial statements to an audit of the performance of a program or operation to the performance of specific agreed-to procedures. GAGAS requires professional rigor and the application of specialized skills when performing an engagement.

For all intents and purposes, GAGAS can only be met by (1) an independent government auditor, such as GAO, a federal Inspector General (IG), an appointed or elected state or local auditor or a government internal audit organization or (2) a CPA firm. Government auditors and CPA firms are subject to oversight of their work through external peer review. Government auditors are also subject to oversight by legislative and/or government regulatory bodies. The work of CPA firms is also subject to regulatory oversight from state licensing boards. Whether government auditors or CPA firms, the auditing profession is characterized by independence and a dedication to providing high-quality professional work that is subject to strong ethical requirements and grounded in rig-

orous professional standards. The requirement to adhere to rigorous professional standards in performing an engagement along with a legal and regulatory oversight structure governing the performance of the work are what distinguish audits and attestation engagements from other types of evaluative engagements.

The goal of this guide is to help government managers make the right decision when procuring audit services. The guide provides a resource to help non-auditors understand the distinction between audit and other professional services that have an evaluative nature. Readers will have a better understanding of what they are buying when they procure an audit. They will know the differences between types of engagements provided by auditors and between audits and non-audit evaluative services. They will learn that audit organizations also provide non-audit services and how they differ from audit engagements performed in accordance with GAGAS. Readers will also know what they may not be getting when they procure a non-audit evaluative services or consulting engagement.

Deciding whether an audit is needed can be a difficult decision. In some cases, a management objective can be satisfied by either a performance audit under GAGAS or a consulting engagement. The guide begins by discussing why you would want an audit and providing a decision model for procuring audit services. The guide then provides greater context around the decision model by discussing the:

- Standards that govern government audits.
- Differences among financial audits, attest engagements and performance audits as defined by GAGAS.
- Differences between audits and other professional services of an evaluative nature.
- Provision of non-audit services by auditors under GAGAS.

The guide then provides final thoughts by highlighting *ten basic principles* to use in determining whether and what type of audit or non-audit evaluative service would best meet an entity’s needs.

This independent AGA research study was made possible through the sponsorship of AGA’s corporate partner, Kearney & Company. The resulting research product, *Procuring Audit Services in Government: A Practical Guide to Making the Right Decision*, represents the work of the researcher, Jeffrey C. Steinhoff. The views are those of the author, and are not necessarily the views of AGA or his current employer, KPMG LLP.

A PRACTICAL GUIDE TO MAKING THE RIGHT DECISION

Why Would You Want an Audit?—A Decision Model for Procuring Audit Services

When you are procuring an audit you are procuring a professional service that is performed in accordance with rigorous professional standards that are developed through a comprehensive process, have general acceptance, and are reinforced by means of comprehensive peer review and oversight by legislative oversight and regulatory bodies and/or state licensing boards.

As defined in Generally Accepted Government Auditing Standards (GAGAS), which are issued by the Comptroller General of the United States¹ and govern most government auditing, an audit is “*an independent, objective, fact-based, nonpartisan assessment of the stewardship, performance and cost of government policies, programs and operations.*”

GAGAS goes on to say that:

“Government audits also provide key information to stakeholders and the public to maintain accountability; help improve program performance and operations; reduce costs; facilitate decision-making; stimulate improvements; and identify current and projected crosscutting issues and trends that affect government programs and the people those programs serve.”

Two Principal Reasons for Procuring an Audit

There are two principal reasons that drive a decision to procure audit services.

- You may be required by law, regulation or terms of a contract or grant to obtain an audit. This makes the decision very easy. But understanding what an audit constitutes will allow you to make the best use of the results and to procure the right type of engagement.
- You may want the professional rigor that comes with an audit performed under GAGAS and, in turn, the assurance or opinion that goes along with applying this level of independent professional rigor. Management has the ultimate responsibility to ensure stewardship and accountability. It is responsible for carrying out its mission in an effective and efficient manner, ensuring adequate internal control and safeguarding of assets, and ensuring the quality of its financial statements and financial reports. In carrying out these roles, independent audit is a very powerful management control to help ensure that internal controls are sound, and programs and operations are being carried out as intended, and also for identifying ways in which government operations can be more efficient and effective. Audits can also be useful for focusing and driving management and accountability improvements to better serve the American public.

Audits provide an independent set of eyes and ears that can be invaluable. Auditors bring to the table:

- Strong analytic skills and an ability to look at situations in a way that is sometimes difficult for management, which is very close to the program or operation.

- Independence, objectivity and disciplined evaluative methodologies and a tremendous amount of know-how and knowledge spanning the broad expanse of government.
- Experience with the full range of government programs and operations. The right auditor takes a multi-dimensional approach and can look at situations and make informed judgments and actionable recommendations to management.
- Adherence to high professional standards in GAGAS when performing their work. This includes opening their organizations up to peer review and oversight by outside groups, such as legislative and regulatory bodies and state licensing boards.
- The public perception and credibility of independence, objectivity and professional rigor that is most useful to government officials in demonstrating accountability.

Deciding whether an audit is the best choice can be a difficult decision. In some cases, a management objective can be satisfied by either an audit under GAGAS or a consulting engagement. The consulting service may well be performed by highly skilled professionals, who may or may not follow a specific professional standard.

Steps to Consider in Procuring Professional Services

Now let us look at the steps to take into consideration in procuring professional audit services of an evaluative nature. The decision model, *Figure 1* on the next page, depicts the key steps.

The following six steps summarize the model.

1. Carefully identify the desired professional services. To help determine the right type of professional service to acquire, begin by answering the following questions:

- What is your objective(s)?
- Do you want an independent assessment?
- What type of assurance do you want?
- What question(s) do you want to have answered?
- How and for what are you going to use the results?
- Is the externally recognized credibility of an audit following GAGAS important?

2. Are there legal, regulatory or contractual requirements or any expectations of outside stakeholders, such as the U.S. Congress, a state legislature, or a city council or local board of supervisors, which would require or favor a GAGAS audit rather than another type of evaluative service?

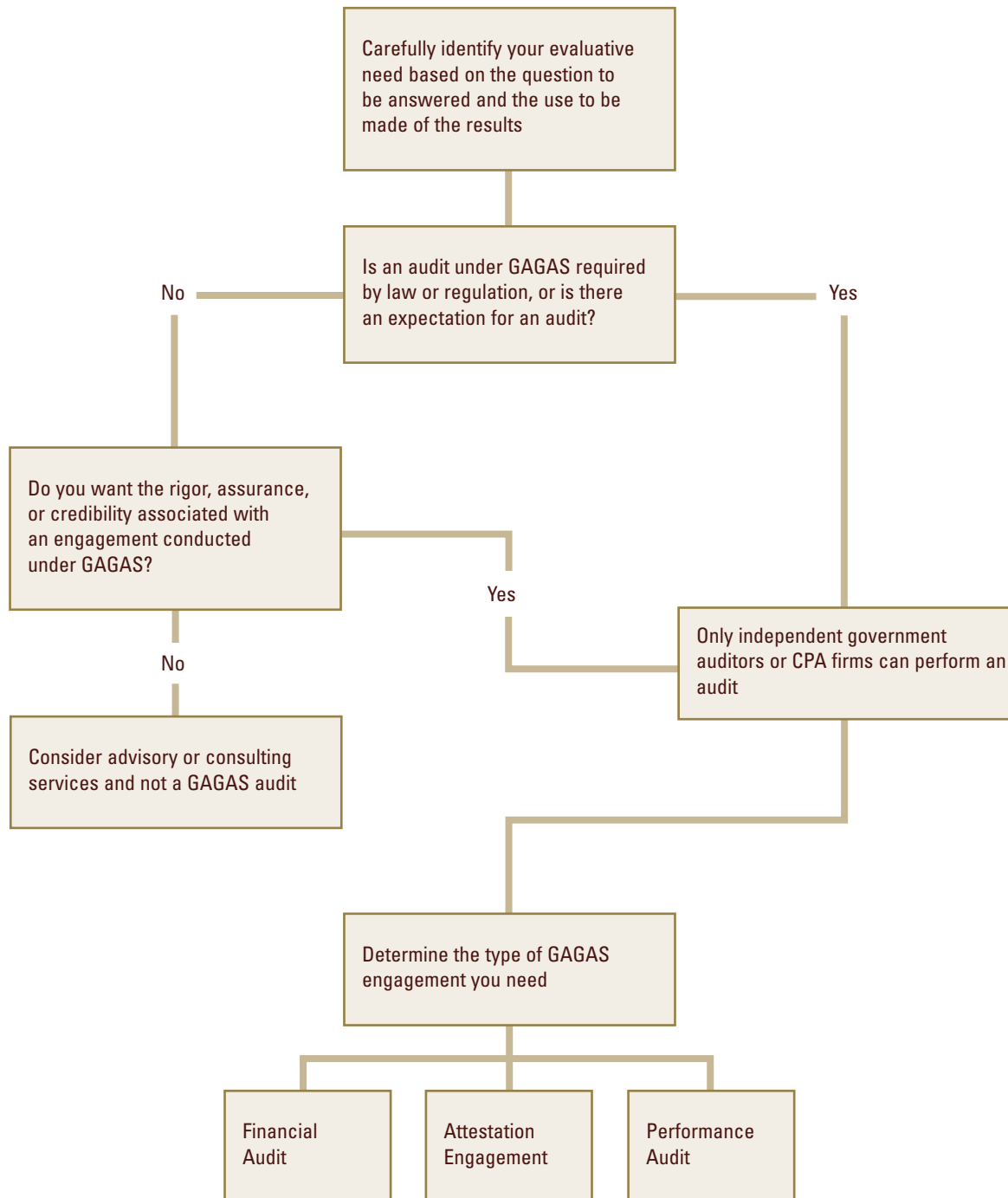
If yes, an audit under GAGAS should be procured. Go to step 5.

See “*What are the Different Types of Audit and Attest Engagements Covered by GAGAS?*” for further information about audit requirements and expectations (Pages 9 to 14).

3. Do you otherwise need the rigor of an audit, such as reasonable assurance, or is the objective of the services to provide information or data without professional evaluation or verification of the information or data? For example,

PROCURING AUDIT SERVICES IN GOVERNMENT:

Figure 1: Decision Model for Procuring Audit Services



A PRACTICAL GUIDE TO MAKING THE RIGHT DECISION

is the needed professional service to compile information without analysis?

If reasonable assurance is needed, a GAGAS audit is necessary. Go to step 5. If no, go to step 6.

See *“What are the Different Types of Audits and Attest Engagements Covered by GAGAS”* for a discussion or reasonable assurance (Pages 9 to 14).

4. Are there options for professional services other than an audit that would achieve your objectives and include professional evaluation or verification? For example, generally an actuarial opinion from an actuarial services firm would achieve the objectives of a similar professional service from an audit organization. However, some professional services, such as a financial statement audit, can be performed only by an independent government auditor or CPA firm.

If yes and a professional service other than an audit is determined to be the appropriate approach, obtain the other professional service. Go to step 6.

See *“How Do Audits Differ From Other Professional Services of an Evaluative Nature?”* for a discussion of other professional services (Pages 14 to 16).

5. After determining that an audit is the appropriate approach for the professional services, a determination needs to be made as to the type of GAGAS audit that is most appropriate to achieve the objectives: financial audit, attestation engagement or performance audit. The types of audits are summarized below.

- **Financial Audit:** A professional opinion about the reliability of financial statements or financial information.
- **Attestation Engagement:** A report based on a specific subject matter (such as internal control or compliance with a requirement) or an assertion about a subject matter. Attestation engagements under GAGAS can take three forms: examination, review or agreed-upon procedures.
- **Performance Audit:** Provide assurance or conclusions based on an evaluation of sufficient, appropriate evidence against stated criteria, such as specific requirements, measures or defined business practices.

See *“What are the Standards That Govern Government Audits?”* or a discussion of GAGAS and *“What are the Different Types of Audit Services and Audit Assurance”* (Pages 9 to 14) for a more detailed discussion of the types of audits, including examples of each type of audit.

6. Whether an audit under GAGAS or another type of professional service is desired, the next consideration is determining who should be selected to perform the professional service. For all intents and purposes, only independent government audit organizations and independent CPA firms can perform audits under GAGAS. A range of organizations, including management consulting firms, CPA firms and government auditors, can perform the other types of professional evaluative services. In selecting the type of organization to provide the professional services, consider, among other things, whether the organization has the

technical expertise and the time and cost to perform the services.

See *“Can Government Audit Organizations and CPA Firms Perform Non-Audit or Advisory Services?”* (Pages 16 to 17).

What are the Standards That Govern Government Audits?

When procuring audit services in government, it is important to know what standards or rules apply. GAGAS, which is issued by the Comptroller General of the United States, governs all federal government audits. The Inspector General Act mandates that all federal auditing be done in accordance with these standards. In addition, the Single Audit Act of 1984 (Public Law 98-502) and the Single Audit Act Amendments of 1996 (Public Law 104-156), as implemented by Office of Management and Budget (OMB) Circular A-133, *Audits of States, Non-Profits, and Local Organizations*, require that recipients of federal funds over certain dollar thresholds set by OMB obtain annual financial and compliance audits in accordance with GAGAS.

Further, other federal, state and local government laws, regulations, contracts, grant agreements and policies require audits in accordance with GAGAS as a requirement of obtaining government grant funding or contracts. Finally, many governmental entities, not otherwise required to follow GAGAS, have adopted the standards because of their comprehensiveness and general acceptance, which includes ethical and independence requirements, a requirement for peer review, specific continuing professional education requirements, and extensive field work and reporting requirements that if followed result in high-quality auditing. Therefore, GAGAS commonly applies to audits of federal, state and local governmental entities, programs, activities and functions as well as government assistance administered by contractors, nonprofit entities and other nongovernmental entities.

In issuing GAGAS, the Comptroller General uses an advisory council. The council is made up of selected federal inspectors general, state, local and private sector auditors, academia, program evaluation experts and users of audit reports. The council membership is typically between 20 to 25 members; so there is broad representation and a range of ideas. The goal of the council is to enable the Comptroller General to receive advice from a broad array of widely respected experts across the auditing profession, those who are impacted by audits and those in the program evaluation community. The latter is desired because of the close tie between program evaluations and the performance audit standards in GAGAS. The use of the council fosters high-quality auditing standards and general acceptance, which are hallmarks of GAGAS. The standards go through an open and rigorous development process and extensive exposure and public comment before they are issued. Comments are sought from all interested parties and considered in the adoption of the standards. Because of their comprehensiveness, high quality and general acceptance, GAGAS have been voluntarily adopted by many audit organizations

PROCURING AUDIT SERVICES IN GOVERNMENT:

not otherwise required to follow the standards, including government auditors in other countries.

GAGAS may also be used in conjunction with other professional standards. Most prominent are the financial audit standards established by the American Institute of Certified Public Accountants (AICPA). The field work and reporting standards and related statements on auditing standards of the AICPA are incorporated in their entirety by reference in GAGAS and represent the basic standards for government financial audits. For financial audits, the AICPA standards are augmented by additional requirements in GAGAS.

Other standards that may be used in conjunction with GAGAS include:

- Financial audit standards issued by the Public Company Accounting Oversight Board (PCAOB)
- Financial audit standards issued by the International Auditing and Assurance Standards Board
- Internal auditing standards issued by The Institute of Internal Auditors
- Evaluation principles issued by the American Evaluation Association

- Program evaluation standards issued by the Joint Committee on Standards for Education Evaluation
- Educational and psychological testing standards issued by the American Psychological Association

The first two standards relate to financial audits and the last four relate to performance audits.

If the auditor is citing another standard in its report and/or audit opinion, the auditor will always be held to the most rigorous standard if any difference or conflicts between the standards exist. GAGAS includes ethical principles, independence standards, requirements for quality control and assurance, audit field work standards and reporting standards that may go beyond other professional standards. These additional requirements would have to be adhered to for all engagements done under GAGAS, even if other standards were cited as well.

It is important for users of audit reports and those procuring audit services to understand GAGAS, just as you should understand the specifications of any commercial item before buying it. GAGAS and implementing audit methodologies, such as that presented in the GAO's Financial Audit Manual, which will be talked about in the next

Figure 2: Types of Audit and Attest Engagements

Engagement Type	Engagement Objective	Criteria	Standards Used to Perform Engagement	Who Can Perform	Type of Assurance
Financial Audit	Opinion that the entity's financial statements are presented fairly	Generally Accepted Accounting Principles	GAGAS, including standards issued by the AICPA	GAO, IG, state and local government auditor, or CPA firm	Reasonable Assurance
Attestation Examination	Opinion that management's assertion is stated fairly	Will vary depending on the management assertion	GAGAS, including standards issued by the AICPA for attest engagements	GAO, IG, state and local government auditor, or CPA firm	Reasonable Assurance
Attestation Review	Performance of sufficient work to provide a conclusion (versus an opinion) on a topic or matter	Will vary depending on the audit objective	GAGAS, including standards issued by the AICPA for attest engagements	GAO, IG, state and local government auditor, or CPA firm	Negative Assurance
Attestation Agreed-Upon Procedures	Performance of specific procedures defined by management	Will vary depending on the audit objectives	GAGAS, including standards issued by the AICPA for attest engagements	GAO, IG, state and local government auditor, or CPA firm	No Assurance
Performance Audit	Assessment of program efficiency and effectiveness	Will vary depending on the audit objective	GAGAS	GAO, IG, state and local government auditor, or CPA firm	Reasonable Assurance

A PRACTICAL GUIDE TO MAKING THE RIGHT DECISION

section of this guide, provide the specifications for an audit. Not only is it valuable to understand what you are buying, these documents provide guidance that can be most helpful to management in carrying out its oversight role. For a financial statement audit, this would translate into whether management prepared a report on its financial condition that can be relied upon. So to the extent auditors have published criteria to guide their work, it behooves management to understand those criteria and have a solid grasp as to how to apply the concepts and requirements to its own day-to-day operations where applicable. For example, the Financial Audit Manual includes extensive checklists, which would be equally useful to management.

What are the Different Types of Audit and Attest Engagements Covered by GAGAS?

The types of audits under GAGAS vary greatly as may the type of assurance provided by the auditor. Also, within each type of audit, there can be varying audit objectives and audit scopes. So you want to understand the differences in order to wisely assess the options available and procure the audit service that best meets your needs.

We will explore the three types of engagements that are provided for under GAGAS and the different types of auditor assurance:

- Financial audits
- Attestation engagements
- Performance audits

Figure 2 illustrates options available for engagements performed in accordance with GAGAS, the engagement objectives and criteria, the standards governing the work, the type of assurance being provided, and who can provide the respective service.

Types of Assurance

As illustrated in *Figure 2*, different engagement types have different types of assurance as follows:

- In *financial audits and attestation examinations*, an opinion is rendered. The opinion will state whether the subject matter is presented, or is fairly stated, in all material respects based on an established criteria. This is the highest level of assurance available under GAGAS engagements.
- An *attestation review* is substantially smaller in scope than an attestation examination. No opinion on the subject matter is expressed. An attestation review report will contain a statement as to whether the auditor is aware of any material modifications that should be made to the subject matter in order for it to be in conformity with the established criteria in all material respects. This is commonly referred to as negative assurance. Negative assurance can have different meaning, depending on the audit scope and the amount of work performed. For example, if the auditor provides negative assurance that no improper payments were identified, it would have greater meaning if the audit work included tests to look for improper payments. If very little work was performed to look for

improper payments, negative assurance would have little meaning. So, when contracting for audit services that provide for negative assurance, make sure you understand the amount of audit work on which the negative assurance is based.

- In an *agreed-upon procedures engagement*, no assurance is given. The agreed-upon procedures report will contain a list of the procedures performed (or a reference to them) and related findings. The auditor will not provide any assurance, even negative assurance.
- *Performance audits* are based on the concept of reasonable assurance. Under GAGAS, auditors must issue audit reports communicating the results of the performance audit and the report must contain (1) the objectives, scope and methodology of the audit; (2) the audit results, including findings, conclusions and recommendations, as appropriate; (3) a statement about the auditors' compliance with GAGAS; (4) a summary of the views of responsible officials; and (5) if applicable, the nature of any confidential or sensitive information omitted.

Types of Audit and Attest Engagements

Now let's talk in a little more detail about the different types of audit and attest engagements covered by GAGAS.

Financial Audits

Financial audits are what people most identify with auditing. As defined in GAGAS, financial audits "provide an independent assessment of and reasonable assurance about whether an entity's reported financial condition, results and use of resources are presented fairly in accordance with recognized criteria." Government financial statement audits go beyond the basic numbers on the financial statements. The auditor is also required to issue a report on internal control over financial reporting and compliance with laws and regulations.

In a financial statement audit, the auditor is providing an opinion as to whether the financial statements are fairly presented in all material respects in conformity with accounting principles that are generally accepted in the United States. In the case of the federal government, the accounting standards are issued by the Federal Accounting Standards Advisory Board (FASAB). Federal accounting standards are tailored to the unique financial transactions and information needs of the federal government. In the case of state and local governments, the accounting standards are issued by the Governmental Accounting Standards Board (GASB), which-similar to FASAB-considers any unique information needs of state and local governments. Both FASAB and GASB are independent standard-setters, which brings legitimacy to and general acceptance and recognition of the standards, both in and outside of government.

In a financial statement audit, whether in government or the private sector, *it is important for users to understand that the auditor is providing reasonable, not absolute, assurance.* To provide reasonable assurance, GAGAS prescribe audit field work standards. To help ensure the high-

PROCURING AUDIT SERVICES IN GOVERNMENT:

est quality financial statement audits that meet GAGAS and the expectations of the public for full financial accountability, GAO and the federal IGs have developed a three-volume Financial Audit Manual (GAO-08-585G and 586G and GAO-07-1173G) to guide all federal financial statement auditing. It is worth repeating: Managers procuring audit services should be aware of such methodologies and understand the additional rigor and distinction they bring to an audit engagement. After all, they define what the entity is getting for its money by spelling out what the audit includes and the assurance being provided.

While there are differing views on the cost-benefit of obtaining opinion-level audit work on internal controls as part of a financial statement audit, those procuring audit services should understand that the normal financial statement audit does not provide this level of assurance. You are receiving an opinion of the reasonableness of the financial statements. The auditor is reporting on any internal control weaknesses over financial reporting that are identified in the course of the audit and any compliance issues that arise. The auditor, though, is not providing reasonable assurance that internal controls over financial reporting are operating effectively and efficiently. Management cannot say that its auditor gave it the same level of assurance as on the financial statements with respect to its internal controls unless management contracted for opinion-level audit work for internal controls.

In this regard, financial statement audits performed by GAO include a level of audit work that permits GAO to issue an opinion on internal controls over financial reporting. This goes beyond the requirements in GAGAS and AICPA standards. An auditor's opinion on internal control is required for publicly traded private companies by PCAOB standards. The PCAOB was established by the Sarbanes-Oxley Act in response to corporate failures, such as WorldCom and Enron, where there were major failures in internal controls and corporate governance. PCAOB standards are applicable only to publicly traded companies. With the exception of financial statement audits done under PCAOB standards and by GAO, opinion-level audit work over internal controls is typically not done in government or the private sector, but can serve as a widely recognized measure and high standard of financial management accountability and credibility.

Also, when there is an opinion on internal control, it typically is limited to the controls associated with financial reporting and compliance with laws and regulations associated with financial reporting. Government entities typically have many internal controls related to programs and operations that go far beyond controls related to financial reporting. Internal control comprises the plans, policies, methods and procedures used to meet the organization's mission, goals and objectives. Internal control includes the processes and procedures for planning, organizing, directing and controlling program operations as well as management's system for measuring, reporting and monitoring program performance. Therefore, the objectives of internal control audits under GAGAS can be very broad. For example,

government entities would have internal controls associated with grant and contract management and with benefit and other payments that would go beyond the internal controls related to financial reporting. A financial statement audit would typically not address this wider range of internal controls.

In addition to financial statement audits, financial audits performed under GAGAS include audits that can provide for types of audit assurance different than financial statement audits as well as varying audit scopes. For example, under GAGAS, financial audits also encompass:

- *Providing special reports* that focus on specific elements, accounts or line items of a financial statement, whereby the audit scope does not cover the entire set of financial statements. The auditor would be providing reasonable assurance over the specific element audited but not for the financial statements as a whole.
- *Reviewing interim financial information* for which the scope of the audit may provide differing types of assurance targeted to management's needs, including negative assurance. It will be important that management understand the type of assurance it needs and is receiving because it may not be the same as with an audit of the financial statements.
- *Reporting on internal controls* over processing of financial transactions by service organizations. An example would be the processing of financial transactions by the National Finance Center (NFC) at the U.S. Department of Agriculture. The NFC provides accounting, payroll and disbursing services for a number of federal government entities. Therefore, an entity receiving services from NFC would want to know whether adequate internal controls are in place and operating effectively and whether the financial information reported by NFC and used by the entity in its own financial statements is reliable. Since service organizations typically serve a wide range of government agencies, it makes sense for those agencies to work together to define their audit needs and have a single audit organization perform the audit work. Reasonable assurance would usually be the type of assurance obtained.
- *Auditing compliance with regulations* relating to federal award expenditures and other governmental financial assistance in conjunction with or as a byproduct of a financial statement audit. Again, the audit scope will need to be defined. Does the entity want reasonable assurance, whereby the auditor is performing enough audit work to provide an opinion? Or does management want negative assurance, meaning nothing came to the auditor's attention as a result of the work performed in the financial statement audit. In this case, "work performed" becomes the driver. In some cases, that may be all you need. Clearly established audit objectives and audit scope are critical to any contract for audit services to clearly define the engagement.

A PRACTICAL GUIDE TO MAKING THE RIGHT DECISION

Attestation Engagements

The second type of engagement provided for in GAGAS is an *attestation engagement*. Whereas a financial audit focuses primarily on financial reporting, attestation engagements can cover a broad range of financial or nonfinancial objectives and may provide different levels of assurance about the subject matter or assertion depending on the user's needs.

As defined in GAGAS, attestation engagements "result in an examination, a review, or an agreed-upon procedures report on a subject matter or on an assertion about a subject matter that is the responsibility of another party." If an entity is contracting or arranging for an attestation engagement, the subject matter or assertion is established by the entity. The auditor is simply completing the work agreed to and answering the question(s) posed. The level of assurance is related solely to the subject matter or assertion and the procedures that have been agreed upon in advance. The auditor's report would focus solely on the results of the procedures performed and would make clear any limitations to the user of the report.

Attestation engagements are most helpful when you want the answer to a specific narrow question or series of narrow questions. The auditor is agreeing to perform certain specified procedures and is reporting the results of performing those procedures. Again, the onus is on the entity to properly define what it wants to be done to meet its objectives. There are three types of attestation engagements.

- **Examination:** In an examination, the auditor is focused on assessing whether something is in conformity with or presented fairly in all material respects related to a specific assertion by management. An example would be an examination of the reliability of reported performance measures. Another example would be an examination of management assertions for Medicare and Medicaid cost reports. Similar to financial audits, materiality is a factor and the independent accountant provides an opinion. In an examination, the audit scope is defined by management. The report is typically not restricted.
- **Review:** In a review, the auditor performs sufficient work to express a conclusion (versus an opinion) whether anything came to its attention that indicates that something is not based on or in conformity with certain criteria or is not fairly presented in all material respects based on the criteria. Reviews are not common in government because of the negative assurance being provided. In this regard, as specified in GAGAS, review-level work is not to be used for reporting on internal controls and compliance with laws and regulations. With a review, the user is receiving a conclusion based on just enough audit work needed to provide negative assurance that nothing came to the auditor's attention. An example of a review would be if management wanted negative assurance with respect to the information in the performance measures database.
- **Agreed-Upon Procedures:** An agreed-upon procedures engagement is the most common type of attestation

engagement. These engagements can be very useful because they can take many forms and consist of specific procedures that are agreed to by the organization requesting or contracting for the engagement. The auditor is asked a specific question by the entity. Again, the onus is on the entity to properly define what it wants to be done to meet its objectives. The auditor's findings are based on the specific procedures performed related to the subject matter. If you are contracting for an agreed-upon procedures engagement, you and the independent accountant agree to the scope of the work, and the independent accountant performs that level of work and nothing more. The level of assurance is defined by the procedures the independent accountant agreed to perform. A very simple example would be to determine if certain accounts reconciled. The auditor would perform the work necessary to determine if the accounts reconciled and would report any differences identified. GAGAS provides the following examples of possible agreed-upon procedures attestation engagements, whereby the auditor would agree to perform certain procedures to review:

- prospective financial or performance information;
- management's discussion and analysis (MD&A) presentation;
- the effectiveness of an entity's internal control over compliance with specified requirements, such as those governing bidding for, accounting for, and reporting on grants and contracts;
- an entity's compliance with requirements of specified laws, regulations, policies, contracts or grants;
- the accuracy and reliability of reported performance measures;
- evidence supporting incurred final contract costs and compliance with contract terms;
- the allowability and reasonableness of proposed contract amounts that are based on detailed costs; and
- the quantity, condition or valuation of assets, such as inventory.

Performance Audits

The third type of engagement provided for in GAGAS is performance audits. Whereas the field work and reporting standards and related statements on auditing standards of the AICPA are incorporated in their entirety by reference in GAGAS, the performance audit standards are contained exclusively in Chapters 7 and 8 of GAGAS. Over the past four decades, performance audits in government have continued to evolve and now represent the predominant type of audit in many government entities, particularly in the federal government. This is where GAGAS varies appreciably from private sector audit standards. The AICPA and the PCAOB standards cover financial audits and attestation engagements. By design, they do not issue performance audit standards, and there is no counterpart to the performance audit standards of GAGAS in the private sector.

The inclusion of performance audit standards is one reason GAGAS has been adopted by many governmental and

PROCURING AUDIT SERVICES IN GOVERNMENT:

non-governmental audit organizations that are not otherwise required to follow these standards, both in the United States and in other countries. There are other standards that may be used in conjunction with the performance audit standards, such as the internal auditing standards issued by the Institute of Internal Auditors and the evaluation principles issued by the American Evaluation Association mentioned earlier. But GAGAS is front and center when you talk about performance audits in government.

So when thinking about auditing in the government environment, remember it is much broader than financial auditing. The skill set differs greatly, with some auditors specializing in financial audits and others specializing in performance audits. Some auditors are equally competent and comfortable in both arenas; but you need to determine if that is the case. Also, it is critical that you understand the difference; since while financial audits and attestation engagements are closely aligned, performance audits are much different. However, all types of audits require adherence to ethical principles and general standards, such as the independence standards defined in GAGAS.

In the federal government, performance audits have almost exclusively been performed by GAO and the IGs. Performance audits require both an in-depth understanding of the program area being audited as well as an expertise in applying the GAGAS performance audit standards. Government auditors typically have this expertise. On the other hand, with the exception of selected financial statement audits performed by GAO, most of the federal financial statement audits are performed by CPA firms, under the oversight of the IGs. CPA firms bring to the table extensive expertise in financial statement auditing. Contracts for audit services often focus primarily on financial audits and attestation engagements. It is very important for management of government entities to understand the various types of audits and the skills needed to conduct the various types of audits, given the potential to make greater use of performance audits as part of their contracting strategy for evaluative services.

As defined in GAGAS: "Performance audits are engagements that provide assurance or conclusions based on an evaluation of sufficient, appropriate evidence against stated criteria, such as specific requirements, measures or defined business practices. Performance audits provide objective analysis so that management and those charged with governance and oversight can use the information to improve program performance and operations, reduce costs, facilitate decision-making by parties with responsibility to oversee or initiate corrective action, and contribute to public accountability."

Similar to financial audits and some attestation engagements, a performance audit provides reasonable assurance. The concept of reasonable assurance generally typifies all types of audits, as auditing is not intended to provide absolute assurance. To ensure that reasonable assurance is meaningful, GAGAS specifies that the auditors must obtain sufficient, appropriate evidence to support the conclusions reached. Tests of evidence will vary based on the audit

objectives and conclusions, but the benchmark for reasonable assurance is high and requires rigor in the application of auditing standards.

Whereas financial audits often follow standard methodologies that tie back to detailed technical standards, GAGAS defines a performance audit as a "dynamic process that includes consideration of the applicable standards throughout the course of the audit." Performance audit objectives may vary widely and are normally tailored for each audit. Performance audit objectives range from program effectiveness to economy and efficiency to program results to internal control to compliance with laws and regulations to prospective analyses. It is normal for a performance audit to have multiple objectives. For example, a performance audit focused on program effectiveness would typically involve an assessment of related internal controls, as they may be the cause of or solution to any shortfalls in program effectiveness. As a general proposition, if internal control is significant within the context of the audit objectives, performance audits under GAGAS would assess whether internal controls have been properly designed and implemented.

The objectives of performance audits are limitless under GAGAS. For performance audits, the nature and amount of audit work performed is driven by the stated audit objectives and, as such, can vary greatly. It is important not only to determine whether a performance audit is the appropriate type of audit service, but what is the appropriate audit objective. Let's examine a few questions that can form the objectives for a performance audit.

- Is a program effectively achieving its goals and objectives? The evaluation questions that support the objective of this performance audit would correlate to the objectives of the program and the criteria established to assess results of the program. Is the program designed in a manner that enables its objectives to be attained? Are the results intended from the program actually being achieved? For example, have dangerous emissions been reduced or student reading levels increased as the result of a government program? This type of audit is oftentimes called a program evaluation, which is why GAGAS includes by reference other relevant program evaluation standards, such as evaluation principles issued by the American Evaluation Association.
- Is the program or operation economical and efficient? Oftentimes intertwined with an assessment of program effectiveness, economy and efficiency performance audits address the costs and resources used to achieve program results or carry out an operation. A program or operation could be highly effective, but is it cost efficient? For example, the entity may be effective in procuring a hammer, but did the hammer cost \$500? The entity may pay the proper amount of disability benefits but did it take six months to make the payment or cost more than a reasonable amount to process the payment?
- Are legislative, regulatory, or organization goals and objectives being achieved? For example, is the organization in legal compliance with worker safety laws and regulations? Is sensitive information, such as medical

A PRACTICAL GUIDE TO MAKING THE RIGHT DECISION

records and Social Security numbers, being safeguarded in accordance with all laws and regulations, such as the Privacy Act?

- What is the relative ability of alternative approaches to yield better program performance or reduce costs and increase efficiency? Alternatives assessments are common performance audit objectives. For example, an auditor assesses which would be more cost effective and/or more efficient-making direct government loans or guaranteed government loans through a third-party lender.
- Are internal controls designed to provide reasonable assurance of achieving effective and efficient operations, reliable financial and performance reporting, and/or compliance with applicable laws and regulations? While meeting internal control audit objectives, primarily those related to financial reporting, can be evaluated using financial audit standards, many internal control reviews in government are performed as performance audits. As stated previously, internal control comprises the plans, policies, methods and procedures used to meet the organization's mission, goals and objectives. Internal control includes the processes and procedures for planning, organizing, directing and controlling program operations, and management's system for measuring, reporting and monitoring program performance. Therefore, the objectives of internal control audits under GAGAS can be very broad-based.
- How well are key functions, such as acquisition and grant management, being carried out, and are the interests of the taxpayer being adequately protected? The objectives for this type of performance audit often tie back to the adequacy of internal control but can address any facet of the function. Since procurement and grants each represent hundreds of billions of dollars in new spending annually and both are typically viewed in government as having a higher than normal risk, these types of functions are extensively audited under the performance audit standards.
- Is the agency vulnerable to cyber attack? The adequacy of computer security is a common performance audit objective and a form of internal control review.
- Has fraud or abuse occurred in a government program? Forensic audits fall within the performance audit category. Forensic audits use techniques, such as data mining, to identify anomalies for audit follow-up and enable the auditor to find the proverbial "needle in the haystack." An auditor is able to scour voluminous data files and make automated comparisons. Forensic audit programs are emerging as management tools as well. Government entities may find it very useful to establish their own internal forensic audit programs, whereby they essentially audit themselves on a continuous basis through the use of forensic tools.
- Do programs, duplicate, overlap or conflict with other related programs? Again, this is a common type of question that would be answered by a performance audit. Governments at all levels constantly face the need to reduce costs and improve service. Therefore, this type of performance audit can be most useful.
- Have user fees been properly set to recover all costs in an equitable manner? Generally, the auditor uses as criteria an express provision in law or regulation that defines what is meant by cost in this type of performance audit.
- Are program performance measures reliable, valid and relevant? This type of audit could be performed as an agreed-upon procedures engagement in accordance with the standards for attestation engagements, but is often done in accordance with the performance audit standards.
- Are government services and benefits reaching the right people based on their need and eligibility under law or regulation? A performance audit could answer questions regarding whether people were receiving services or benefits they were not entitled to, and/or whether people entitled to the services or benefits were somehow not reached by the program.
- Are appropriations being used in accordance with applicable laws and regulations? This is largely a compliance audit under the performance audit standards. A question to ask if you are contracting for this type of performance audit is what you expect from the auditor if problems are identified. In an audit under GAGAS, the government auditor (GAO, an IG or a state or local auditor) would typically go beyond the compliance question to determine what caused any non-compliance, such as a lack of or breakdown in internal control, and would make specific recommendations for corrective action. But this may not always be the case with a CPA firm, unless the expectation for this work is clear in the contract terms and there are provisions to pay for any additional audit work necessary to determine the cause of material problems and develop actionable recommendations.
- Are incurred or proposed costs in accordance with all applicable laws, regulations, and contract provisions or grant agreements? This would be largely a compliance audit, but may have elements of a forensic audit since the auditor may use forensic techniques to identify costs that fall outside the applicable criteria? Also, performance audits of contract costs are oftentimes initiated as part of the contracting process prior to awarding a contract.
- What is the future potential impact on government programs and services of current and projected demographic trends? This audit objective is an example of prospective analysis whereby the auditor would provide analysis or conclusions based on assumptions about the future as well as possible actions that the audited entity may take in response to the future events. This type of performance audit objective differs from an attestation engagement, which may also involve prospective information, because the scope is broader. For example, what will be the impact on the Medicare and Medicaid programs of an aging population and the projected increasing life spans of recipients? Other objectives pertaining to prospective analysis audits under GAGAS include

PROCURING AUDIT SERVICES IN GOVERNMENT:

assessing (1) program or policy alternatives, including forecasting program outcomes under various assumptions and/or scenarios, (2) policy or legislative proposals, including advantages, disadvantages, and the analysis of stakeholder views, (3) prospective information prepared by management, (4) budgets and spending forecasts that are based on assumptions about expected future events and management’s expected reaction to those future events, and (5) management’s assumptions on which prospective information is based.

What is important in thinking about a performance audit is that it can take on any question and can have many different faces. This is why this type of audit is heavily used in government. If you are contracting for performance audits, remember to identify auditors who have both an understanding of and ability to apply the GAGAS performance audit standards, have a good track record in performance auditing, have successfully undergone peer review of their performance audit practice, and have the requisite subject matter expertise in the program area or issue being audited.

The Audit Report

Reports under GAGAS will describe the type of assurance the auditor is providing. The audit report discusses the objectives, scope and methodology. The audit report will describe any limitations, such as incomplete or unreliable data.

For an audit report to meet the requirements of GAGAS, the user should be able to readily tell the extent of work performed by the auditor and the type of assurance being provided. Whereas reasonable assurance is the norm, an auditor may not be able to provide reasonable assurance in

all cases. An example of this would be where the underlying information provided by management may not be complete or reliable. For a performance audit, the auditor would report what it found, but then caution the reader that because of internal control or other problems, it is not sure if the information is complete or reliable. For a financial statement audit, the auditor will disclaim any opinion if it cannot be reasonably assured that the financial statements are fairly presented in accordance with generally accepted accounting principles.

Understanding the distinctions being made in the objectives, scope and methodology section of the audit report are critical to understanding the type of assurance being provided by the auditor and properly using the audit results.

How Do Audit and Attest Engagements Differ From Other Professional Services of an Evaluative Nature?

Differences between audit and attest engagements and non-audit services of an evaluative nature generally boil down to the underlying standards. The simple way to think about this is that engagements performed under GAGAS provide for a high standard of independence, field work, evidence and reporting. Non-audit evaluative services are simply not performed under these professional standards. This is not to say that those performing non-audit evaluative services are not technically proficient or do not do a good job. They just do not do their work under GAGAS.

Professional standards exist for virtually every profession-from actuaries to statisticians to engineers to fraud examiners to computer security specialists to systems developers to acquisition managers to program evaluators-and

Figure 3: Engagements Performed Under GAGAS v Non-Audit Evaluative Services

GAGAS Audit and Attest Engagements	Non-Audit Evaluative Services
Must be a government auditor or independent accountant with statutory authority (GAO, IG, state and local auditor) or a CPA firm	Generally no limitation as to who can perform the work
Must follow rigorous professional standards in GAGAS and sound methodologies	May or may not follow a defined professional standard, unless specified in the contract
Must be independent and follow ethical principles defined in GAGAS, state licensing agency, and industry regulators such as the AICPA and state CPA boards of accountancy	May or may not have an independence requirement unless specified in the contract; ethical standards may be firm based
Compliance with GAGAS and AICPA auditing standards enforced through peer review and oversight from state and industry regulators	No independent oversight or regulation unless specified in whatever standards are being followed
Broadly recognized measure of credibility	Credibility typically associated with the individual/firm performing the engagement and any defined professional standards they may be following
The report is supported by GAGAS, specifically standards for conducting field work, collecting evidence, and reporting	May offer a conclusion based on expertise and analysis unless following a defined professional standard

A PRACTICAL GUIDE TO MAKING THE RIGHT DECISION

the list goes on and on. Most professions operate under some type of standard or set of principles. Other professional standards may have some or even many of the same attributes as GAGAS. Examples would be standards related to professional care, sufficiency of evidence, and ethics. Auditors do not have the corner on any of these standards. They are common to many professions. However, if you want an audit, only GAGAS applies.

So if you are contracting for non-audit services, you need to make sure you understand what professional standards are being applied and what those standards entail. Ask yourself the question upfront: Will the application of these standards give you what you need and the type of assurance you are looking for? If there are no professional standards per se, your vigilance needs to be even greater in determining the criteria or technical approach being used and the type of assurance being provided.

Figure 3 illustrates some of the differences between engagements performed under GAGAS and non-audit evaluative services.

You know when you contract for an engagement under GAGAS that you are receiving a high level of professional assurance that the findings and conclusions are based on adequate and relevant evidence and the work is conducted to the highest of professional standards. You know that the findings and conclusions are independent, objective and fact-based and that due professional care was applied in performing the work. You need to make the same determination when contracting for evaluative services using other professional standards or criteria.

What if you are just seeking someone's expert opinion? If so, that can be very valuable, such as in the case of an expert witness or someone providing technical advice. An expert opinion or technical advice may be preferable if that is what you need. But understand, an expert opinion or technical advice is not an audit, even if provided by someone who is an auditor. Again, unless they say their opinion is being provided under GAGAS, they are simply providing their opinion and not an audit opinion, and perhaps not even an opinion under some other professional standard.

As discussed in the previous section, understanding the distinctions being made in the objectives, scope and methodology section of the audit report and the reporting requirements in GAGAS are critical to understanding and properly using audit results. The same applies to non-audit evaluative services, such as advisory services provided by an audit organization (which could be a government auditor or a CPA firm) or by a consulting organization, such as an actuarial, information technology or management consulting firm. You have to understand what the resulting report is really saying and is not saying. You have to focus on the standards or criteria on which the report is based.

Now let's look at a hypothetical example of reporting related to a non-audit evaluative service and the type of assurance that is being provided under several scenarios. An entity wants to know whether a capitalization threshold of \$50,000 is appropriate for its major assets. The entity does

not contract for an audit, but for advisory services. This is a common type of non-audit evaluative service in government, whereby experts are brought in to look at an issue.

The consultant hired to provide this advisory service performs extensive analysis and reports that the \$50,000 capitalization threshold is not unreasonable based on the information available to the entity. It then goes on to say in its report that the quality of the underlying information on the quantity, type and cost of assets is lacking in certain material respects and that with more reliable and complete data the result could be different. Finally, the consultant suggests that the entity may wish to improve data quality and then reevaluate the capitalization threshold.

What did the consultant providing the non-audit evaluative service report in this case? Was it that management of the entity could go to the bank with its \$50,000 capitalization threshold? Was it giving its seal of approval to the \$50,000 capitalization threshold? No on both counts; it was not giving any assurance that \$50,000 was the right number to use. The consultant did not find that the \$50,000 figure was unreasonable based on the information available; but likewise, did not find this number was reasonable because of serious shortfalls in the quality of the underlying supporting data. That should be the message that everyone takes away from this non-audit advisory service report.

Looking at this same situation from the lens of an audit, if a financial statement audit had been performed and major assets were a material balance on the financial statements, the auditor would have reported that it was not in a position to provide reasonable assurance that the financial statements were fairly presented. If the work had been done as a performance audit, the auditor would have reported that management had no reasonable basis for its capitalization threshold and would point to internal control and other weaknesses that made the underlying information supporting management's capitalization threshold unreliable.

In the above scenarios, the non-audit evaluative or advisory services scenario and the financial statement audit and performance audit scenarios, the entity received no assurance with respect to the reasonableness of the \$50,000 capitalization threshold. However, the way the message was presented was markedly different. For the financial statement audit, the message of a disclaimer is fairly well understood. The same would go for the performance audit, where the auditor would make clear its problems with the underlying information. The message may not be as clear for the non-audit evaluative service, which is not governed by the reporting requirements in GAGAS. The consultant providing the non-audit advisory services would be telling management it did not find the \$50,000 capital threshold to be unreasonable based on the available information, which is a somewhat different message. While the consultant pointed out serious problems it found with the underlying information, there could be a tendency for management of the entity to say that they had a reputable consulting firm come in and study this, and they did not find that the \$50,000 was unreasonable.

PROCURING AUDIT SERVICES IN GOVERNMENT:

That is why it is critical that everyone not only understand the differences between audits and attest engagements performed under GAGAS and non-audit evaluative services based on any other defined professional standards and/or criteria that may be applied in doing the work, but also understand the reporting standards and type of assurance being provided.

Can Government Audit Organizations and CPA Firms Perform Non-Audit or Advisory Services?

This brings us to the question of whether government auditors and CPA firms can provide non-audit advisory services in addition to conducting audits. The answer is yes. In fact, it happens every day. What an audit organization cannot do is cite adherence to GAGAS in reporting on this work. GAGAS does not cover professional services other than audits and attestation engagements. Government auditors and CPA firms regularly provide non-audit or advisory services. However, the range and amount of such services may vary greatly and there are limits if the organization wishes to retain its ability to audit the entity for which the non-audit services are being provided.

While GAGAS does not provide standards for non-audit services, it does cover the situation when audit organizations provide non-audit services for an entity for which the audit organization also provides audit services. Because auditor independence is one of the linchpins of auditing, GAGAS provides criteria for evaluating whether non-audit services would cause an impairment, in fact or appearance, to the audit organization's ability to subsequently perform audits of the entity. (See paragraphs 3.01 to 3.30 of GAGAS for a full discussion of auditor independence requirements.) This is very important because management of an entity may go to its auditor for non-audit advisory services and should understand where the line is drawn.

As a rule of thumb, GAGAS provides two overarching principles to assess the impact on independence if an auditor performs non-audit services for an entity it may currently audit or wishes to audit in the future. These two principles are simple in construct, while getting to the heart of auditor independence:

- Auditors must not provide non-audit services that involve performing management functions or making management decisions.
- Auditors must not audit their own work or provide non-audit services in situations in which the non-audit services are significant or material to the subject matter of the audits (meaning, those audits performed by the auditor now or in the future).

There are certain routine non-audit advisory services that involve providing technical advice based on professional knowledge and expertise that do not impair independence and do not require the application of the overarching principles. These services, which are spelled out in section 3.26 to 3.28 of GAGAS, include answering technical questions, providing training, tools, methodologies and guidance documents.

If non-audit advisory services go outside of these boundaries and violate either of the two overarching principles or the four supplemental safeguards, which GAGAS provides in paragraph 3.30 of GAGAS to further bolster the two overarching principles, the auditor is precluded from auditing the entity and citing adherence to GAGAS.

This is why oftentimes an entity will obtain advisory services from an auditor who does not also audit the entity. Sometimes, the auditor will elect to provide only advisory services to the entity and not compete for contracts involving audit services. The auditor providing advisory services will normally follow its own internal organization policies and procedures to help ensure quality of work that may in many respects parallel GAGAS. It may even follow another professional standard if one is applicable. But this work, no matter how rigorous, would not constitute an audit under GAGAS.

Advisory services may be exactly what you need. But at the end of the day, even if performed by an audit organization that has applied rigorous internal processes or another professional standard in performing the work, you cannot say you received an audit. This distinction is lost on many managers, who assume that since the messenger is an audit organization, the message is an audit opinion. That is simply not the case.

Let's now look at an example that may occur in a government organization. The entity needs to know whether its actuarial projections are reasonable. This information may be critical to program management, such as being used in budgeting, setting reimbursement rates or fees, contracting, long- and short-range planning, and/or financial reporting. The entity has a number of choices to make if it needs to go outside of the organization to get an answer to this question. Here are a few scenarios.

1. If the context is the financial statements and the actuarial projections are material to the financial statements, a financial statement audit would provide an opinion that would encompass the actuarial projection.
2. If the context is reimbursement or fee setting, the entity could go to an actuarial firm that specializes in this type of analysis. The entity could specify the scope of the work and that it is to be done under the Actuarial Standards of Practice issued by the Actuarial Standards Board. A CPA firm or a consulting firm could have staff that possess this level of actuarial expertise and could perform the work in accordance with the Actuarial Standards of Practice. In none of these examples would the entity be receiving an audit under GAGAS.
3. If the context is an opinion other than as part of a financial statement audit, the entity could contract for an attestation examination or a performance audit under GAGAS. The audit organization would provide opinion-level audit work based on reasonable assurance.
4. If the context is an opinion but not an audit opinion, you could again go to the Actuarial Standards of Practice as in scenario two.

A PRACTICAL GUIDE TO MAKING THE RIGHT DECISION

Let's say you wanted to know if your internal controls are effective. The same type of reasoning applies. If you want or are required to have an audit opinion, you will need to contract for an engagement performed under GAGAS. This means you will be contracting with a government auditor or CPA firm that is in a position to adhere to GAGAS. If you do not want or need to have an audit opinion, you can contract with a consulting firm that has this expertise or with a CPA firm that is not your auditor. However, you cannot later say that your auditor provided an audit opinion if you did not contract for an engagement under GAGAS.

An easy way to think about this is that you need to be precise in what you ask someone to do. If an audit is what you want, then basically only government auditors and CPA firms can perform it. If you want non-audit advisory services, then a broader range of consultants, government auditors and CPA firms may be in a position to provide the services. In any event, it is important to be sure to identify the right skills and expertise for the task. The point that bears repeating and repeating is that in the end you have to determine what best meets your needs and the expectations of your stakeholders.

Ten Basic Principles to Consider If You Need Audit or Evaluative Services

Contracting for audit and other evaluative services is not like buying a commodity. You are buying professional expertise of a specialized nature. But, if you follow the ten basic principles shown in *Figure 4*, in concert with the *Decision Model for Procuring Audit Services*, you should be able to successfully navigate these waters.

1. **Understand what you need.** This is first and foremost. It gets back to the initial question in this guide: *Why Would You Want an Audit? A Decision Model for Procuring Audit Services*. To help determine the right type of evaluative service, begin by answering the following questions.

- What is your objective(s)?
- What question(s) do you want to have answered?
- Do you want an independent assessment
- Do you need assurance, and if so, what type of assurance—reasonable assurance or negative assurance?

- How and for what are you going to use the results?
- Are there any expectations of outside stakeholders, such as the U.S. Congress, a state or local legislative body, or a regulator for an audit in accordance with GAGAS?
- Is the externally recognized credibility of an audit following GAGAS important to you?
- Who can perform an audit or attest engagement and comply with GAGAS?
- What are the alternatives available to meet the objective(s) and to answer the key question(s)?

2. **Determine how you can best use or leverage the results of whatever audit or evaluative services you ultimately obtain.** Identify up front how you can best use or leverage the results of the engagement to improve the accomplishment of your mission and/or improve accountability.

3. **Understand what an audit entails.** GAGAS is written in a way that you can understand the nature of the rigor and requirements underlying an audit and supporting the type of assurance an audit provides. As stated earlier in this guide, similar to understanding the specifications of any commercial item before you buy it, GAGAS and any related audit methodologies provide the specifications for an audit.

4. **Understand the different types of audit and attest engagements, so that you pick the one that best meets your needs.** Do you need a financial audit, an attestation engagement or a performance audit? As highlighted in this guide, not all engagements are the same. They have a lot of the same attributes, such as professional and technical rigor; but their objectives, scope, methodology and execution can be vastly different.

5. **Understand the concept of reasonable assurance and the limits of negative assurance.** How you plan to use the results drives the type of assurance you need. Remember that if it is a financial statement audit, the type of assurance is reasonable assurance under GAGAS. Negative assurance may be appropriate where management only wants specific procedures performed.

6. **Understand the nature of other professional standards, such as the Actuarial Standards of Practice.** Keep in mind that you may not need an audit. There are a range of advisory services that can be targeted to a specific evaluative

Figure 4: Ten Basic Principles to Keep in Mind When Obtaining Audit or Evaluation Services

Understanding Your Needs	Understanding What an Audit Entails	When an Audit is What You Need	When Consulting Services are What You Need
<ul style="list-style-type: none"> • Understand what you need • Determine how you can best leverage services • Make sure your expectations are realistic 	<ul style="list-style-type: none"> • Understand what compliance with GAGAS means • Know who can perform • Only independent statutory auditors or CPA firms can perform audits 	<ul style="list-style-type: none"> • Understand the different types of engagements • Understand assurance type 	<ul style="list-style-type: none"> • Understand qualifications of consultant and professional expertise • Know what CPA firms performing audits can provide if not performing an audit of the entity

PROCURING AUDIT SERVICES IN GOVERNMENT:

objective and designed to provide an answer to a specific question. The services may be anchored by professional standards that provide the type of rigor needed to draw meaningful conclusions. However, this may not be the case, and you need to thoroughly understand the nature of the requirements of any professional standards being used.

7. Always remember that in practical terms only an independent government auditor or CPA firm can meet the requirements of GAGAS. So never hire a non-audit organization to perform an audit.

8. Recognize that while auditors routinely provide advisory and other non-audit services, GAGAS includes independence standards that would prohibit auditors from performing both audit and non-audit advisory services if either of the two overarching principles for auditor independence or the four supplemental safeguards in GAGAS would be violated. Independence is at the heart of auditing. Therefore, you may need to have one auditor to perform audits and another to provide advisory and other non-audit services for which an organization that performs audits may be uniquely or best qualified to perform.

9. In selecting the contractor, consider the experiences of the organization and technical qualifications of its staff as they relate to the objective(s) and the question(s) you want to have answered. Government auditors and CPA firms have expertise critical to a high-quality audit or attestation engagement in compliance with GAGAS. The same principle applies to non-audit evaluative services. You should look carefully at the skills and expertise of the organization. While price is always a consideration, ensuring you have the right team, who are guided by the right evaluation objectives and professional standards, if applicable, should be paramount.

10. Understand any limitations in the work you are contracting for so that your expectations are realistic and use of the results appropriate. If you contract for advisory services that have limits on the objectives, scope and methodology or for which any underlying data or assumption have known problems, understand the limitations of any results. Also, be cognizant of any caveats in the ensuing report and the resulting limitations on how the results can be used.

Applying these 10 principles should enable you to select the right evaluative tool, whether it is an engagement under GAGAS or a non-audit service. In either case, remember you are buying professional services, where the skills and abilities of those providing the services are very important. The best result comes when you combine the right talent with the right evaluative engagement and make the right use of the results.

Final Thoughts

Through this guide, it is hoped you now have a basic understanding of what a government audit entails, the standards under which government audits are performed, the types of audit and attestation engagement available, the types of assurance provided by the different type of engagements, who can perform audits and attestation engagements, and the distinction between engagements performed under GAGAS and non-audit services of an evaluative nature. In this way, you will be able to make sound, informed decisions as to the type of engagement that best meets your needs. Always think about what are you trying to accomplish, and what is the best means of doing so? If you do this in the context of the 10 basic principles above, which are attached in summary form as Appendix A, and the *Decision Model for Procuring Audit Services* on page 6, you should be able to procure the right type of evaluative service.

Appendix A: Ten Basic Principles to Consider If You Need Audit or Evaluative Services

1. Understand what you need.
2. Determine how you can best use or leverage the results of whatever audit or evaluative services you ultimately obtain.
3. Understand what an audit entails.
4. Understand the different types of audit and attest engagements, so that you pick the one that best meets your needs.
5. Understand the concept of reasonable assurance and the limits of negative assurance.
6. Understand the nature of other professional standards, such as the Actuarial Standards of Practice.
7. Always remember that in practical terms only an independent government auditor or CPA firm can meet the requirements of GAGAS.
8. Recognize that while auditors routinely provide advisory and other non-audit services, GAGAS includes independence standards that would prohibit auditors from performing both audit and non-audit advisory services if either of the two overarching principles for auditor independence or the four supplemental safeguards in GAGAS would be violated.
9. In selecting the contractor, consider the experiences of the organization and technical qualifications of its staff as they relate to the objective(s) and the question(s) you want to have answered.
10. Understand any limitations in the work you are contracting for so that your expectations are realistic and use of the results appropriate.

Appendix B: Advisory Group Members

The following individuals served on an expert advisory group to the project researcher, **Jeffrey C. Steinhoff, CGFM, CPA, CFE**, who in January 2009 became a Director in the Federal Advisory Services practice of KPMG LLP. Before his retirement from government in January 2008, after 40 years of federal service, Mr. Steinhoff served as Managing Director for Financial Management and Assurance at GAO, which included leadership of GAO's largest audit unit and the responsibility for the development of GAGAS.

WA Broadus Jr., CGFM, CPA

President, W.A. Broadus Jr., CPA, P.C.

Robert F. Dacey, JD, CGFM, CPA

Chief Accountant, U.S. Government Accountability Office

Adam H. Goldberg, MPA

Chief, Financial Analysis and Systems Branch, Office of Federal Financial Management, U.S. Office of Management and Budget

Elliot P. Lewis, CPA

Assistant Inspector General for Audit, U.S. Department of Labor

Sam M. McCall, CGFM, CPA, CIA

City Auditor, City of Tallahassee, Florida; AGA Past National President

David P. Smith, CPA

Harold I. Steinberg, CGFM, CPA

Member, Federal Accounting Standards Advisory Board and Retired Deputy Controller, Office of Federal Financial Management, U.S. Office of Management and Budget, and Partner, KPMG

James L. Taylor, MPA

Principal Deputy Inspector General, U.S. Department of Homeland Security

David M. Zavada, MPA, CPA

Partner, Kearney & Company

In addition, AGA would like to thank the following individuals for their contributions to this report:

Julia Duquette, CPA

Principal, Kearney & Company

Jeffrey W. Green, CGFM, CPA

Senior Partner, Kearney & Company

AGA CPAG Research Reports Previously Published

- No. 1, March 2005:** *Audit Federal Financial Controls: Sooner Rather than Later?*
- No. 2, July 2005:** *Financial Management Shared Services: A Guide for Federal Users*
- No. 3, November 2005:** *Trends in Technology*
- No. 4, April 2006:** *The Federal Purchase Card: Use, Policy and Practice*
- No. 5, June 2006:** *Challenges in Performance Auditing: How a State Auditor with Intriguing New Performance Authority is Meeting Them*
- No. 6, June 2006:** *PAR—The Report We Hate to Love*
- No. 7, February 2007:** *The State Purchase Card: Uses, Policies and Best Practices*
- No. 8, March 2007:** *Federal Real Property Asset Management*
- No. 9, May 2007:** *Should State and Local Governments Strengthen Financial Controls by Applying SOX-Like Requirements?*
- No. 10, April 2007:** *Process-Based Financial Reporting*
- No. 11, May 2007:** *The State Travel Card—Uses, Policies and Best Practices*
- No. 12, June 2007:** *Trends in Technology—2007 Review*
- No. 13, June 2007:** *The Federal Travel Card—Uses, Policies and Best Practices*
- No. 14, January 2008:** *21st Century Financial Managers—A New Mix of Skills and Educational Levels?*
- No. 15, July 2008:** *SAS 70 Reports: Are they Useful and Can They Be Improved?*
- No. 16, Sept. 2008:** *XBRL and Public Sector Financial Reporting: Standardized Business Reporting: The Oregon CAFR Project*
- No. 17, Nov. 2008:** *Characteristics of Effective Audit Committees in Federal, State and Local Governments*
- No. 18, Jan. 2009:** *Grants Management: How XBRL Can Help*



*Advancing
Government
Accountability*

Association
of Government
Accountants

2208 Mount Vernon Avenue
Alexandria, VA 22301

PH: 703.684.6931
TF: 800.AG.A.7211
FX: 703.548.9367

www.agacgfm.org
agamembers@agacgfm.org