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AICPA audit committee toolkit: Government organizations; Audit committee toolkit

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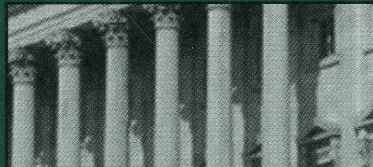
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The AICPA
**Audit
Committee
TOOLKIT:**
Government
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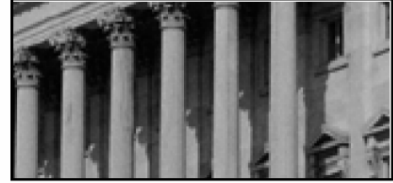
NOTICE TO READERS

The *AICPA Audit Committee Toolkit: Government Organizations* material is designed to provide illustrative information with respect to the subject matter covered. It does not establish standards or preferred practices. The *AICPA Audit Committee Toolkit: Government Organizations* material has not been considered or acted upon by any senior technical committee or the AICPA Board of Directors and does not represent an official opinion or position of the AICPA. It is provided with the understanding that the author and publisher are not engaged in rendering legal, accounting or other professional service. If legal advice or other expert assistance is required, the services of a competent professional should be sought. The author and publisher make no representations, warranties or guarantees as to, and assume no responsibility for the content or application of the material contained herein, and expressly disclaim all liability for any damages arising out of the use of, reference to or reliance on such material.

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September 2005

In January 2004 the AICPA launched its Audit Committee Effectiveness Center to provide resources in the public interest to those who work with, and serve on, audit committees of boards of directors. Since that time, the two main features of the Center: *The AICPA Audit Committee Toolkit* and the *Audit Committee Matching System* have helped thousands of organizations effectively carry out their corporate governance responsibilities.

We are pleased to introduce *The AICPA Audit Committee Toolkit: Government Organizations*, which has been developed by CPAs working in and with government organizations, and is tailored to meet the unique needs of the organizations that they serve.

The foundational component of *The AICPA Audit Committee Toolkit: Government Organizations* is the Audit Committee Charter Matrix. This Matrix and the accompanying checklists, interview guides, questionnaires and other resources are intended to be used as active tools to help the audit committee do the job they need to do.

All of the tools are also available as free downloads in MS Word from the Center Web site at www.aicpa.org/audcommctr, which will allow you to tailor and customize each of them to your organization's specific requirements.

We also encourage you to make use of the *Audit Committee Matching System*, which is a means to link CPAs that are willing to serve as members of boards of directors and audit committees with the organizations that need the CPA skill set in these roles.

Another feature of the Center is the E-Alert option. By registering for the e-mail alerts, you will be kept informed of new tools as they are released, updates to existing tools, and other developments that relate to audit committee responsibilities.

We are grateful to CNA for their sponsorship and continued support of the Center.

If you have questions, comments, ideas for additional tools or other feedback please e-mail our staff at acc@aicpa.org.

Sincerely,

Barry C. Melancon, CPA
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John F. Morrow, CPA
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Author's Note

It is important to note when using this Toolkit that we use the term *governing body* to describe those in government organizations that have the ultimate authority and responsibility for accountability of that government's public resources. At the different levels of government, the governing body will vary and may be a federal agency department head, legislative body, elected official(s), governing board, supervisory board, council, or any designee established by law or charter. This Toolkit also refers generically to chief executive officers, chief financial officers, and chief audit executives for positions in government organizations that are responsible for management, financial reporting and accounting, and internal audit matters. Because of the diverse titles in government organizations, we ask that you focus more on the function of a particular position rather than the title of that position.

Acknowledgments

We want to thank several of our members who participated in creating the *AICPA Audit Committee Toolkit: Government Organizations*. First, the task force that created the tools and made sure they were appropriate for use at all levels of government, and the organizations that employ them for allowing the time necessary to participate in this project. Combined, the task force members have vast knowledge of working in government at all levels and their input has been invaluable.

A special thanks to Debbie Davenport, who chaired the task force, and for allowing her colleague Randy Roberts to participate on the task force as well. Randy's depth of technical knowledge is outstanding and he reviewed each tool several times to ensure they are technically accurate and useful.

Finally, to our staff colleagues, Pam Green, Emanuela LiMandri, Marie Bareille, Michael Doyle and Karen Coutinho, and others, each of whom brought their personal skills and knowledge to make the publication of this *Toolkit* happen. We are grateful to these members and staff for their help and their willingness to make this book and the accompanying Web site available in support of the public interest.

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Audit Committee Charter Matrix for Government Organizations

INSTRUCTIONS FOR USING THIS TOOL: Government organizations have become increasingly interested in establishing audit committees to provide oversight for financial reporting, internal controls, and auditors' activities. Preparing an audit committee charter is actually required for most public companies. However, the charter is voluntary and a best practice for government organizations. This tool is designed to help government organizations consider the full breadth of audit committee activities and make the audit committee charter an effective document for managing audit committee activities. This tool is meant as a sample. Because government organizations have their own laws and regulations to consider, the audit committee charter presented here (first column) should be modified based on each government's requirements. Users of the tool should establish their own charter; list each charter objective in the first column; and use this example as a guide for defining the steps to accomplish each objective, the associated deliverable, and the frequency.

This tool uses the term governing body to describe those in government organizations that have the ultimate authority and responsibility for accountability of that government's public resources. At the federal, state, and local levels of government, the governing body may be a federal agency department head, legislative body, elected official(s), governing board, supervisory board, council, or any designee established by law or charter. This tool also refers generically to chief executive officers, chief financial officers, and chief audit executives for positions in government organizations that are responsible for management, financial reporting, and accounting, and internal audit matters.

Audit Committee Charter Matrix for the Year Ending: _____

Audit Committee Charter	Steps to Accomplish the Objective	Deliverable	When to Achieve (Frequency Due Date)	Date Completed
<p>1. Each member of the audit committee should be appointed by the governing body.</p>	<p>Identify/solicit interested individuals, including governing body members, who wish to serve on the committee. Forward information about interested individuals to the governing body for consideration.</p>	<p>Indicate in the audit committee minutes whenever a new member is appointed.</p>	<p>Affirm annually or whenever a change in status by any audit committee member occurs.</p>	
<p>2. At least one member of the audit committee should have financial experience.</p>	<p>Ascertain that at least one member of the audit committee has sufficient financial experience to provide guidance and assistance to other audit committee members; provide training if necessary.</p>	<p>Acknowledge in audit committee meeting minutes which member of the audit committee is designated as having financial experience.</p>	<p>Affirm annually, unless there is a change in status.</p>	
<p>3. Review the committee's charter annually, reassess the adequacy of this charter, and recommend any proposed changes to the governing body. Consider changes that are necessary as a result of new laws, regulations, or accounting and auditing standards, including <i>Government Auditing Standards</i> (Yellow Book) issued by the Comptroller General of the United States.</p>	<p>Review the charter each year. Assess the appropriateness of each point in the charter in light of the previous year's experience. Assess the completeness of the charter in light of new best practices and new legal, regulatory, accounting, or auditing requirements.</p>	<p>Report to the governing body on the appropriateness of the audit committee charter and any revisions recommended.</p>	<p>Review annually, unless changes are needed during the course of the year.</p>	

Audit Committee Charter	Steps to Accomplish the Objective	Deliverable	When to Achieve (Frequency Due Date)	Date Completed
<p>4. The audit committee should meet at least four times per year, and at additional times when necessary. These meetings may be combined with regularly scheduled meetings, or may be held more frequently as circumstances may require. The audit committee may ask members of management or others to attend the meetings and provide pertinent information as necessary.</p>	<p>In-person meetings should be held at least once each quarter. All members should be expected to attend. Arrange meetings in accordance with the government organization's open meeting laws. Prepare agendas for meetings and provide to members in advance, along with appropriate briefing materials.</p>	<p>Prepare meeting notices and advertisements as required by open meeting laws. Prepare minutes that document decisions made and action steps and approve them. File meeting minutes according to open meetings laws.</p>	<p>Minutes should be distributed as soon as possible but no later than before the next meeting.</p>	
<p>5. Conduct executive sessions with the independent auditors, chief executive officer (CEO), chief financial officer (CFO), chief audit executive/internal auditor (CAE), general counsel, outside counsel, director of financial reporting, controller, and anyone else as desired by the committee.</p>	<p>Determine reasons for which executive sessions may be conducted according to the government organization's open meeting laws. Establish these sessions in conjunction with quarterly meetings or as necessary. (See the tool "Conducting an Audit Committee Executive Session: Guidelines and Questions" in this toolkit.</p>	<p>Develop action steps to be taken, if appropriate.</p>	<p>Review quarterly, and as necessary.</p>	
<p>6. The audit committee shall be authorized to hire professional consultants as necessary. (This may take place any time during the year.) See the tool "Points to Consider When Engaging External Resources" in this toolkit.</p>	<p>A budget should be established for this purpose. Requests for proposals (RFPs) should be used if required by the government organization's procurement laws.</p>	<p>Review the report submitted by consultant.</p>	<p>Review as needed.</p>	

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Audit Committee Charter	Steps to Accomplish the Objective	Deliverable	When to Achieve (Frequency Due Date)	Date Completed
<p>7. Review and concur on the appointment, replacement, reassignment, or dismissal of the CAE. (Note: some or all of this objective may not apply in those circumstances in which the CAE is an elected official.) (See the tool "Guidelines for Hiring the Chief Audit Executive" in this toolkit.</p>	<p>Meet in executive session at each meeting with the CAE. Hold special meetings as may be necessary to address appointment, reassignment, or dismissal of CAE. The audit committee chair should be available if any unforeseen issues arise between meetings relating to the CAE. Meet at least once annually with other members of executive management and the independent auditors to discuss the performance of CAE. Discuss job satisfaction and other employment issues with the CAE.</p>	<p>Report to the governing body on the performance of the CAE including the effectiveness of the internal audit function.</p>	<p>Conduct ongoing reviews, as changes can be made at any time during the year.</p>	
<p>8. Oversee the appointment of the independent auditors to be engaged by the government organization for external reporting, and establish the related audit fees. (Note: this objective does not apply when the independent auditors are mandated by laws or regulations to perform audits for external reporting purposes.)</p>	<p>At least once each year, discuss the appointment and related audit fees with management, the CAE, and the governing body. Review total audit fee in relation to any nonaudit services being provided by the independent auditor.</p>	<p>Report on the performance of and recommend the fees to be paid to the independent auditors. Review the scope of all services provided by the independent audit firm throughout the government organization.</p>	<p>Review soon after year end, so that the recommendations for next year's external audit requirements can be met.</p>	

Audit Committee Charter	Steps to Accomplish the Objective	Deliverable	When to Achieve (Frequency Due Date)	Date Completed
<p>If the audit organization provides any nonaudit services, determine that the audit organization has considered and documented its consideration of how providing these nonaudit services does not violate the requirements that the audit organization (1) not provide services that involve performing management functions or making management decisions, and (2) not audit their own work, as stipulated in <i>Government Auditing Standards</i>.</p> <p>Review and evaluate the performance of the independent auditors.</p> <p>Review with the full governing body any proposed discharge of the independent auditors.</p> <p>(Note: this objective does not apply when the independent auditors are mandated by laws or regulations to perform audits for external reporting purposes.)</p> <p>(See the tool "Guidance for Developing a Request for Proposal for CPA Services (Government Organizations)" in this toolkit.)</p>	<p>Discuss the audit committee's review of the independent auditors with the governing body.</p> <p>Ascertain that the independent auditors do not perform any nonaudit service that is prohibited by generally accepted auditing standards or <i>Government Auditing Standards</i>.</p>			

Audit Committee Charter	Steps to Accomplish the Objective	Deliverable	When to Achieve (Frequency Due Date)	Date Completed
<p>9. In cases where the use of a particular independent auditor is not specified by law or regulation, consider establishing a regular schedule for periodically re-bidding the audit contract with an outside CPA firm.</p> <p>(See the tool "Guidance for Developing a Request for Proposal for CPA Services (Government Organizations)" in this toolkit.)</p>	<p>Create a regular schedule to re-bid the audit contract.</p>	<p>Document the schedule in audit committee meeting minutes.</p>	<p>Review schedule annually as part of the evaluation of independent auditors, and determine if the schedule needs to be accelerated.</p>	
<p>10. Review with management the policies and procedures with respect to the government organization's public officials' and management's use of expense accounts, public monies, and public property, including, for example, their use of the government organization's vehicles. Consider the results of any review of these areas by the internal auditors or the independent auditors.</p>	<p>Review policies and procedures annually. Discuss with CAE the need for testing by either the internal auditors, independent auditors, or other parties.</p>	<p>Report issues, if any, to the governing body.</p>	<p>Review policies and procedures at the second quarterly meeting and discuss audit plan.</p> <p>Review any significant findings as they arise.</p>	
<p>11. Consider, with management, the rationale for employing audit firms other than the principal independent auditors for services that the government organization or the independent auditors determine would not be appropriate for the principal independent auditors to perform.</p>	<p>If the independent auditors are being considered to provide nonaudit services, ensure that they have considered how these services would impact their independence with respect to the financial statement audit, as required by <i>Government Auditing Standards</i>.</p>	<p>Document auditor selection criteria. Also, use a decision matrix to evaluate and document independent auditor selection.</p> <p>Review engagement letter for each engagement.</p>	<p>Continually review the policy and compliance with it.</p> <p>Other auditors may need to be hired at any point during the year.</p>	

Audit Committee Charter	Steps to Accomplish the Objective	Deliverable	When to Achieve (Frequency Due Date)	Date Completed
	<p>Use RFPs for engaging auditors or other professionals for nonaudit or other services that the auditors cannot perform.</p> <p>Review compliance with the policy by management. (See the tool “Guidance for Developing a Request for Proposal for CPA Services (Government Organizations)” in this toolkit.)</p>			
<p>12. Inquire of management, the CAE, and the independent auditors about significant risks or exposures facing the government organization; assess the steps management has taken or proposes to take to minimize such risks to the government organization; and periodically review compliance with such steps.</p>	<p>Create a portfolio that documents the material risks that the government organization faces. Update as events occur. Review with management and the CAE quarterly, or sooner if necessary, to make sure it is up-to-date.</p>	<p>Submit a risk report including mitigation strategies and quantifiable risks and insurance to cover such risks, e.g., loss of business.</p>	<p>Review at least once each year, and more frequently if necessary.</p>	
<p>13. Review with the independent auditors, the controller/finance director of the government organization, and the CAE, the audit scope and plan of the internal auditors and the independent auditors. Address the coordination of audit efforts to assure the completeness of coverage, reduction of redundant efforts, and the effective use of audit resources.</p>	<p>Meet with independent audit partner, the controller/finance director, and the CAE to discuss scope of the previous year’s audit, and lessons learned. Later, discuss planned scope for audit of current year.</p>	<p>Document the meeting in the audit committee meeting minutes.</p>	<p>At the second-quarter meeting each year, review the scope of the previous year’s audit, and the interrelationship between the internal and independent auditors with respect to the scope of the independent auditors’ work.</p> <p>At the third-quarter meeting each year, review the plans for the audit of the current year.</p>	

Audit Committee Charter	Steps to Accomplish the Objective	Deliverable	When to Achieve (Frequency Due Date)	Date Completed
<p>14. Review with management and the CAE:</p> <ul style="list-style-type: none"> • Significant findings on internal audits during the year and management's responses thereto • Any difficulties the internal audit team encountered in the course of their audits, including any restrictions on the scope of their work or access to required information • Any changes required in the scope of their internal audits • The internal audit department budget and staffing • The internal audit department charter • The internal audit department's compliance with applicable standards (for example, <i>Government Auditing Standards</i>, or the Institute of Internal Auditors' (IIA's) Standards for the Professional Practice of Internal Auditing) 	<p>Review reports of all internal audits from the preceding 12 months and planned for the upcoming 6 months along with the status of each planned audit.</p> <p>Review and discuss the findings for each audit completed since the prior meeting, and management's response to the report.</p> <p>Discuss the internal audit department budget and staffing with the CAE.</p> <p>Discuss the internal audit department's compliance with applicable standards, including the requirement for a peer review once every three years.</p>	<p>Report on the status of all internal audits planned for the next quarter and/or year.</p>	<p>Review at each meeting.</p>	
<p>15. Inquire of the CEO and CFO regarding the fiscal health of the government organization as well as the financial status of the government organization in relation to its adopted budget.</p>	<p>Discuss the fiscal health of the government organization and its financial status in relation to the adopted budget with the CEO, CFO, and other executives. Identify any issues addressed, and their resolution.</p>	<p>Include in agenda for executive sessions.</p> <p>See the tool "Conducting an Audit Committee Executive Session: Guidelines and Questions" in this toolkit.</p>	<p>Review, as necessary, but at least annually.</p>	

Audit Committee Charter	Steps to Accomplish the Objective	Deliverable	When to Achieve (Frequency Due Date)	Date Completed
<p>16. Review with the independent auditors and the CAE:</p> <ul style="list-style-type: none"> The adequacy of the government organization's internal controls including computerized information system controls and security Any related significant findings and recommendations of the independent auditors and internal auditors together with management's responses thereto <p>(See the tools "Internal Control: A Tool for the Audit Committee" and "Fraud and the Responsibilities of the Government Audit Committee" in this toolkit.)</p>	<p>Review the reports of the internal audit team for all audits completed since the prior audit committee meeting.</p> <p>Review key internal controls with the CAE, and understand how these controls will be monitored during the year.</p> <p>Review these plans with the independent auditor to understand their scope with respect to key controls.</p> <p>Review with the CAE the plans for audits of other elements of the control environment.</p> <p>Determine that all internal control weaknesses are quantified, reviewed, and addressed.</p>	<p>Report to the governing body on issues relating to internal controls, with emphasis on management's ability to override controls and related monitoring.</p>	<p>Submit a comprehensive report to the governing body at the second-quarter meeting each year.</p> <p>Update on anything new, or any changes to the internal control system, at every meeting.</p>	
<p>17. Review with management and the independent auditors the effect of any regulatory and accounting initiatives, such as related organizations financing structures, derivatives, or securities lending.</p>	<p>Independently, through professional reading and CPE, keep up-to-date on new developments related to the government environment, including any regulatory and accounting requirements the government may be subject to.</p> <p>Discuss with management and the independent auditors in meetings. (See the tool: "Management's Summary of Unique Transactions and Financial Relationships" in this toolkit.)</p>	<p>Record discussion and any action steps in audit committee meeting minutes.</p>	<p>Review as necessary.</p>	

The AICPA Audit Committee Toolkit: Government Organizations

Audit Committee Charter	Steps to Accomplish the Objective	Deliverable	When to Achieve (Frequency Due Date)	Date Completed
<p>18. Review with the independent auditors that perform the financial statement audit:</p> <ul style="list-style-type: none"> All critical accounting policies and practices used by the government organization All alternative treatments of financial information within generally accepted accounting principles that have been discussed with the government organization's management, the ramifications of each alternative, and the treatment preferred by the government organization 	<p>Discuss each matter, and related matters that may come to the attention of the audit committee and/or the independent auditors through this process.</p> <p>Create an action plan and follow-up plan as necessary.</p>	<p>Submit reports and documentation of discussions and resolution of disagreements.</p>	<p>Review, at least annually, and/or in conjunction with the year-end audit.</p>	
<p>19. Review all significant written communications between the independent auditors and management, such as any management letter or schedule of unadjusted differences.</p>	<p>Discuss each item with the independent auditors and management (including the CAE) and conclude on the appropriateness of the proposed resolution.</p>	<p>Submit reports and documentation of discussions, resolution of issues, and the action plan for any items requiring follow-up and monitoring.</p>	<p>Review at the completion of the independent audit.</p>	
<p>20. Review with management and the independent auditors:</p> <ul style="list-style-type: none"> The government organization's annual financial statements, related footnotes, and management's discussion and analysis The independent auditors' audit of the financial statements and their report thereon 	<p>Discuss each matter, and others that may come to the attention of the audit committee through this process, with management (including the CAE) and the independent auditors.</p> <p>Review with management the course of action to be taken for any action requiring follow-up.</p> <p>Monitor any follow-up action that requires continued audit committee intervention.</p> <p>(See the tool "Discussions to Expect From the Independent Auditor" in this toolkit.)</p>	<p>Submit reports and documentation of discussions, resolution of disagreements, or action plan for any item requiring follow-up.</p>	<p>Review at the completion of the independent audit.</p>	

Audit Committee Charter	Steps to Accomplish the Objective	Deliverable	When to Achieve (Frequency Due Date)	Date Completed
<ul style="list-style-type: none"> The independent auditors' judgments about the quality, not just the acceptability, of the government organization's accounting principles as applied in its financial reporting The independent auditors' single audit of the federal awards administered by the government organization and their reports thereon Any significant changes required in the independent auditors' audit plan Any serious difficulties or disputes with management encountered during the audit Matters required to be discussed by Statement on Auditing Standards (SAS) No. 61, <i>Communication With Audit Committees</i> (AICPA, <i>Professional Standards</i>, vol. 1, AU sec. 380), as amended; U.S. Government Accountability Office's <i>Government Auditing Standards</i>; and the U.S. Office of Management and Budget's Circular A-133 related to the conduct of the audits 				

Audit Committee Charter	Steps to Accomplish the Objective	Deliverable	When to Achieve (Frequency Due Date)	Date Completed
<p>21. Review with the general counsel and the CAE legal and regulatory matters that, in the opinion of management, may have a material impact on the financial statements and compliance with federal, state, and local laws and regulations.</p>	<p>Discuss whether the government organization is in compliance with applicable laws and regulations.</p>	<p>Report to the governing body that the review has taken place and any matters that need to be brought to its attention.</p>	<p>Review at each meeting.</p>	
<p>22. Periodically review the government organization's code of conduct to ensure that it is adequate and up to date. Review with the CAE and the government organization's general counsel the results of their review of compliance monitoring with the code of conduct.</p>	<p>Review results with the CAE and general counsel. Consider any adjustments that may be necessary to the government organization's code of conduct. Consider steps that may need to be taken to ensure that compliance is at the highest possible level.</p>	<p>Report to the governing body that the review of the code of conduct was done. Recommend changes to the code of conduct to the governing body as needed.</p>	<p>Review annually at the fourth-quarter meeting. Review any significant findings as they arise.</p>	
<p>23. Review the procedures for the receipt, retention, and treatment of complaints received by the government organization regarding accounting, internal auditing controls, auditing matters, or suspected fraud that may be submitted by any party internal or external to the organization. Review any complaints that might have been received, current status, and resolution if one has been reached.</p>	<p>Review procedures with the CAE and the general counsel. Review all complaints that have been received and the status of resolution. Ensure that proper steps are taken to investigate complaints and resolve them in a timely manner. See the tool: "Anonymous Submission of Suspected Wrongdoing (Whistleblowers)—Issues for Government Audit Committees to Consider" in this toolkit.</p>	<p>Review an original of each complaint received, no matter the media used to submit them. Discuss the status or resolution of each complaint. Review a cumulative list of complaints submitted to date for common patterns or other observations.</p>	<p>Review at each meeting.</p>	

Audit Committee Charter	Steps to Accomplish the Objective	Deliverable	When to Achieve (Frequency Due Date)	Date Completed
<p>24. Review procedures for the confidential, anonymous submission by the government organization's employees of concerns regarding questionable accounting or auditing matters, or suspected fraud. Review any submissions that have been received, the current status, and the resolution if one has been reached.</p>	<p>Review procedures with the CAE and the general counsel. Review all complaints that have been received and the status of resolution. Ensure that proper steps are taken to investigate complaints and resolve them timely.</p>	<p>Review an original of each complaint received no matter the media used to submit them. Discuss the status of resolution of each complaint. Review a cumulative list of complaints submitted to date for common patterns or other observations.</p>	<p>Review at each meeting.</p>	
<p>25. The audit committee should evaluate the independent auditors and internal auditors.</p>	<p>Use information from audit committee meetings and executive sessions conducted throughout the year. Use a formal assessment tool for each group. See the tools: "Evaluating the Independent Auditors: Questions to Consider" and "Evaluating the Internal Audit Team: Guidelines and Questions" in this toolkit.</p>	<p>Submit recommendations for changes in process and procedures. For independent auditors, request RFPs if changes are being considered. (Note: this deliverable does not apply when the independent auditors are mandated by laws or regulations to perform audits for external reporting purposes.)</p>	<p>Review after completion of the annual audit cycle.</p>	
<p>26. The audit committee should review its effectiveness.</p>	<p>The audit committee should conduct a self-assessment and 360-degree evaluation of all members. See the tool: "Conducting an Audit Committee Self-Evaluation: Guidelines and Questions" in this toolkit.</p>	<p>Discuss recommendations for improving the effectiveness of the audit committee with the governing body.</p>	<p>Review annually.</p>	
<p>27. Create an agenda for the ensuing year or review and approve the agenda submitted by the CAE.</p>	<p>Complete the "Audit Committee Charter Matrix." (Use this tool as a sample, and tailor it to your organization.)</p>		<p>Review at the fourth-quarter meeting for the upcoming year.</p>	



Audit Committee Financial Experience Considerations

PURPOSE OF THIS TOOL: While there is no explicit requirement for a government audit committee to include a member having some level of financial expertise, it is considered a good practice. In addition, it should be the goal of the government audit committee that all its members have some level of experience in financial matters. The following information illustrates how the audit committee might approach assuring it has access to requisite financial expertise.

Audit Committee Financial Expertise

The following attributes are all deemed to be typical components of financial expertise:

- An understanding of generally accepted accounting principles (GAAP), including those relevant standards for state and local government accounting and financial reporting issued by the Government Accounting Standards Board (GASB); an understanding of financial statements, generally accepted auditing standards (GAAS), and generally accepted government auditing standards (GAGAS, also known as the *Yellow Book*). Depending on the circumstances at the government organization in question, knowledge of the Single Audit Act of 1984, as amended, and the U.S. Office of Management and Budget Circular A-133 might also be appropriate.
- The ability to assess the general application of the foregoing principles and standards in connection with the accounting for estimates, accruals, and reserves.
- Experience preparing, auditing, analyzing, or evaluating financial statements that present a breadth and level of complexity of accounting issues that can reasonably be expected to be raised by the organization's financial operations, or experience actively supervising (that is, direct involvement with) one or more persons engaged in such activities.
- An understanding of internal controls and procedures for financial reporting.
- An understanding of audit committee functions.
- A general understanding of the government environment and specific knowledge of the government sector operations (for example, local government, municipal services and finance, labor relations, public health, education, transit, etc.) in which the organization participates.

The following questions should be used to assess whether an individual audit committee member, or the committee as a whole, possesses the above attributes.

- Have one or more individuals completed a training program in accounting or auditing?
- Do one or more individuals have experience as a chief or principal financial officer (for example, finance director or business manager), principal accounting officer, controller, public accountant, or auditor?

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- Do one or more individuals have experience in position(s) that involve the performance of similar functions?
- Have one or more individuals gained experience by actively supervising a person(s) performing one or more of these functions?
- Do one or more individuals have experience overseeing or assessing the performance of other government organizations, companies, not-for-profit organizations, public accountants, or government auditors with respect to the preparation, auditing, or evaluation of financial statements?
- Do one or more individuals have other relevant financial experience in the government sector (for example, service on other government boards or experience as a banker or investment adviser)?
- Do one or more individuals have experience serving on audit committees of other government organizations?

Alternative Approaches to Acquiring Financial Expertise on the Committee

If no individual member of the audit committee possesses the attributes required for financial expertise, and the committee members collectively do not possess such attributes, several options might be considered:

- Establish a relationship with a peer or otherwise comparable government organization to have the chief financial officer for one organization provide financial expertise to the other. Such arrangements can be reciprocal or involve multiple organizations. (While this could be a solution, the appearance of interlocking boards might be seen as an impairment of independence and/or objectivity.)
- Engage a financial professional to provide financial expertise as a paid consultant to the audit committee. Such an individual must be otherwise independent with respect to the government organization (that is, must have no other financial arrangements with the organization).
- Establish a training program for audit committee members to develop the necessary financial expertise. Such training can include professional development programs offered by the AICPA, associations serving the government industry, or the specific sector in which the government organization participates, or in-house training programs led by members of the organization's financial management team.

Resources

Various organizations provide information to support audit committees in carrying out their responsibilities. In addition to this toolkit, the AICPA maintains the Audit Committee Effectiveness Center (www.aicpa.org/audcommctr/homepage.htm). Independent Sector has devoted significant attention to issues related to financial expertise, as have sector organizations such as the National Association of College and University Business Officers. Many public accounting firms provide information on these subjects as well. Finally, although its provisions are not directly applicable to government organizations, the "SEC Rule on Audit Committee Financial Experts" contains information that may be of interest. See the tool, "Resources for Audit Committees," for additional sources of information.



Conducting an Audit Committee Executive Session: Guidelines and Questions

PURPOSE OF THIS TOOL: Although it is generally accepted that audit committees should hold executive sessions with various members of the executive management, leaders of the financial management team, the leader of the internal audit team, and the independent auditor, the audit committee member may not understand the type of questions and the extent of the questions they should ask. This tool is intended to help the audit committee ask the right *first* questions, bearing in mind that the audit committee should have the necessary expertise to evaluate the answers and the insight to identify the appropriate follow-up question. See the “Other Questions for Management” section of this tool for possible follow-up questions audit committee members can ask key members of the financial management team in order to improve their understanding of the day-to-day operating environment and management teams’ decision-making processes and interactions.

What Is an Executive Session?

An executive session is a best practice that could be employed by audit committees for any reason, but here we are advocating that the executive session be used to meet with key members of the financial management team on a one-on-one basis. Executive sessions should occur at every meeting of the audit committee, though not every individual need be in an executive session at every meeting. For example, it is appropriate for the chief audit executive (CAE) and the independent auditors to have an executive session at every meeting, but the director of financial reporting might be in executive session with the audit committee only at the meeting before year-end results are released.

During an executive session meeting, minutes are (usually) not recorded, and when meeting with members of the financial management team, anyone who is not a member of the audit committee is excluded from the meeting. The purpose is to ask questions of various members of the financial management staff in a safe environment. It is important that, when meeting with the controller for example, the chief financial officer (CFO) not be in the room. Executive sessions should be a matter of routine at every audit committee meeting, and not on an exception basis.

The audit committee should avoid asking in an open session whether an individual has anything to discuss in an executive session. Such a question could put the individual in an awkward position with others in the government.

Asking open-ended questions in this kind of environment could be a major source of information for the audit committee. This tool includes examples of the kinds of questions the audit committee should ask. These are meant to be sample questions to help start a conversation and create dialogue between the individual and the audit committee. *These sample questions are not intended to be a checklist.* Audit committee members need to be financially sophisticated enough to understand the answers to the questions and to use these answers to develop appropriate follow-up questions. Since

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it will not be unusual to ask similar questions of key government officials or employees, the independent auditors and/or the internal auditors, a comparison of their respective responses could be a good source of insight. Depending on the answers, follow-up action may also be necessary, and the audit committee must be prepared to take that action. The most important thing to do when conducting an executive session is to *listen to the answers that are given and follow up on anything that is not understood!*

Note an executive session provides “safety” and comfort that allows discussants to give honest answers to questions that they might not feel free to answer in an open environment.

Nevertheless, the audit committee may want additional information. “Other Questions for Management” is an associated section of questions that follow the suggested executive session questions. The formality of an executive session may not be required for these questions, which nevertheless may elicit information the audit committee wants.

Audit committee members should also consider the history of the governmental entity, the current economic climate, the political environment, etc., when asking questions in executive session. Finally, each executive session should be concluded with a reminder to the member of management that audit committee members are accessible outside the meeting, and that they should feel free to reach out to the audit committee member at other times if the need arises.

It is important to note that not every government will have different individuals in each position, as assumed in the following questions. Nevertheless, the audit committee should be aware of the functions that are part of dual roles, and adjust the questions accordingly. For example, in a small government, the CFO and controller might share the duties of the director of financial reporting. The audit committee should explore how a function or role is accomplished, and compose questions accordingly. Also, the audit committee should consider and take into account other roles in the government. It may be that other people within a government should also be asked to meet with the audit committee in executive session.

INSTRUCTIONS FOR USING THIS TOOL: This tool is intended to help the audit committee ask the right *first* questions, bearing in mind that the audit committee should have the necessary expertise to evaluate the answers and the insight to identify the appropriate follow-up question. Audit committee members may want to use the questions in the “Other Questions for Management” section in conjunction with this one in order to formulate and ask the appropriate follow-up question.

Conducting an Executive Session— Sample Questions	Comments
Chief Financial Officer	
1. Do you believe the financial statements fairly present the government’s net assets and activities in accordance with generally accepted accounting principles (GAAP) or some other comprehensive basis of accounting (OCBOA)?	
2. Do you believe the disclosures are adequate and are understandable to the average user?	
3. Are you satisfied that an appropriate audit was performed by the independent auditors?	
4. Are you aware of any situations of management override (as it relates to financial reporting) within the government?	
5. Are you aware of any current or past fraud occurrence or any kind of fraud within the government? Do you know of any situations in which fraud could occur?	
6. Discuss areas in which an accounting treatment could be complex and/or unusual.	
7. Is there any activity at any level within the government that you consider to be a significant violation of laws, regulations, contracts or grants, or significant departures from GAAP? Are you aware of any abuse within the government that you would consider to be material?	

Conducting an Executive Session— Sample Questions		Comments
Chief Financial Officer (cont.)		
8. Have you encountered any situations in which the government complied with legal minimums of behavior, yet failed to go the extra mile to demonstrate its commitment to the highest ethical standards?		
9. Is there any activity within the government that you are uncomfortable with or consider unusual that warrants further investigation?		
10. Do you feel comfortable raising issues without fear of retribution?		
11. Are there any questions we have <i>not</i> asked that should have been asked? If so, what are those questions? Are there any individuals within or external to the government to whom we should address questions?		
Chief Executive Officer		
1. Do you believe the financial statements fairly present the government’s net assets and activities in accordance with GAAP or OCBOA?		
2. Do you believe the disclosures are adequate and are understandable to the average user?		
3. Are you satisfied that an appropriate audit was performed by the independent auditors?		
4. Are you aware of any situations of management override (as it relates to financial reporting) within the government?		
5. Are you aware of any disagreements between management of the government and the independent auditors?		
6. Are you aware of any disagreements between management and the internal auditors?		

Conducting an Executive Session— Sample Questions		Comments
Chief Executive Officer (cont.)		
7. Is there any activity at any level of the government that you consider to be a significant violation of laws, regulations, contracts or grants, or significant departures from GAAP? Are you aware of any abuse within the government that you would consider to be material?		
8. Have you encountered any situations in which the government complied with legal minimums of behavior, yet failed to go the extra mile to demonstrate its commitment to the highest ethical standards?		
9. Is there any activity within the government that you are uncomfortable with or consider unusual that would warrant further investigation?		
10. Are there any questions we have <i>not</i> asked that should have been asked? If so, what are those questions? Are there any individuals within or external to the government to whom we should address questions?		
Chief Audit Executive (leader of Internal Audit Team)		
1. Overall, is management cooperating with the internal audit team? Does management have a positive attitude in responding to findings and recommendations, or is it insecure and defensive of findings?		
2. Has management set an appropriate “tone at the top” with respect to the importance of and compliance with the internal control system around financial reporting?		
3. Are you aware of any current or past occurrence of any type of fraud in the government? Do you know of any situations in which fraud could occur?		

Conducting an Executive Session— Sample Questions		Comments
Chief Audit Executive (leader of Internal Audit Team) (cont.)		
4. Discuss areas in which there is an accounting treatment that could be construed as complex and/or unusual.		
5. Have you encountered any situations in which the government complied with legal minimums of behavior, yet failed to go the extra mile to demonstrate its commitment to the highest ethical standards?		
6. Do you have the freedom to conduct audits as necessary throughout the government?		
7. Were you restricted or denied access to requested information?		
8. Have you been pressured to change findings, or minimize the language in those findings so as to not reflect badly on another member of management? Are findings and recommendations given the level of discussion needed to properly satisfy any issues raised to your satisfaction?		
9. Do you feel comfortable raising issues without fear of retribution?		
10. Is there any activity at any level within the government that you consider to be a significant violation of laws, regulations, contracts or grants, or significant departures from GAAP? Are you aware of any abuse within the government that you would consider to be material?		
11. Have you encountered any situations in which the government complied with legal minimums of behavior, yet failed to go the extra mile to demonstrate its commitment to the highest ethical standards?		

Conducting an Executive Session— Sample Questions		Comments
Controller		
1. Do you believe the financial statements fairly present the government’s net assets and activities in accordance with GAAP or OCBOA?		
2. Do you believe the disclosures are adequate and are understandable to the average user?		
3. If you were the CFO, would you change the financial statements and accompanying footnotes, and, if so, for what reason(s) would you change them?		
4. Are you aware of any current or past occurrence of any type of fraud within the government? Do you know of any situations in which fraud could occur?		
5. Discuss areas in which there is an accounting treatment that could be construed as complex.		
6. Are you satisfied that an appropriate audit was performed by the independent auditors?		
7. Are you aware of any situations of management override of internal controls (as it relates to financial reporting) within the government?		
8. Are you aware of any disagreements between the management of the government and the independent auditors?		
9. Has management set an appropriate “tone at the top” with respect to the importance of and adherence to the internal control system around financial reporting?		
10. Do you feel comfortable raising issues without fear of retribution?		
11. Have you encountered any situations in which the government complied with legal minimums of behavior, yet failed to go the extra mile to demonstrate its commitment to the highest ethical standards?		

Conducting an Executive Session— Sample Questions		Comments
Controller (cont.)		
12. Is there any activity at any level of the government that you consider to be a significant violation of laws, regulations, contracts or grants, or significant departures from GAAP? Are you aware of any abuse within the government that you would consider to be material?		
13. Is there any activity within the government that you are uncomfortable with or consider unusual that would warrant further investigation?		
14. Are there any questions we have <i>not</i> asked that should have been asked? If so, what are those questions? Are there any individuals within or external to the government to whom we should address questions?		
Director of Financial Reporting		
1. Are there any issues since our last meeting that you wish to discuss with the audit committee?		
2. Are you aware of any current or past occurrences of any type of fraud within the government? Do you know of any situations in which fraud could occur?		
3. Discuss areas in which there is an accounting treatment that could be construed as complex.		
4. Are you aware of any situations of management override (as it relates to financial reporting) within the government?		
5. Do you believe the financial statements and related disclosures adequately convey the net assets and activities of the government to an average user?		

Conducting an Executive Session— Sample Questions		Comments
Director of Financial Reporting (cont.)		
6. Now that you have the opportunity, is there anything you want to tell the audit committee? Is there anything else that we need to know? Is there anyone else with whom we should speak?		
7. Are you aware of any disagreements between management of the government and the independent auditors?		
8. Do you feel comfortable raising issues without fear of retribution?		
9. Is there any activity at any level of the government that you consider to be a violation of laws, regulations, contracts or grants, or significant departures from GAAP? Are you aware of any abuse within the government that you would consider to be material?		
10. Is there anything going on within the government with which you are uncomfortable?		
11. Are there any questions we have <i>not</i> asked that should have been asked? If so, what are those questions? Are there any individuals within or external to the government to whom we should address questions?		
General Counsel		
1. Are you aware of any issues that could cause embarrassment or significant public outcry regarding the government's operations?		
2. Have you ever been told anything in confidence or otherwise that would embarrass or cause significant negative publicity for the government if it was known publicly?		

Conducting an Executive Session— Sample Questions		Comments
General Counsel (cont.)		
3. Are you aware of any situations of management override of internal controls (as it relates to financial reporting) within the government?		
4. Are there any items that you have discussed with the chief executive officer (CEO), CFO, other government officials, or outside counsel about which the audit committee is not already aware?		
5. Are you aware of any disagreements between management of the government and the independent auditors?		
6. Do you feel comfortable raising issues without fear of retribution?		
7. Is there any activity at any level within the government that you consider to be a significant violation of laws, regulations, contracts or grants, or significant departures from GAAP? Are you aware of any abuse within the government that you would consider to be material?		
8. Have you encountered any situations in which the government complied with legal minimums of behavior, yet did not go the extra mile to demonstrate its commitment to the highest ethical standards?		
9. Is there any activity within the government that you are uncomfortable with or consider unusual that would warrant further investigation?		
10. Are there any questions we have <i>not</i> asked that should have been asked? If so, what are those questions? Are there any individuals within or external to the government to whom we should address questions?		

Conducting an Executive Session— Sample Questions		Comments
Chief Information Officer		
1. Is there any activity within the government that you are uncomfortable with or consider unusual that would warrant further investigation?		
2. Do you feel comfortable raising issues without fear of retribution?		
3. Are there any questions we have <i>not</i> asked that should have been asked? If so, what are those questions? Are there any individuals within or external to the government to whom we should address questions?		
Conducting an Executive Session—Sample Questions		
Independent Auditors		
<p>Note that certain communications are required between the independent auditors and the audit committee. A separate tool, “Discussions to Expect From the Independent Auditors,” has been prepared for the audit committee to ensure the completeness of the independent auditors’ required communication with the audit committee. These suggested questions are meant to be in addition to the required communications.</p>		
<p>1. Explain the process your firm goes through to assure that all of your engagement personnel are independent and objective with respect to our audit. Particularly, with respect to nonaudit services, how do those services affect the work that you do or the manner in which the engagement team or others are compensated? Are you aware of any anticipated event that could possibly impair the independence, in fact or in appearance, of the firm and any member of the engagement team?</p>		
<i>Comments:</i>		
<p>2. Has management, legal counsel, or others made you aware of anything that could remotely be considered a significant violation of laws, regulations, contracts or grants, or significant departures from GAAP? Are you aware of any abuse within the government that you would consider to be material?</p>		
<i>Comments:</i>		

Conducting an Executive Session—Sample Questions	
<i>Independent Auditors (cont.)</i>	
3. Are there any areas of the financial statements, including, and most important, the notes, in which you believe we could be more explicit or transparent, or provide more clarity to help a user better understand our financial statements?	
<i>Comments:</i>	
4. Have you expressed any concerns or comments to management with respect to how our presentation, including the notes or Management’s Discussion & Analysis could be improved?	
<i>Comments:</i>	
5. Which accounting policies or significant accounting transactions do you think a user would have trouble understanding based on our disclosure? What additional information could (should) we provide?	
<i>Comments:</i>	
6. Based on your auditing procedures, do you have any concerns as to whether management may be attempting to commit management override? Have you noticed any biases as a result of your audit tests with respect to accounting estimates made by management?	
<i>Comments:</i>	
7. In which areas have you and management disagreed?	
<i>Comments:</i>	

Conducting an Executive Session—Sample Questions

Independent Auditors (cont.)

8. Discuss your impressions of the performance of the CAE in terms of the completeness, accuracy, and faithfulness of the financial reporting process.

Comments:

9. Has the firm been engaged to provide any services besides the independent audit of which the audit committee is not already aware?

Comments:

10. How can management improve in terms of setting an appropriate “tone at the top”?

Comments:

11. Describe the ideas you have discussed with management for improving the internal control system over financial reporting.

Comments:

12. Describe for us any situation in which you believe management has attempted to circumvent the spirit of GAAP, but has yet complied with GAAP.

Comments:

Conducting an Executive Session—Sample Questions	
<i>Independent Auditors (cont.)</i>	
13.	Is there anything going on within the government that you are uncomfortable with or consider unusual that would warrant further investigation?
<i>Comments:</i>	
14.	Are there any questions we have <i>not</i> asked that you wish to share with the audit committee?
<i>Comments:</i>	

Other Questions for Management

PURPOSE OF THIS SECTION: It is important for the audit committee to be solidly familiar with the management team, since the committee relies heavily on them. In some large governments, there is an expectation that members of the board will interact with members of management one-on-one on a regular basis. However, such interaction is not always possible. This section lists other questions that the audit committee may wish to address to key members of the financial management team. These questions need not be asked in an executive session, but can be addressed more informally as opportunities arise.

Other Questions for Management	Comments
Chief Financial Officer	
1. Describe your working relationship with the chief executive officer.	
2. If you were the partner-in-charge of the audit, what would you do differently?	
3. Are you aware of any disagreements between management of the government and the independent auditors?	
4. How frequently do you meet with the lead audit partner? Describe your relationship with him or her.	
5. Are you aware of any disagreements between management and the internal auditors?	
6. Describe your relationship with the chief audit executive. Discuss your impressions of his or her performance.	
7. How do you interface with the internal audit function?	
8. Have the independent auditors been engaged for services other than the annual audit about which the audit committee is not already aware?	
9. What significant issues arose from the understanding of the internal control systems?	

Other Questions for Management	Comments
Chief Financial Officer (cont.)	
10. What aspects of the government appear to put the most strain on management? Could any of these aspects significantly strain the government's net assets or activities?	
11. Are the computer systems upon which you rely integrated, or is manual intervention required to integrate your systems?	
12. Which systems are the most difficult to work with?	
13. Are there any new systems or functionality that you would like to purchase but have delayed due to cost considerations?	
14. What procedures or oversight do you apply to manual journal entries that are proposed during the book-closing process?	
15. Do each of the accounting and finance departments of the government have adequate personnel, both in numbers and quality, to meet all their obligations?	
16. What are the most difficult challenges facing the finance department today?	
17. Which departments might benefit the most from additional people resources?	
18. What are the personnel turnover rates in the accounting and finance teams for the last year?	
19. Which of the government's business-type activities caused the largest decrease in net assets in the past year? The biggest increase?	
20. What, if any, changes do you believe need to be made in these areas?	
21. Describe your working relationship with the heads of the respective departments.	
22. What are the biggest obstacles facing the government in the next year? What steps do you think the government should take to address those obstacles?	
23. What are the biggest obstacles facing the government over the long term? What measures do you believe the government should take to address those obstacles?	

Other Questions for Management	Comments
Chief Executive Officer	
1. Discuss your impressions of the performance of the chief audit executive.	
2. Has the independent auditor been engaged for any services other than the annual audit about which the audit committee is not already aware?	
3. What issues arose from the understanding of the internal control systems?	
4. Which of the government’s business-type activities had the largest decrease in net assets this past year? The largest increase?	
5. What, if any, changes do you believe need to be made in these areas?	
6. Describe your working relationship with the heads of the respective departments.	
7. What are the biggest obstacles facing the government in the next year? What steps do you think the government should take to address those obstacles?	
8. What are the biggest obstacles facing the government over the long term? What measures do you believe the government should take to address those obstacles?	
Chief Audit Executive (leader of Internal Audit function)	
1. What procedures do you apply to the review of manual journal entries made during the book-closing process, and to other entries that could be termed as a management override of the internal control system around financial reporting?	
2. If you were the CEO, how would you do things differently in the internal audit department?	
3. Do you believe you have adequate resources available to you to fulfill the charge of the department? If not, what additional resources are needed?	

Other Questions for Management	Comments
Chief Audit Executive (leader of Internal Audit function) (cont.)	
4. Did you encounter any disagreements or difficulties between the internal audit team and the independent auditors in connection with the recently completed audit of the government's financial statements? How will you approach the financial statement audit differently next year?	
5. What critical risks are being monitored by the internal audit team on a periodic or regular basis? How do you address the continuous auditing of these critical risks, and is automation and integrated system reporting assisting you in this effort?	
6. Are you aware of any other disagreements between management of the government and the independent auditors?	
7. Are there any disagreements between the internal audit team and management?	
8. Have the independent auditors been engaged for any services other than the annual audit about which the audit committee is not already aware?	
9. What issues arose from the understanding of the internal control system?	
10. Are the computer systems upon which you rely integrated, or is manual intervention required to integrate your systems?	
11. Do you monitor payments to the independent audit firm to ensure that the audit is only providing services that are related to the audit, or other services that have been preapproved by the audit committee?	
12. Which of the government's business-type activities had the largest decrease in net assets this past year? The largest increase?	
13. What, if any, changes do you believe need to be made in these areas?	
14. Describe your working relationship with the heads of the respective departments.	

Other Questions for Management	Comments
Chief Audit Executive (leader of Internal Audit function) (cont.)	
15. What are the biggest obstacles facing the government in the next year? What steps do you think the government should take to address those obstacles?	
16. What are the biggest obstacles facing the government over the long term? What measures do you believe the government should take to address those obstacles?	
Controller	
1. Have the independent auditors been engaged for any services other than the annual audit about which the audit committee is not already aware?	
2. If you were the partner-in-charge of the audit, what would you do differently?	
3. Discuss your impressions of the performance of the chief audit executive.	
4. Are the computer systems upon which you rely integrated, or does it require manual intervention to integrate your systems?	
5. What procedures do you apply to review manual journal entries proposed during the book-closing process, or to other entries that could be termed as a management override of the internal control system around financial reporting?	
6. Which of the government's business-type activities had the largest decrease in net assets this past year? The largest increase?	
7. What are the biggest obstacles facing the government in the next year? What steps do you think the government should take to address those obstacles?	
8. What are the biggest obstacles facing the government over the long term? What measures do you believe the government should take to address those obstacles?	

Other Questions for Management	Comments
Director of Financial Reporting	
1. How could the financial statements and related disclosures be improved?	
2. Are the computer systems upon which you rely integrated, or is manual intervention required to integrate your systems?	
General Counsel	
1. Discuss your impressions of the performance of the chief audit executive.	
2. Have the independent auditors been engaged for any services other than the annual audit about which the audit committee is not already aware?	
3. Describe your working relationship with the heads of the respective departments.	
4. What are the biggest obstacles facing the government in the next year? What steps do you think the government should take to address those obstacles?	
5. What are the biggest obstacles facing the government over the long term? What measures do you believe the government should take to address those obstacles?	
Chief Information Officer	
1. Are you satisfied with the integrity of the information running through the systems in the government? How could technology improve the integrity of the information?	
2. What exposure is associated with the government's firewalls?	
3. If you had an unlimited budget, how would you spend money to improve the government's information architecture?	
4. What do you consider your critical risk areas?	
5. Describe your relationship with the CFO and other key people in the accounting and finance team.	

Other Questions for Management	Comments
Chief Information Officer (cont.)	
6. Are manual journal entries identified and approved? Are they somehow brought to the attention of the CAE, or other officer(s) that did not have a hand in creating the journal entries?	
7. Is documentation updated every time there is a change to the internal controls process?	
8. Describe your working relationship with the heads of the respective departments.	
9. What are the biggest obstacles facing the government in the next year? What steps do you think the government should take to address those obstacles?	
10. What are the biggest obstacles facing the government over the long term? What measures do you believe the government should take to address those obstacles?	
Independent Auditors	
1. What audit procedures do you apply to manual journal entries that are proposed during the book-closing process, or to other journal entries that could be termed as a management override of the internal control system around financial reporting?	
2. Was any audit work not performed due to any limitations placed on you by management (e.g., any areas scoped out by management, or any restriction on fees that limited the scope of your work)?	
3. Was the audit fee that you charged the government sufficient for the work that you performed?	
4. If you had an unlimited audit fee, what additional work would you have performed?	
5. What are the biggest obstacles facing the government in the next year? What steps do you think the government should take to address those obstacles?	
6. What are the biggest obstacles facing the government over the long term?	

Other Questions for Management	Comments
Independent Auditors (cont.)	
7. What steps do you believe the government should take to address those obstacles?	
Notes	



Points to Consider When Engaging External Resources

PURPOSE OF THIS TOOL: The audit committee of a government organization may, on occasion, need the services of a professional consultant to fulfill its mission. This tool is intended to assist audit committees in understanding the process of engaging external resources when needed.

When selecting external resources for an engagement within the government organization, the audit committee should not only consider the education, training, and experience of the specialists and staff assistants actually performing the work, but it should determine that the service provider (1) maintains integrity and objectivity; (2) is free of conflicts of interest with respect to the members of the audit committee and the government organization; (3) has the expertise and resources necessary to do the work it is under consideration to do; and (4) has a reputation for reliability, among other considerations. The selection of external resources should also follow the procurement policy and procedures applicable to the government organization.

Although the nature of every engagement will be different, the initial steps the audit committee (or its designee) should undertake when engaging external resources include the following:

1. Determine that the expert/adviser has the competence and experience to perform the requested service. Check references with other clients of the service provider.
2. Determine whether the expert/adviser has a conflict of interest with respect to the government organization. Such a conflict might arise if the expert/adviser has a relationship with the external auditor. Depending on the nature of the service to be offered, a conflict could arise if the expert/adviser has a relationship with a member of the governing body, elected officials or a member of the government organization's management. Be aware of other potential conflicts of interest that may distract, or undermine, the work to be done.
3. Determine if the expert/adviser has sufficient resources to perform the work in the time frame specified by the audit committee.
4. Evaluate the scope of work to be performed and other issues, including the proposed plan for payment of fees and expenses.
5. Make sure all parties (including management and the expert/adviser) understand that the audit committee is the owner of the service relationship. Make sure that management understands that the expert/adviser is working on behalf of the audit committee and the audit committee expects management to be fully cooperative and forthcoming with respect to any information that may be requested.
6. Determine the criteria that will be used to measure the expert/adviser work and document those criteria in an agreement with the service provider.

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7. Follow the applicable procurement policy and procedures in obtaining the external resources.
As with any relationship, communication and expectations management is important.



Guidelines for Hiring the Chief Audit Executive

PURPOSE OF THIS TOOL: The internal audit function in a government organization is a key mechanism in the internal control structure. Careful efforts must be taken in hiring the right individual to lead the internal audit team (known as the chief audit executive or CAE), one that fits the government organization's needs with the necessary technical expertise, but also one that meets other requirements (industry experience and competence, independence and temperament, objectivity and integrity, management and human relationship skills, etc.)

Role of the Chief Audit Executive

A critical activity of the audit committee or its equivalent is to be involved in the hiring of the CAE of the government. The audit committee will have to work closely with the CAE, so the committee should be comfortable with this person. In many governments, the CAE will report functionally to the audit committee and may report administratively to a senior executive. Alternatively, the CAE may report directly to the legislative body or its equivalent.

Chief Audit Executive Qualifications

In general, candidates for a CAE position should have distinguished themselves professionally by earning a CPA and/or certified internal auditor credential, significant experience in a management role, and strong technical skills in accounting and auditing. The audit committee should seek candidates who have experience in public accounting (or its equivalent) and possibly an advanced business degree such as an MBA.

Additionally, the AICPA's competency self-assessment tool (CAT) may be a useful exercise for candidates to complete, provided they agree to share results with the audit committee. The CAT is available at <https://www.cpa2biz.com/CPEConferences/CAT.htm>.

INSTRUCTIONS FOR THIS TOOL: The audit committee or its equivalent should consider asking the following questions of candidates who have passed the initial employment screening by either the government’s human resource department or an outside recruiting firm. This tool is meant to prepare the audit committee for the kinds of questions that should be asked of candidates for this important position. Note that some sample questions may not be appropriate for your government. It is also noted that this tool may not be applicable given a government’s charter or other governing provisions.

Chief Audit Executive—Sample Candidate Interview Questions	Interviewer Notes
What do you consider to be internal audit’s role within the government?	
What do you see as the biggest challenges for an internal team in the short run (three to six months), medium term (six to twelve months) and over the next two to three years?	
What experience do you have in government accounting and auditing, and how do you plan to keep abreast of the significant developments relevant to internal audit in government?	
What is your knowledge of the generally accepted government auditing standards (GAGAS)?	
What methodology would you employ to ensure an internal quality control system for recruiting, hiring, training, and evaluating staff, including the continuous monitoring of the effectiveness in policies’ and procedures’ compliance?	
Have you worked with audit committees in the past? What processes have you put in place to keep the audit committee fully and appropriately informed? In the course of a year, what is the typical number of meetings and communications between the CAE and the audit committee (chair)?	

Chief Audit Executive—Sample Candidate Interview Questions	Interviewer Notes
<p>Give some examples of situations you have faced that required special meetings with the audit committee in executive session as a result of disagreements with management. How were these situations resolved with management? Have there been situations in which management has tried to squash your recommendations or discredit your findings, and how did you respond to this? In retrospect, would you now handle these situations differently?</p>	
<p>How would you go about addressing fraud, abuse, or organizational improprieties that come to your attention?</p>	
<p>Have you worked with the Committee of Sponsoring Organizations of the Treadway Commission (COSO) <i>Internal Control—Integrated Framework</i>? How has the framework influenced your process in evaluating the adequacy of internal controls? How is this framework used to design your internal audits?</p>	
<p>In your previous employment, what type of technology platform was used? Have you been involved in a new system (enterprise resource planning or other accounting systems) implementation? What role did you play in the process and how did you make sure that the proper controls were in place when the system went live?</p>	
<p>Have you used technology in conducting internal audits, and how has it enhanced conducting the internal audit? How would you recognize a problem that might exist either in the internal audit data, or in the government's records? What would you do about it?</p>	
<p>Do you use a formal project planning process that is applied consistently for all internal audits? If so, what benefits have you derived in meeting your team's goals and objectives? What is your average report cycle time from the end of fieldwork?</p>	
<p>Have you ever conducted a formal risk assessment, and how have you incorporated it into setting up an audit plan?</p>	
<p>What roles do the government's strategic and technology plans play in the development of an audit plan?</p>	

Chief Audit Executive—Sample Candidate Interview Questions	Interviewer Notes
<p>Have you gone out to departments, divisions, component units, or agencies to ensure that they have significant input into audit objectives and scope? How is this achieved? How have you resolved differences of opinion in this area without compromising the goals you have established for an audit?</p>	
<p>What role have you played in assisting departments, divisions, component units or agencies in implementation of recommendations?</p>	
<p>When you or your team conduct an internal audit, do you have a service orientation to your audit process? Do you work to improve the effectiveness and efficiency of the operations and controls in each audit area? How would you make your recommendations to management? What process would you use to resolve differences of opinion?</p>	
<p>Would you use a process for conducting a customer satisfaction survey after an internal audit is completed? How would you integrate this feedback into future audits?</p>	
<p>How would you ensure that the personnel in internal audit have the necessary skills to ensure an adequate understanding of governmental business?</p>	
<p>How would you ensure that the personnel in internal audit remain independent when reporting internally to management, in fact and in appearance, as prescribed by GAGAS?</p>	
<p>How many people have you managed, either as direct reports, or within an organization that you might have overseen? How would you describe your management style? Have you ever participated in a 360-degree assessment process? If so, what did you learn about yourself that surprised you? How did the results of the assessment change your behavior?</p>	

Chief Audit Executive—Sample Candidate Interview Questions	Interviewer Notes
What is your experience with external peer reviews as prescribed by GAGAS, and how would you incorporate such a process in internal audit?	
What professional training have you participated in regarding organizational ethics?	
<i>Other Notes and Questions:</i>	
Refer to the Government Finance Officers Association (GFOA), Institute of Internal Auditors (IIA), and/or other professional associations for further insight in preparing interview questions for the CAE.	



Guidance for Developing a Request for Proposal for CPA Services (Government Organizations)

PURPOSE OF THIS TOOL: This tool consists of a checklist to be used by the government's audit committee or its equivalent oversight body to ensure the organization's request for proposal is complete and contains the necessary elements for the successful procurement of professional auditing services.

Background

This tool has been prepared to assist a government's audit committee or its equivalent in the preparation or review of a request for proposal (RFP) for professional auditing services, and describes the RFP contents and sample format for said services. As a generic model, it should be used for reference purposes only. A government organization most likely will obtain the services of a team of qualified experts including legal advisers, accountants, internal auditors, procurement officers, and other technical resources to assist in the preparation of an RFP for CPA services.

The preparation of a sound RFP is important. The RFP should outline the proposal and selection process, as well as summarize the background, objectives, expectations, and requirements of the engagement to be undertaken. Therefore, the following should be remembered when writing the RFP:

- Communicate the facts and conditions surrounding the engagement to be completed.
- State your objectives and requirements clearly and thoroughly.
- Be specific about the information needed to properly evaluate the proposal.
- Require the proposal to be presented in a common format to allow for efficient and effective evaluation.

A quality RFP will determine the quality of the respondents and will help to reduce the time and effort expended in the overall RFP and selection process. A quality RFP can be a factor in mitigating potential challenges associated with subsequent contract negotiations.

Because each government is different and unique in its own right, the following is offered as a checklist for government oversight bodies to assess the quality and comprehensiveness of the RFP document for professional auditing services.

Guidelines on the Introduction

The Introduction of the RFP establishes the tone for the proposal document and provides an indication of the scope of work to be performed. The Introduction should accomplish the following:

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- Describe why the RFP is being released. Discuss in general terms the objective to be achieved and the reason professional CPA services are being sought.
- Discuss the term of the engagement, such as the length of time the contemplated contract covers (for example, an annual or a multi-year engagement), along with renewal options.
- Provide an overview of how the RFP is structured and describe what information or supporting documents are contained in the appendixes, attachments, or the body of the RFP document.

Guidelines When Describing the Government Organization

The objective in describing the government organization is to provide an understanding of the composition and makeup of the organizational structure and financial reporting considerations. This information should provide respondents with insight about the possible size and complexity of the work to be performed.

Depending on the information deemed relevant in describing a particular government organization, incorporate the following:

- Year of incorporation
- Charter date
- Form of government
- Term length and term limits for elected officials
- Composition of governing body
- Composition of audit committee
- Population size and other relevant demographics
- Activities and services provided by the government to its citizenry
- Accounting and reporting structure, including chart of accounts or summary description of number and types of funds and account groups
- Accounting systems/software used in accounting and financial reporting activities
- Basis of accounting used in daily operations (for example, generally accepted accounting principles, budgetary basis)
- Component units and joint ventures included in the reporting entity
- Pension plans and actuarial services information
- Additional resource information (for example, budget documents, official statements, annual financial reports, policies and procedures, prior internal or external audits, single audits), along with contact names and numbers to obtain access to this information.

Guidelines on the Scope of Work

This section of the RFP should describe the required services to be provided as a result of this engagement. It should describe the scope of work and any special considerations, such as the following:

- Provide a general description of the services being solicited, including the term of the engagement (for example, number of fiscal year(s) to be audited and related time frame).
- Indicate the exact scope of work to be performed, including the expected deliverables (that is, expressed opinion on the fair presentation of the government's basic financial statements in conformity with generally accepted accounting principles). Specific language should distinguish whether the expected deliverables are to include:
 - An expression of an audit opinion in conjunction with the full-scope audit of a comprehensive annual financial report (CAFR)
 - Audit report on basic financial statements only
 - Single audit report relative to state and/or federal financial assistance programs
 - Quality control reviews (for example, reviews related to financial assistance programs)
 - Management letter indicating deficiencies or opportunities for accounting and reporting improvements, specifically identifying any reportable condition or material weakness
 - Disclosure of irregularities and illegal acts
 - Other reports to be issued or deliverables to be completed
- Include any other special services that may be required of the auditor such as:
 - Reporting on the internal control system based on the auditor's assessment of the structure and control risk
 - Providing continuing education training for the government's staff
 - Conducting performance audits to assess operating effectiveness and efficiency
- Indicate the standards required in performing the auditing services, such as
 - Generally accepted auditing standards as set forth by the American Institute of Certified Public Accountants
 - Standards for financial audits as set forth in the U.S. Government Accountability Office's *Government Auditing Standards (2003)*, known as the Yellow Book
 - Provisions of the *Single Audit Act Amendments of 1996* and the U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*
 - Standards as set forth by local or state charter, code, or other legal mandate

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- Identify any special considerations that will allow the respondent to properly assess the size and complexity of the prospective engagement, for example:
 - Participation in the Government Finance Officers Association (GFOA) Certificate of Achievement for Excellence in Financial Reporting program, which will require a certain level of knowledge and experience to assist governments in achieving this reporting milestone
 - Specific timelines that must be satisfied (for example, CAFR and single audit timeline requirements)
 - Preparation of the entire CAFR and/or certain support schedules (at minimum, any assistance from the auditors must follow the AICPA's *Code of Professional Conduct* and the independence standards as set forth in the U.S. Government Accountability Office's *Government Auditing Standards (2003)*).
 - Assistance in preparing official statements or other documents or disclosures related to sales of debt instruments
 - Foreseeable difficulties that may be encountered as part of the audit process

Guidelines on Proposal Content and Other Submission Requirements

This section should consist of a discussion of specific requirements and parameters to ensure the RFP proposal is submitted successfully. From this information, the respondent should have a clear understanding of what should be included in the proposal, and what steps and timelines must be met for proposal consideration. Ask the respondent, when considering proposal content, to:

- Disclose qualifications and experience of the firm and staff assignment
 - Respondent's experience in providing professional auditing service (for example, prior engagements)
 - Respondent's quality control review reports
 - Partner, supervisory, and staff qualifications and experience for those who are assigned to the specific engagement and the procedures for changing assigned staff during the audit process
 - Audit approach (for example, statistical sampling, analytical procedures, methodology for documenting, EDP use in the auditing process)
- Comply with local, state, or federal statutes and regulations
 - Maintenance of independence as required by U.S. Government Accountability Office's *Government Auditing Standards (2003)*, known as the Yellow Book
 - Adherence to the AICPA's *Code of Professional Conduct*
 - Conflict of interest (for example, ethics ordinance, code of ethics requirements)
 - Assignment of professional services contract to a third party
 - Minority, women, and/or small business participation goals and requirements
 - License requirements to contract and practice public accounting/auditing in a specific locality
 - Other relevant laws and statutes affecting proposal process and submission of the proposal

- Discuss whether subcontracting will be used and to what extent. If joint ventures are permissible, disclose how such business arrangements will comply with RFP requirements.

Additionally, the government should:

- Identify submission criteria for proposals
 - Government contact name(s) and telephone number(s)
 - Address where proposals will be accepted
 - Required number of original and copies of the proposal document to be submitted
 - Whether proposals are to be signed and by whom
 - Submission date and time deadline (including time zone)
 - How proposals are to be delivered (for example, in a sealed package marked plainly)
 - Response format or presentation layout for the proposal (for example, title page, table of contents, transmittal letter, detailed proposal)
- Communicate other information useful to the respondent, such as:
 - Basis on which government organization will/can reject proposals
 - Public information disclosure indicating proposals are subject to open records laws and regulations
 - Costs that will be reimbursed by the government organization, if any
 - Basis for contract termination, including the termination notification process and related timelines
 - Insurance requirements and indemnification clause (for example, liability insurance, workers' compensation)
 - Procedures to handle inquiries from potential RFP respondents

Guidelines on the Schedule of Events and Timelines

Proposal milestones and related timelines should be specifically outlined for complete understandability. This information is often presented in a table format for easy reference. Regardless of the presentation, provide potential respondents with a calendar of proposal events and dates.

Guidelines on the Proposal Evaluation

To complete the body of the RFP document, clearly outline the proposal evaluation process. A properly defined evaluation process promotes consistency and fairness in the selection process and will reduce the time spent assessing the respondents' qualifications and experience. When developing the proposal evaluation process and subsequently completing this section of the RFP document:

- Identify the composition of the selection committee (for example, audit committee)
- Disclose elements of the proposal that will be specifically evaluated (for example, technical experience and expertise)

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- Indicate the methodology for scoring the proposal (for example, point system)
- Outline the steps involved in the selection process
- Incorporate a right-to-reject clause

Appendixes and Attachments

Appendixes and attachments can be used to accompany the body of the RFP in an attempt to provide added relevant information to prospective respondents. Following is a list of information that is often included in the appendixes and/or attachments to RFP documents:

- Glossary
- Organization chart
- List of key personnel, office locations, and telephone numbers
- Recent external and internal audit findings
- Audited financial statements
- Summary budgetary information
- Single audit reports
- Corrective action plans
- Management letters
- Respondent guarantees and warranties
- Format for schedules of professional fees and expenses
- Offering statements
- Excerpts from state and local laws and regulations
- Standard legal language to be included in the audit contract
- Previous listing of schedules prepared by client (PBC)

Conclusion

The RFP is an important step in the selection process. It establishes an opportunity for dialogue regarding a certain set of procurement needs. The previous checklist is not all-inclusive and depends upon a particular government organization and its individual requirements. Therefore, a government organization seeking professional auditing services should employ the help of a team of experts to develop the specific RFP.

For further guidance on developing or assessing an RFP of this type, refer to the following organizations:

- Government Finance Officers Association at www.gfoa.org
- AICPA Audit Committee Toolkit—Sample Request for Proposal for a Public Company at www.aicpa.org/audcommctr
- Institute of Internal Auditors at www.theiia.org

The Internet can be used as a resource to locate RFPs originated by other governments.



Monitoring the Auditor: An Overview of the Peer Review Process

PURPOSE OF THIS TOOL: This tool is intended to educate government audit committee members about how CPA firms and government audit organizations are monitored to ensure that they comply with professional auditing standards in the work they do. This monitoring process is known as the Peer Review Process.

Generally Accepted Government Auditing Standards (GAGAS) requires any CPA firm or government audit organization that performs audits and attestation engagements in accordance with those standards to undergo an external peer review. In fact, CPA firms and government audit organizations must undergo a peer review at least once every three years. This tool will help audit committee members understand the requirements for a peer review, how to interact with the independent auditor concerning peer review results, and why the independent auditor's peer review should be important to an audit committee member.

Peer Review of a CPA Firm and Government Audit Organization¹

A peer review of a CPA firm/government audit organization can be used by an audit committee as a tool to assess whether the government organization's independent auditor:

1. Has a system of quality control that has been designed to meet the requirements of the AICPA's Statements on Quality Control Standards (SQCS) and the U.S. Government Accountability Office's (GAO) Generally Accepted Government Auditing Standards (GAGAS) for the audit and attestation engagements it performs.
2. Is complying with that system of quality control during the peer review year to provide the firm or organization with reasonable assurance of complying with professional standards.

The AICPA's standards regarding quality control provide requirements in the quality control areas of auditor independence, integrity, and objectivity; audit personnel management; acceptance and continuance of audit clients and engagements; audit engagement performance; and firm quality control monitoring. Professional standards include generally accepted auditing standards (GAAS), generally accepted accounting principles (GAAP), GAGAS, and the standards on auditor independence.

A peer review team will be engaged by the CPA firm or government audit organization to perform the review. Each member of the peer review team is required to be independent of the CPA firm or

¹ The term *peer review* is commonly used to describe the formal process for monitoring CPA firms and government audit organizations. The process is also known as a quality control review or quality assessment review. In addition to the AICPA, organizations such as the National Association of Local Government Auditors, National State Auditors Association, and the Institute of Internal Auditors have established review programs for monitoring government audit organizations.

government audit organization and must be qualified to perform the review. The AICPA SQCS and the GAGAS establish the requirements for the peer review team and the conduct of the review. The peer review team will evaluate the firm's or organization's internal quality control policies and procedures and select audits and attestation engagements to evaluate whether the firm or organization followed its internal quality control policies and procedures when performing those engagements. The results of the peer review team's evaluation are submitted in a peer review report.

Peer Review Reports

There are three types of peer review reports: unmodified, modified, and adverse:

1. An *unmodified report* means the reviewed CPA firm's or government audit organization's system of quality control has been designed to meet the requirements of the quality control standards for an auditing practice and the system was being complied with during the peer review year to provide the firm or organization with reasonable assurance of complying with professional standards.
2. A *modified report* means the design of the firm's or organization's system of quality control created a condition in which the firm or organization did not have reasonable assurance of complying with certain professional standards or that the firm's or organization's degree of compliance with its quality control policies and procedures did not provide it with reasonable assurance of complying with all professional standards.
3. An *adverse report* means there are significant deficiencies in the design of the firm's or organization's system of quality control, pervasive instances of noncompliance with the system as a whole, or both, resulting in several material failures to adhere to professional standards on engagements.

Typically, unmodified and modified reports are accompanied by a letter of comments. A letter of comments describes matters that the peer review team believes resulted in conditions in which there was more than a remote possibility that the CPA firm or government audit organization would not comply with professional standards and sets forth recommendations regarding those matters. A letter of comments might not be prepared when an adverse report is issued if all deficiencies, comments, and recommendations are contained in the report itself.

The reviewed CPA firm or government audit organization responds in writing to the peer review team's comments on matters in the peer review report and/or in the letter of comments (called *the letter of response*). The response describes the actions taken or planned with respect to each matter in the report and/or the letter.

We recommend that audit committees request a copy of the auditor's latest peer review report, and any letter of comments and letter of response, if the CPA firm or government audit organization has not already submitted them to the committee. The audit committee should discuss both the report and the letters of comment and response with the auditor. If a report is modified or adverse, the audit committee should discuss the reasons as part of its evaluation of the independent auditor, and to assist in its assessment, where applicable, of whether it should engage or continue to engage the auditor.

Common Misconceptions About Peer Review

1. *Fiction:* A peer review team evaluates every engagement audited by a CPA firm or government audit organization.

Fact: A peer review is performed using a risk-based approach. A peer review team must review enough engagements to obtain reasonable assurance that the reviewed firm or organization is complying with its quality control policies and procedures. Therefore, it is possible that the review would not disclose all weaknesses in the system of quality control or all instances of lack of compliance with it.

2. *Fiction:* An unmodified report provides assurance with respect to every engagement conducted by the firm or organization.

Fact: Every engagement conducted by a firm or organization is not included in the scope of a peer review, nor is every aspect of each engagement reviewed. The peer review includes reviewing all key areas of engagements selected.

3. *Fiction:* If a firm or organization receives a letter of comments, its system of quality control is inadequate.

Fact: The criterion for including an item in the letter of comments is whether the item resulted in the creation of more than a remote possibility that the firm or organization would not comply with professional standards on auditing engagements. Because this is a very low threshold, most peer reviews result in the issuance of a letter of comments.

Questions for the Auditor Regarding Peer Review

The audit committee should consider asking the following questions of its independent auditors to gain a better understanding of the auditors' peer review experience.

Question	Yes	No	Comments
1. Has the CPA firm or government audit organization undergone a peer review within the last three years? If not, please explain.	<input type="checkbox"/>	<input type="checkbox"/>	
2. What do the findings and recommendations in the letter of comments mean?	<input type="checkbox"/>	<input type="checkbox"/>	
3. Is the firm's or organization's letter of response evidence that it is committed to making the changes necessary to improve its practice? If not, please explain.	<input type="checkbox"/>	<input type="checkbox"/>	
4. If the peer review report was modified, explain why.	<input type="checkbox"/>	<input type="checkbox"/>	
5. Did the firm or organization correct the deficiencies noted in either the peer review report or the letter of comments, or both? If not, please explain.	<input type="checkbox"/>	<input type="checkbox"/>	

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Question	Yes	No	Comments
6. Was our government organization selected for review during the peer review? If so, were any negative responses noted?	<input type="checkbox"/>	<input type="checkbox"/>	
7. Was the engagement partner (and other key engagement team members) selected for review during the peer review? If so, were any negative responses noted on audits performed by them?	<input type="checkbox"/>	<input type="checkbox"/>	



Internal Control: A Tool for the Audit Committee

PURPOSE OF THIS TOOL: Internal control over financial reporting has always been a major area in the governance of any organization, and this importance has been magnified in recent years. This tool is intended to give audit committees basic information about internal control to understand what it is, what it is not, how it can be used most effectively in a governmental organization, and the requirements of management with respect to the system of internal control over financial reporting. Note that the primary responsibility of the audit committee with respect to internal control is the system of internal control over financial reporting.

Internal Control Primer—Basics of Internal Control

In 1992, the Committee of Sponsoring Organizations (COSO)¹ of the National Commission on Fraudulent Financial Reporting (also known as the Treadway Commission) published a document called *Internal Control—Integrated Framework*,² which defined *internal control* as “a process, effected by an entity’s board of directors, management and other personnel, designed to provide reasonable assurance regarding the achievement of objectives” in three categories:

1. Effectiveness and efficiency of operations
2. Reliability of financial reporting
3. Compliance with applicable laws and regulations

Internal control can be judged as effective in each of these categories if the board of directors and management have reasonable assurance that:

1. They understand the extent to which the entity’s operations objectives are being achieved.
2. Published financial statements are being prepared reliably.
3. Applicable laws and regulations are being complied with.

The COSO Framework went on to say that internal control consists of five interrelated components as follows:

¹ The Committee of Sponsoring Organizations (COSO) consists of the American Institute of CPAs (AICPA), the Institute of Management Accountants (IMA), the Institute of Internal Auditors (IIA), Financial Executives International (FEI), and the American Accounting Association (AAA).

² The COSO publication *Internal Control—Integrated Framework* (product code number 990012), may be purchased through the AICPA store at www.cpa2biz.com. The proceeds from the sale of the Framework are used to support the continuing work of COSO.

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1. *Control environment.* Sometimes referred to as the “tone at the top” of the organization, meaning the integrity, ethical values, and competence of the entity’s people; management’s philosophy and operating style; the way management assigns authority and responsibility and organizes and develops its people; and the attention and direction provided by the board of directors. It is the foundation for all other components of internal control, providing discipline and structure.
2. *Risk assessment.* The identification and analysis of relevant risks to achieve the objectives that form the basis to determine how risks should be managed. This component should address the risks, both internal and external, that must be assessed. Before conducting a risk assessment, objectives must be set and linked at different levels.
3. *Control activities.* Policies and procedures that help ensure that management directives are carried out. Control activities occur throughout the organization at all levels in all functions. These include activities such as approvals, authorizations, verifications, reconciliations, reviews of operating performance, security of assets, and segregation of duties.
4. *Information and communication.* Components that address the need in the organization to identify, capture, and communicate information to the right people to enable them to carry out their responsibilities. Information systems within the organization are key to this element of internal control. Internal information, as well as external events, activities, and conditions must be communicated to enable management to make informed business decisions and for external reporting purposes.
5. *Monitoring.* The activity undertaken by management and others in the organization with regard to the internal control system. This is the framework element that is associated with the internal audit function in the company, as well as other means of monitoring such as general management activities and supervisory activities. It is important that internal control deficiencies be reported upstream, and that serious deficiencies be reported to top management and the board of directors.

These five components are linked together, thus forming an integrated system that can react dynamically to changing conditions. The internal control system is intertwined with the organization’s operating activities and is most effective when controls are built into the organization’s infrastructure, becoming part of the very essence of the organization.

Note that while the Sarbanes-Oxley Act of 2002, which applies to publicly traded companies, does specifically mention the COSO Framework, the Act acknowledges that this is not the only framework that can be used to fulfill management’s requirements about the internal control system. The Act specifically states that other frameworks may be created either within or outside the United States that may satisfy the intent of the statutes. The Act further states certain conditions that must be met for a framework to be considered suitable. While this Act is not applicable to government organizations, its internal control system intent is equally important to government organizations and should be considered.

An effective internal control structure can actually be part of the competitive advantage of the government organization.

Key Terms in Internal Control

A few terms arise frequently during discussions of internal control, identified and described as follows.

Reportable condition. Has the same meaning as the term *significant deficiency*. These two terms are used to define a significant deficiency in the design or operation of internal control that could adversely affect an organization's ability to record, process, summarize, and report financial data consistent with the assertions of management in the organization's financial statements. An aggregation of significant deficiencies could constitute a material weakness.

Material weakness. Defined in the auditing literature as a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by errors or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned duties.

Compensating controls. Instituted by management to cover for the lack of a basic control, or if a basic control is not able to function for some period of time. They are important for some organizations that, by virtue of their size, are not able to implement basic controls such as segregation of duties.

What Internal Control Cannot Do

As important as an internal control structure is to an organization, an effective system is not a guarantee that the organization will be successful. An effective internal control structure will keep the right people informed about the organization's progress (or lack of progress) in achieving its objectives, but it can neither turn a poor manager into a good one nor ensure success.

Internal control is not an absolute assurance to management and the board about the organization's achievement of its objectives. It can only provide reasonable assurance, due to limitations inherent in all internal control systems. For example, breakdowns in the internal control structure can occur due to simple error or mistake, as well as to faulty judgments that could be made at any level of management. In addition, controls can be circumvented by collusion or by management override. Finally, the design of the internal control system is a function of the resources available, meaning that there must be a cost-benefit analysis in the design of the system.

Roles and Responsibilities

Just as roles and responsibilities vary in each governmental organization, so do the titles of the role-players. While the corporate position titles of chief executive officer (CEO), chief financial officer (CFO), and others are well-defined and understood, their government equivalents are perhaps less well-known. For example, governor, mayor, administrator, and manager are some of the common equivalents to the title and duties of a CEO. Treasurer, clerk, finance director, and controller are often the equivalent of a CFO. For the purposes of this toolkit, the titles normally used in corporate entities will be used for consistency. However, users of the toolkit should realize it is not the title of the position that they should be concerned with, but rather the substance of the duties of the position, recognizing that everyone in the organization has some role to play in the organization's internal control system.

CEO. The CEO has ultimate responsibility and "ownership" of the internal control system. The individual in this role sets the tone at the top that affects the integrity and ethics and other factors that

create the positive control environment needed for the internal control system to thrive. Aside from setting the tone at the top, much of the day-to-day operation of the control system is delegated to other senior managers in the organization, under the leadership of the CEO.

CFO. Much of the internal control structure flows through the accounting and finance area of the organization under the leadership of the CFO. In particular, controls over financial reporting fall within the domain of the chief financial officer. The audit committee should use interactions with the CFO, and others, as a basis for their comfort level on the internal control over financial reporting.

This is not intended to suggest that the CFO must provide the audit committee with a level of assurance regarding the system of internal control over financial reporting. Rather, through interactions with the CFO and others, the audit committee should get a “gut feeling” about the completeness, accuracy, validity, and maintenance of the system of internal control over financial reporting.

Controller. Much of the basics of the control system comes under the domain of this position. It is key that the controller understands the need for the internal control system, is committed to the system, and communicates the importance of the system to all people in the accounting organization. Further, the controller must demonstrate respect for the system through his or her actions.

Internal audit. A main role for the internal audit team is to evaluate the effectiveness of the internal control system and contribute to its ongoing effectiveness. With the internal audit team reporting directly to the audit committee of the governing body and/or the most senior levels of management, it is often this function that plays a significant role in monitoring the internal control system.

Governing body/audit committee. A strong, active governing body is necessary. This is particularly important when the organization is controlled by an executive or management team with tight reins over the organization and the people within the organization. The governing body should recognize that its scope of oversight of the internal control system applies to all three major areas of control: operations, compliance with laws and regulations, and financial reporting. The audit committee is the governing body’s first line of defense with respect to the system of internal control over financial reporting.

All other personnel. The internal control system is only as effective as the employees throughout the organization that must comply with it. Employees throughout the organization should understand their role in internal control and the importance of supporting the system through their own actions and encouraging respect of the system by their colleagues throughout the organization.

Compensating Controls

It is important to realize that both the design and compliance with the internal control system is important. The audit committee should be “tuned-in” to the tone-at-the-top of the organization as a first indicator of the functioning of the internal control system.

In addition, audit committees should realize that the system of internal control should be scaled to the organization. Some organizations will be so small, for example, that they will not be able to have appropriate segregation of duties. The message here is that the lack of segregation of duties is not

automatically a material weakness, or even a reportable condition, depending on the compensating controls that are in place.

For example, suppose an organization's accounting department is so small that it is not possible to segregate duties between the person that does the accounts payable, and the person that reconciles the bank statements. In this case, it is one and the same person, so the implication is that there are no checks and balances on the accounts payable person, who could be writing checks to a personal account, then passing on them during the bank reconciliation process (that is, there is no one to raise the red flag that personal checks are being written on the organization's account).

Compensating controls could make up for this apparent breach in the internal control system. Here are some examples of compensating controls in this situation:

1. All checks are hand signed by an officer, rather than using a signature plate that is in the control of the person that prepared the checks.
2. The bank reconciliation may be reviewed by the person's manager.
3. A periodic report of all checks that are cleared at the bank could be prepared by the bank and forwarded to an officer for review.

Audit committees should be aware of situations like this and be prepared to ask questions and evaluate the answers when an obvious breach in internal control becomes apparent.

Management Override of Controls

Another area that an audit committee needs to focus on is the ability of management to override internal controls over financial reporting to perpetrate a fraud. Examples of techniques used by management in overriding internal controls over the financial reporting function include:

- Approving inappropriate and/or irregular transactions without proper support
- Making adjusting entries during the financial reporting closing process
- Reclassifying items improperly between the statement of financial position and the statement of changes in financial position

Some of these override techniques were used in some of the recent scandals and have gained substantial notoriety.

An audit committee has the responsibility to help prevent or deter a management override of controls. It is important for the audit committee to understand that there is a system to uncover an override, as well as follow-up to determine its appropriateness. Questions about management override, and the controls over management override, as well as audit steps to detect if a management override has occurred, should be addressed to the CEO, CFO, chief audit executive (CAE), and independent auditor during the respective executive sessions with the audit committee as noted elsewhere in this toolkit.

Conclusion

This primer should have given you a sense of what people mean when they refer to *internal control*. The concepts are not complex, but sometimes the application of internal control can be a challenge in an organization, depending on its size and its culture. However, it is vitally important to design the system of internal control to achieve the objectives of (1) effectiveness and efficiency of operations, (2) reliability of financial reporting, and (3) compliance with applicable laws and regulations.

Simply stated, at the end of the day, a strong system of internal control (both in its design and compliance) is good business.

Internal Control—A Tool for the Audit Committee

The following tool, “Internal Control—A Tool for the Audit Committee,” contains questions modeled on those found in the COSO report, *Internal Control—Integrated Framework*.

Internal Control—A Tool for the Audit Committee

PURPOSE OF THIS TOOL: This tool focuses on the five interrelated components of an internal control system, as described in the Committee of Sponsoring Organizations (COSO) *Internal Control—Integrated Framework*³ publication. Refer to “Internal Control Primer—Basics of Internal Control,” earlier in this section for a discussion of the COSO components. The audit committee’s role in the internal control structure in the organization focuses on internal controls over financial reporting and the various systems (human resources, computing, and other) available to support that process, and this tool is created to facilitate that role. The audit committee needs to be assured that the controls are in place and operating effectively. This can be achieved through the committee’s interaction with senior management, independent auditors, internal auditors, and other key members of the financial management team.

INSTRUCTIONS FOR USING THIS TOOL: This tool is created around the five interrelated components of an internal control structure. Within each component is a series of questions that the audit committee should focus on to assure itself that controls are in place and functioning. These questions should be discussed in an open forum with the individuals who have a basis for responding to the questions. The audit committee should ask for detailed answers and examples from the management team, including key members of the financial management team, internal auditors, and independent auditors, to assure itself that the system is operating as management represents. Evaluation of the internal control structure is not a one-time, but rather a continuous event for the audit committee—the audit committee should always have its eyes and ears open for potential weaknesses in internal control and should continuously probe the responsible parties regarding the operation of the system. These questions are written in a manner such that a “No” response indicates a weakness that must be addressed.

³ The questions in this tool are adapted from “Evaluation Tools,” volume 2 of the Committee of Sponsoring Organizations (COSO) 1992 publication *Internal Control—Integrated Framework* (product code number 990012). It may be purchased through the AICPA store at www.cpa2biz.com. The proceeds from the sale of the Framework are used to support the continuing work of COSO.

Control Environment—Tone at the Top	Yes	No	Not Sure	Comments
<i>Integrity and Ethical Values</i>				
1. Does the organization have a comprehensive code of conduct and/or other policies addressing acceptable operating practices, conflicts of interest, and expected standards of ethical and moral behavior?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
2. Is the code distributed to all officials and employees?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
3. Are all officials and employees required to periodically acknowledge that they have read, understood, and complied with the code?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
4. Do elected officials and management demonstrate through actions its own commitment to the code of conduct?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
5. Are dealings with customers, suppliers/vendors, employees, and other parties based on honesty and fair business practices?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
6. Does management take appropriate action in response to violations of the code of conduct?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
7. Is management explicitly prohibited from overriding established controls? What controls are in place to provide reasonable assurance that controls are not overridden by management? Are deviations from this policy investigated and documented? Are violations (if any) and the results of investigations brought to the attention of the audit committee?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
8. Is the organization proactive in reducing fraud opportunities by (1) identifying and measuring fraud risks, (2) taking steps to mitigate identified risks, (3) identifying a position within the organization to “own” the fraud prevention program, and (4) implementing and monitoring appropriate preventative and detective internal controls and other deterrent measures?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	

Control Environment—Tone at the Top	Yes	No	Not Sure	Comments
<i>Integrity and Ethical Values (cont.)</i>				
9. Does the organization use an anonymous ethics and fraud hotline, and, if so, are procedures in place to investigate and report results to the audit committee?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
<i>Commitment to Competence</i>				
1. Are the level of competence and the requisite knowledge and skills defined for each job in the accounting and internal audit functions?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
2. Does management make an effort to determine whether the accounting and internal audit functions have adequate knowledge and skills to do their jobs?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
<i>Governing Body and/or Audit Committee</i>				
1. Are the audit committee's responsibilities defined in enabling legislation or a written policy statement of the governing body? If by policy, is the policy updated annually and approved by the governing body?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
2. Are audit committee members independent of the organization and of management? Do audit committee members have the knowledge, government experience, and financial experience to serve effectively in their role?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
3. Are a sufficient number of meetings held, and are the meetings of sufficient length and depth to cover the agenda and provide healthy discussion of issues?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
4. Does the audit committee constructively challenge management's planned decisions, particularly in the area of financial reporting, and probe the evaluation of past results?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	

Control Environment—Tone at the Top	Yes	No	Not Sure	Comments
Governing Body and/or Audit Committee (cont.)				
5. Are regular meetings held between the audit committee and the chief financial officer (CFO), the chief audit executive (the CAE, the leader of internal audit team), or their government equivalent, other key members of the financial management and reporting team, and the independent auditors? Are executive sessions conducted on a regular basis?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
6. Does the audit committee approve internal audit's annual audit plan?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
7. Does the audit committee receive key information from management in sufficient time in advance of meetings to prepare for discussions at the meetings?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
8. Does a process exist for informing audit committee members about significant issues on a timely basis and in a manner conducive to the audit committee having a full understanding of the issues and their implications?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
9. Is the audit committee informed about personnel turnover in key functions including the audit team (both internal and the independent auditors), senior executives, and key personnel in the financial accounting and reporting teams? Are unusual employee turnover situations observed for patterns or other indicators of problems?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
10. Does the audit committee review qualifications of external auditors and audit scope of service and make appropriate recommendations to the governing body on contracts with external auditors?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
11. Does the audit committee monitor the performance of the external auditors and report as needed to the governing body on performance issues?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	

Control Environment—Tone at the Top	Yes	No	Not Sure	Comments
Management's Philosophy and Operating Style				
1. Is the accounting function viewed as a team of competent professionals bringing information, order, and controls to decision making?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
2. Is the selection of accounting principles made in the long-term best interest of the organization?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
3. Are valuable assets protected from unauthorized access and use?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
4. Do managers respond appropriately to unfavorable signals and reports?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
5. Are estimates and budgets reasonable and achievable?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
Organizational Structure				
1. Is the organizational structure within the accounting function and the internal audit function appropriate for the size of the organization?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
2. Are key managers in the accounting and internal audit functions given adequate definition of their responsibilities?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
3. Do sufficient numbers of employees exist, particularly at the management levels in the accounting and internal audit functions, to allow those individuals to effectively carry out their responsibilities?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
Assignment of Authority and Responsibility				
1. Is the authority delegated appropriate for the responsibilities assigned?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
2. Are job descriptions in place for management and supervisory personnel in the accounting and internal audit functions?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
3. Do senior managers get involved as needed to provide direction, address issues, correct problems, and/or implement improvements?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	

Control Environment—Tone at the Top	Yes	No	Not Sure	Comments
Human Resources Policies and Practices				
1. Are policies and procedures in place for hiring, training, promoting, and compensating employees in the accounting and internal audit functions?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
2. Do employees understand that sub-standard performance will result in remedial action?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
3. Is remedial or corrective action taken in response to departures from approved policies?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
4. Do employees understand the performance criteria necessary for promotions and salary increases?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
Risk Assessment				
1. Does the organization consider risks from external sources such as creditor demands, economic conditions, laws and regulations, bond covenants, labor relations (e.g., unions), etc.?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
2. Does the organization consider risks from internal sources such as key employees (retention and succession planning), financing and the availability of funding for key programs, competitive compensation and benefits, information systems security, and backup systems?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
3. Is the risk of a misstatement of the financial statements considered and are steps taken to mitigate that risk?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
Control Activities				
1. Does the organization have a process in place to ensure that controls as described in its policy and procedures manuals are applied as they are meant to be applied? Do the policy and procedures manuals document all important policies and procedures? Are these policies and procedures reviewed and updated on a regular basis? If so, by whom?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	

Control Environment—Tone at the Top	Yes	No	Not Sure	Comments
Control Activities (cont.)				
2. Do supervisory personnel review the functioning of controls? If so, how is that review conducted and what happens to the results? Is appropriate and timely follow-up action taken on exceptions?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
Information and Communication				
1. Is a process in place to collect information from external sources, such as economic and regulatory information, that could have an impact on the government and/or the financial reporting process?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
2. Are milestones to achieve financial reporting objectives monitored to ensure that deadlines are met?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
3. Is necessary operational and financial information communicated to the right people in the organization on a timely basis and in a format that facilitates its use, including new or changed policies and procedures?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
4. Is a process in place to respond to new information needs in the organization on a timely basis?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
5. Is there a process in place to collect and document errors or complaints and to analyze, determine cause, and eliminate a problem from recurring in future?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
6. Is a process established and communicated to officials, employees, and others, about how to communicate suspected instances of wrongdoing by the government or its employees? Further, does a process exist to ensure that anyone making such a report is protected from retaliation for making such a report?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	

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Control Environment—Tone at the Top	Yes	No	Not Sure	Comments
Monitoring				
1. Do elected officials, other officials, upper management, and other employees understand their obligation to communicate observed weaknesses in design or compliance with the internal control structure of the organization to the appropriate supervisory or management personnel?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
2. Are interactions with external stakeholders periodically evaluated to determine if they are indicative of a weakness in the internal controls structure? (For example, consider the frequency of customer complaints about incorrect bills or correspondence regarding noncompliance from granting or oversight agencies.)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
3. Is there follow-up on recommendations from the internal and external auditors for improvements to the internal control system?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
4. Are personnel asked to periodically state whether they understand and comply with the organization’s code of conduct?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
5. Are personnel required to sign off, indicating their performance of critical control activities such as performing reconciliations?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
6. Does the internal audit team have the right number of competent and experienced staff? Do team members have access to the governing body and audit committee? Is the reporting structure in place to ensure their objectivity and independence? Is the work of the internal audit team appropriate to the organization’s needs, and prioritized with the audit committee’s direction?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	




Fraud and the Responsibilities of the Government Audit Committee

PURPOSE OF THIS TOOL: A government audit committee should take an active role in the prevention, deterrence, and detection of fraud and encourage the government organization to establish an effective ethics and compliance program. The government audit committee should constantly challenge management and the auditors to ensure that the organization has appropriate antifraud programs and controls in place to identify potential fraud, and, that investigations are undertaken if fraud is detected. Also, the committee should take an interest in ensuring that appropriate action is taken against known perpetrators of fraud.

This tool is intended to make government audit committee members aware of their responsibilities as they undertake this important role. It highlights areas of activity that may require additional scrutiny by the audit committee.

Introduction

Historically, the audit committee has been associated with the private sector and, in particular, publicly traded companies. With the recent occurrence of a number of high profile corporate fraud scandals and resulting passage of the Sarbanes-Oxley Act of 2002, audit committees' roles and responsibilities have been greatly elevated, discussed, and scrutinized. The Act's audit committee requirements were intended for publicly traded companies. A halo effect has occurred, however, transferring to the public sector much of the same corporate concern over fraud and ethics. This, in turn, has spawned a renewed interest in *government* audit committees. Although audit committees and their equivalents may differ widely, both within their own level of government and among the local, state, and federal levels, certain responsibilities and expectations concerning fraud prevention, deterrence, and detection are pervasive nonetheless.

The June 2003 revision of *Government Auditing Standards* (GAS) issued by the Comptroller General of the United States through the Government Accountability Office (GAO—formerly General Accounting Office) and known as the Yellow Book, recognizes the melding of AICPA standards and GAS concerning fraud in paragraph 5.17 stating, “AICPA standards and GAGAS¹ require auditors to address the effect fraud or illegal acts may have on the audit report and to determine that the **audit committee or others with equivalent** [emphasis added] authority and responsibility are adequately informed about the fraud or illegal acts.” This section also links the government audit committee or its equivalent to fraud responsibility.

Also the AICPA issued Statement on Auditing Standards (SAS) No. 99, *Consideration of Fraud in a Financial Statement Audit* (AICPA, *Professional Publications*, vol. 1, AU sec. 316), which details the responsibilities and functions of the auditor as they relate to fraud in an audit of financial statements.

¹ The terms GAS, for *Government Auditing Standards*, and GAGAS, for Generally Accepted Government Auditing Standards are used interchangeably here. Further, both are synonymous with the term Yellow Book, as noted.

The Statement gives new and expanded guidance for identifying and assessing the risks of material misstatement due to fraud; evaluating and documenting evidence; and communicating to management, the audit committee, and others.

Definition and Categories of Fraud

An understanding of fraud is essential for the audit committee to carry out its responsibilities. The term *fraud* is defined in *Black's Law Dictionary* (Sixth Edition, 1990) as:

An intentional perversion of truth for the purpose of inducing another in reliance upon it to part with some valuable thing belonging to him or to surrender a legal right. A false representation of a matter of fact, whether by words or by conduct, by false or misleading allegations, or by concealment of that which should have been disclosed, which deceives and is intended to deceive another so that he shall act upon it to his legal injury. . . A generic term, embracing all multifarious means which human ingenuity can devise, and which are resorted to by one individual to get advantage over another by false suggestions or by suppression of truth, and includes all surprise, trick, cunning, dissembling, and any unfair way by which another is cheated.

Categories of Fraud

The audit committee needs to be aware that fraud affecting the organization often falls into one of two categories:

- *Internal fraud* involves activities perpetrated within the organization such as intentional misrepresentation of financial statements or financial statement transactions, theft, embezzlement, or improper use of the organization's resources.
- *External fraud* involves theft or improper use of the organization's resources perpetrated by individuals outside the organization. Some examples of external fraud prevalent in the government arena include false claims and statements, beneficiary fraud, and contract and procurement fraud.

This categorization of fraud is useful but not absolute. For example, an organization's employees may collude with outside individuals to procure contracts or provide goods and services (that is, kickbacks).

Fraud and the Responsibilities of the Government Audit Committee or Its Equivalent

The members of the government audit committee should understand their role of ensuring that the organization has antifraud programs and controls in place to help prevent fraud and to properly fulfill their fiduciary duties of:

- Monitoring the financial reporting process.
- Overseeing the internal control system.
- Overseeing government auditors and public accounting firms engaged to perform government audits.
- Reporting findings to the legislative body or other independent governing body.

Fraud can be a catastrophic risk to a government organization. If the organization does not identify and monitor fraud, the results can be devastating to the organization's financial position, reputation, citizens' confidence level, and success in achieving its goals and objectives.

Setting the tone to reduce the risks of fraud begins with the governing body. Depending on the type of government organization that will be applying these concepts, the governing body can consist of a legislative body, council, supervisory board, or any designee approved by that government as the responsible party for ensuring the accountability of public resources.

Create an Environment to Reduce Risk of Fraud

Often, a government organization's elected officials and management must adhere to a code of ethics, or choose to establish one in the absence of a legal requirement to do so. An audit committee can help the governing body provide the guidance necessary to create a culture of honesty and integrity in preventing, deterring, and detecting fraud. It is important to clearly communicate to each employee acceptable behavior and expectations that foster an environment where the risks of fraud are reduced. Such a culture is rooted in a strong set of core values that provides the foundation for employees as to how the organization conducts business. It also allows an organization to develop an ethical framework that discourages (1) fraudulent financial reporting, (2) misappropriation of assets, (3) circumventing internal controls, and (4) other forms of corruption.

An ethical framework should include:

- A code of ethics that is based on the organization's core values and that clearly states acceptable and unacceptable behaviors.
- A training program for its code of ethics that includes sessions for new hires, management, and newly elected officials, and continuing education for all employees and officials.
- An adequate channel of communication for employees and others to obtain advice when facing difficult ethical decisions and the reporting of known or potential unlawful activities against the government organization.
- A system to monitor compliance with the code of ethics.

Establish Antifraud Programs and Internal Controls

The audit committee should ensure that the government organization establishes antifraud programs and internal controls to help prevent and detect fraud. To meet its responsibilities, the audit committee should ensure that the government organization has:

- Designated a senior level member of the government organization to manage fraud risk.
- Established policies and procedures that identify, evaluate, and mitigate the organization's fraud risk exposure.
- Maintained an effective internal control structure designed to prevent, deter, and detect fraud.
- Created a system to monitor compliance with policies and procedures and controls.

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- Established and communicated the process for reporting potential fraudulent activities, for example, fraud hotline, Web site address, suggestion box, or tracking report.
- Developed a process for investigating potential unlawful activities against the organization.

When Fraud Is Discovered

Many large government organizations have a structure for reporting potential fraud and resources available such as an audit or investigative function that gathers the evidence and coordinates with appropriate law enforcement agencies. With this structure, the government audit committee should ensure that a process is in place to receive periodic reports describing the nature, status, and eventual disposition of any fraud investigations.

With smaller government organizations, the audit committee may be directly responsible for overseeing the investigation of a potential fraud. In this circumstance, if fraud is discovered, or there is a reasonable basis to believe that fraud may have occurred, the audit committee is responsible for ensuring that an investigation is undertaken. The committee should retain professionals with experience and training in fraud investigations. Professionals such as internal or external auditors, forensic accountants, legal counsel, and law enforcement officials can provide the expertise to assist with the investigation. The audit committee should stay informed on the progress of the investigation to its conclusion.

Accounting and auditing professionals may also provide audit committees with other related services, for example, (1) evaluation of controls and operating effectiveness through compliance verification, (2) creation of special investigation units (SIUs), (3) incident management committees, (4) assessment of risks, (5) ethics hotlines, (6) and code of conduct.

Government Auditors

Government auditors can serve a vital role in aiding the audit committee in determining whether the government organization is achieving its goals and objectives. Auditors that are experienced and trained in fraud prevention, deterrence, and detection can help provide assurance that the government organization's risks are effectively identified and monitored; processes are effectively controlled and tested periodically; and appropriate follow-up action is taken to address control weaknesses. If the government organization does not have an audit or oversight function trained in fraud prevention, deterrence, and detection, the organization may consider contracting with an audit firm for specialized accounting/auditing services.

The audit committee needs to ensure that the auditors are fulfilling their responsibilities in deterring potential fraud by following applicable professional standards. *Government Auditing Standards* and AICPA Statements on Auditing Standards require auditors to assess the risk of material misstatements of financial statement amounts or other financial data significant to the audit objectives due to fraud and to consider that assessment in designing the audit procedures to be performed. Specifically, SAS No. 99 addresses auditor responsibilities in planning and performing financial statement audits, including the requirement that fraud involving senior management, and any fraud (whether caused by senior management or other employees) that causes material misstatement of the financial statements, should be reported directly to the audit committee.

Whistleblowers

Many federal, state, and local government organizations have whistleblower laws and regulations. These regulations may require the organization to establish procedures for the confidential receipt, retention, and treatment of complaints received regarding suspected fraudulent activities. The audit committee should ensure that the organization has established a process to address applicable whistleblower laws and regulations.

Conclusion

The demands of the public, U.S. corporations, and the regulatory environment have focused attention on the increased need to fight fraud. The public is demanding greater vigilance from all parties involved in organizational governance. Audit committees are required to play a pivotal role in the prevention of fraud and to take appropriate action in the discovery of fraud. Government auditors can provide additional assistance to audit committees so they may better carry out their fiduciary responsibilities in fighting fraud and protecting the public interest.

Other Information

To obtain more information on fraud and implementing antifraud programs and controls, please visit the following Web sites where additional materials, guidance, and tools can be found:

American Institute of Certified Public Accountants	www.aicpa.org
AICPA Antifraud & Corporate Responsibility Resource Center (including SAS No. 99)	www.aicpa.org/antifraud/homepage.htm
Association of Certified Fraud Examiners	www.cfenet.com




Management's Summary of Unique Transactions and Financial Relationships

PURPOSE OF THIS TOOL: Some transactions and financial relationships put a government organization at greater financial risk. Generally accepted accounting principles (GAAP) for governments provide guidance about how a government organization should account for and report these transactions and relationships as a means to fully inform the government organization's constituents. It is important that the audit committee understand the nature and the reason for these transactions and relationships, and ensure that management adequately discloses them in its financial statements. This tool is intended to assist audit committee members in gaining an understanding of management's use of certain unique transactions and relationships so they may weigh in on the appropriateness of the treatment and whether it will meet the government organization's objectives for public accountability.

Some transactions and financial arrangements put a government organization at greater financial risk. The audit committee should be aware of these transactions, relationships, and circumstances that may require recognition in the government organization's financial statements and should ensure that those transactions and events have been accounted for properly. Some of the more common of these transactions and relationships that the audit committee should be aware of are:

1. Investments in derivative financial instruments
2. Securities lending transactions
3. Relationships with legally separate entities
4. Joint ventures with other governments or organizations

The following information provides background about these types of transactions and relationships.

Derivatives

A government organization's investment policies, when allowed by laws or regulations, may allow investments in financial instruments that are not routine or actively traded in the market. Routine or actively traded financial instruments, such as repurchase agreements, government agency debt securities, and money market funds, have some degree of risk. Derivatives, however, which are financial instruments or contracts that have unique characteristics underlying their ultimate investment yield, typically have much greater risk.

If a government organization holds derivatives, these financial instruments are included in the amount of investments reported in the government's financial statements, preferably at the instrument's market value, referred to as its fair value. Because the derivative's fair value may not be actively traded in the market, or may be based on complicated, unknown events, the derivative might not be

reflected in the financial statements at its fair value. In these cases, the notes to the financial statements should discuss the following:

- The significant terms, associated debt, and objectives of the derivative
- Level of exposure to the various risks, such as credit risk, interest rate risk, basis risk, termination risk, rollover risk, and market access risk

Government Accounting Standards Board (GASB) Technical Bulletin 2003-01, *Disclosure Requirements for Derivatives Not Reported at Fair Value on the Statement of Net Assets* provides more information about reporting derivatives that are not reported at fair value in the financial statements.

Securities Lending Transactions

Sometimes, government organizations have large amounts of long-term investments in their portfolios. If a government organization wants to earn additional income, it might lend some securities to brokers or financial institutions that need to borrow those securities to cover a short position (that is, they sold a security without owning it) or to avoid a failure to receive a security they purchased for delivery to a buyer. In these transactions, the government organization transfers their securities for collateral, which may be cash or other securities, and agrees to return the collateral for their original securities at some time in the future.

When a government organization lends its securities, it still reports these securities as investments in its financial statements. If the government organization receives cash as collateral on the securities lending transactions, makes investments with that cash, or can sell the securities it received as collateral, these amounts are also reported as assets in the financial statements. Of course, because the collateral must be returned in the future, the government organization also reports a liability for these transactions in the financial statements. In addition, the notes to the financial statements should explain:

- The legal or contractual authorization for the use of securities lending transactions, and any significant violations of those provisions
- Whether the maturities of the investments made with cash collateral generally match the maturities of the securities loaned
- Summary information about the credit risk associated with the transactions
- General information about the types of securities lent, the types of collateral received, and whether the government has the ability to sell collateral securities.

GASB Statement No. 28, *Accounting and Financial Reporting for Securities Lending Transactions*, provides specific guidance on accounting and reporting for securities lending transactions.

Relationship with Legally Separate Entities

The structure of many government organizations has become increasingly complex. For a variety of reasons, many government organizations create legally separate organizations. Some of the more common reasons include greater efficiency in financing and administering debt backed by revenue-generating activities, providing additional services that may not have been envisioned when the

charter or statute was written, and overcoming constitutional or statutory limitations on the issuance of debt or other financial resources. Whatever the reason, financial reporting for public accountability requires determining which of these organizations should be included as part of a government organization's financial reporting entity.

Although detailed and complex analyses ultimately determine which legally separate organizations should be included in a government organization's financial reporting entity, these organizations are generally included if the government organization appoints a voting majority of an organization's governing board and is either:

- Able to impose its will on that organization, or
- The organization provides specific financial benefits to or imposes specific financial burdens on the government organization.

Organizations with a separately elected governing body may also be included in a government organization's financial reporting if that organization is fiscally dependent on the government organization, or the organization's resources are available or promised for the government organization's use.

If a legally separate organization should be included in a government organization's financial reporting entity, the financial statements of the legally separate organization will be included in the government organization's financial statements, usually in a column separate from the government. Notes to the financial statements also explain why the organization is included, and any significant transactions between the government and the separate organization.

GASB Statements No. 14, *The Financial Reporting Entity*, and No. 39, *Determining Whether Certain Organizations Are Component Units*, provide specific guidance on financial reporting under such circumstances.

Joint Ventures

Sometimes, a government organization decides to pool resources and share the costs, risks, and rewards of providing goods or services with other governments or organizations for the benefit of the general public or specific service recipients. This arrangement, known as a joint venture, is a legal entity that results from a contractual arrangement between a government entity and another government or organization. In a joint venture such as this, each of the participants retains an ongoing financial interest or an ongoing financial responsibility.

For financial reporting purposes, there are two types of joint ventures:

- Joint ventures whose participants have equity interests
- Joint ventures whose participants do not have equity interests

If the government has an equity interest in the joint venture, that equity interest should be reported

- as an asset in the government organization's government-wide financial statements

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- as a receivable from or payable to the joint venture in the fund financial statements of the governmental fund that has the equity interest, and
- as an asset in the fund financial statements of the proprietary fund that has the equity interest

GASB Statement No. 14, as amended by GASB Statement No. 34, *Basic Financial Statements—and Management’s Discussion and Analysis—for State and Local Governments*, provides guidance on joint ventures and other, similar arrangements, such as undivided interests and cost-sharing arrangements.

It is important that the audit committee have a healthy and continuing dialogue with management about these kinds of transactions and relationships. In doing so, the following are some questions that should be regularly asked of management:

Audit Committee Questions of Management		Notes
Derivatives		
1. Describe the government organization’s policies for investing in derivative financial instruments. Are there any restrictions as to the type, maturity length, or percentage of total portfolio?		
2. Describe how management has valued its derivatives for financial statement presentation. Discuss the types of credit risk, interest rate risk, or other risk these investments have and how management has decided to manage those risks.		

Management’s Summary of Unique Transactions and Financial Relationships

Audit Committee Questions of Management		Notes
Securities Lending		
3. Describe the government organization’s policies for entering into securities lending agreements, including the legal authority to do so.		
4. Describe how any securities lending transactions have been accounted for and whether they have been included in the government’s financial statements. Include whether collateral can be used to purchase securities, whether maturities of original and collateral securities match, and the credit risk associated with the securities.		
Legally Separate Entities		
5. Has the government organization created, authorized, or become aware of any legally separate organizations that have financial relationships with the government organization (e.g., flood control, public works, library, jail, assessment, lighting, or other special purpose districts; capital or property financing authorities; fund-raising organizations)? If so, please provide details.		

Audit Committee Questions of Management		Notes
Legally Separate Entities (cont.)		
6. For any such organizations, describe who appoints its government body, whether the government organization can impose its will on the organization or receive a financial benefit or burden from the organization, and whether the organization is fiscally dependent upon the government organization. Also explain if and how such organizations are displayed and disclosed in the government’s financial statements.		
Joint Ventures		
7. Has the government organization entered into any agreement with another government or organization to share resources, cost, and risks for providing goods and services to the general public or specific recipients? If so, please describe the details of the arrangement.		
8. For any such agreements, please describe how the government organization accounts for its participation and how the effects of such participation are displayed or disclosed in the government’s financial statements.		



Issues Report From Management

PURPOSE OF THIS TOOL: This tool is to be used by audit committees in considering significant issues, estimates, and judgments that may have a material impact on the government organization's financial statements and operations. Management should be encouraged to use this tool as a means to document any significant issues, judgments, and estimates for discussion with the audit committee. Each matter should be prepared as a separate issues report. Statements should be clear and concise. Some issues may carry over to subsequent meetings, in which case, any updated information should be included in bold.

Defining Significant Issues, Estimates, and Judgments

As a first step to any discussion of this nature among the audit committee members, it is important for the audit committee to define its threshold for a significant issue, estimate, and judgment. The following are some points that the audit committee should consider in its quest to define a significant issue, estimate, and judgment.

A significant issue, estimate, or judgment is one that:

1. Creates controversy among members of the management team, or between management and the internal or independent auditors.
2. Has or will have a material impact on the financial statements and/or operations.
3. Is or will be a matter of public interest or exposure.
4. Must be reported to an external body and management is unclear or undecided on its presentation, for example, single audit findings, grants, public requests for disclosure, or bond issuances.
5. Applies a new accounting standard. (*Note:* the application of a new accounting standard may or may not be considered a significant issue, estimate, or judgment for the organization. However, for the record, the audit committee may ask management to use this format as a means to brief the audit committee on the application of the new standard.)
6. Relates to the application of a standard in a way that is not consistent with general practice.
7. Relates to key controls over financial information that are being designed or redesigned, have failed, or otherwise are being addressed by the organization.

The audit committee needs to be proactive and consistent in its inquiries regarding significant issues, estimates, and judgments. At each meeting, the audit committee should inquire about current and/or unresolved issues or problems that have arisen in the financial, compliance, or operational control environment. Management's response should be documented in the meeting minutes.

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Management's report to the audit committee concerning significant issues, estimates, and judgments should contain the following elements for a proper basis of discussion by the audit committee:

1. *Define the significant issue, estimate, or judgment.* In this section of the issues report, management should define/summarize the issue as concisely and clearly as possible.
2. *Management's position.* This section should address management's position on the issue. If there is disagreement among members of management, those disagreements should be identified here as explicitly as possible, with brief explanations of why each member of the management team has taken his or her position.
3. *Relevant literature.* Any professional literature or regulatory requirements addressing this issue should be cited here. If there is no professional literature available, it would be appropriate to define the governmental practice in this space. If this is a developing area, and there is no accepted best practice or other sources to support or refute these positions, this fact should be reported. If there is a choice of accounting treatments, that should be disclosed here along with a discussion on how the choices of treatment were compared and the basis for the final choice made.
4. *Risks.* Management should identify various risks (both good and bad) associated with this proposal.
5. *Regulatory disclosure.* Management must inform the audit committee of how it intends to address any required disclosures to appropriate regulatory bodies as required by law.
6. *Auditors' position.* Has management consulted with the internal and external auditors on this issue? Do they agree with management's position? Has management addressed the audit issues that might be associated with it? If so, use this section of the issues report to discuss the internal and external auditors' positions. If not, use this section to explicitly state that the auditors have not been consulted.
7. *Other information relating to this issue, estimate, or judgment.* Management should use this section of the issues report to highlight other related and relevant information that is not already included in the previous sections.

INSTRUCTIONS FOR USING THIS TOOL: Management should be encouraged to use this tool as a means to document any significant issues, estimates, and judgments for discussion with the audit committee. Each matter should be prepared as a separate issues report. Statements should be clear and concise. Some issues may carry over to subsequent meetings, in which case, any updated information should be included in bold.

Issues Report to the Audit Committee

1. *Define the significant issue, estimate, or judgment.* Following is a summary of a significant issue, estimate, or judgment in the view of management.
2. *Management's position.* Management's position on this matter is as follows. Any disagreements are highlighted here as well.
3. *Relevant literature.* The following professional literature, regulatory requirements, and/or industry best practice support management's position. Other background is provided as needed (area of developing practice, choice of accounting treatment, basis of decision, etc.).
4. *Risks.* Management has identified the following risks (good and bad) associated with this proposal.
5. *Regulatory disclosure.* Management must inform the audit committee of how it intends to address any required disclosures to appropriate regulatory bodies as required by law.
6. *Auditor's position.* Management [*has/has not*] consulted with the internal and external auditors on this issue. The auditors [*do/do not*] agree with the management's position. Management [*has/has not*] addressed the audit issues that might be associated with its position. The following further discusses the auditor's position. If management has not discussed this issue with the auditor(s), a declaration to that affect is included below.
7. *Other information relating to this issue, estimate, or judgment.* Included in the following is further information not included in the preceding sections.

Sample Issues Report From Management

1. Define the significant issue, estimate, or judgment. Management is concerned with the inability to accurately estimate its health care costs at year end. At any given time, including year end, the most difficult estimate related to those costs is what is known as claims that are incurred but not reported (IBNR). Plan participants have received treatment from health care providers and incurred liabilities that have not yet been billed to the government's self-funded plan for payment. The government uses a third-party administrator (TPA) to pay the claims and to actuarially estimate what the IBNR is at year end. Generally, about 80 percent of these expenses will be paid during the first three to four months after the end of the plan year. Because of recent changes in the TPA's billing system, changes in the demographic makeup of the government's participant base, and an unusual increase in the number of large dollar claims, the IBNR estimate/accrual was significantly underestimated. This has caused the fund, which is funded by employer and employee contributions, to experience unexpected deficits in recent years.
2. Management's position. The government has covered these deficits through general fund transfers. Management plans to request that the TPA carefully review the actuarial assumptions used to compute the IBNR, determine the cause of the shortage, and identify how to improve the accuracy of the IBNR estimate. Management is also considering creating a reserve to handle such fund fluctuations caused by the IBNR and considering adding stop-loss insurance coverage to the self-funded plan to mitigate the effects of unusually large claims. Stop-loss coverage insures the self-funded plan for claims exceeding a certain dollar amount (\$100,000 is typical). The premiums for this coverage are paid from the fund but protect it against the negative effects of catastrophic claims and help in the IBNR estimate.
3. Relevant literature. The government's TPA agreement for its self-funded health plan contains the required computation of the IBNR. Creating a reserve is *not* a legal requirement, therefore, there is no regulatory literature regarding this issue. There is a variety of actuarial and industry literature concerning the computation of the IBNR and reserve issues.
4. Risks. Underestimating the IBNR can cause administrators of the plan to misread the true profitability and solvency of the plan. This may delay the recognition of emerging claim and demographic trends as well as cause administrators to make faulty decisions in setting unrealistic rates and employee/employer contribution amounts needed to cover the plan's expenses. If the true IBNR paid out over the ensuing months is much greater than estimated amounts accrued, other sources of revenue must be called upon to bail the fund out, causing budget difficulties and ill will elsewhere in the organization.
5. Regulatory disclosure. None.
6. Auditor's position. Management has held informal discussions with the auditors on this issue. The auditors are in full support of management's position to have the TPA review its actuarial assumptions for calculating the IBNR, create a reserve in the fund to handle fluctuations due to the inexact nature of IBNR estimates, and negotiate a stop-loss policy for the self-funded plan that will hedge against the effects of unanticipated large catastrophic claims.

7. Other information relating to this issue, estimate or judgment. While exploring the possibility of creating a reserve, it is important to remember the difference between a reserve and a contingency. A contingency is set up for an event that has not, and in fact may never occur. For a contingency to be accruable it must be both probable and reasonably estimable. The IBNR reserve, on the other hand, is for events that have already occurred and, therefore, is not a contingency and must always be accrued. Because we do not know the exact amount of the liability we must use our best estimate.

Issues Report From Management

1. Define the significant issue, estimate, or judgment.
2. Management's position.
3. Relevant literature.
4. Risks.
5. Regulatory disclosure.
6. Auditor's position.
7. Other information relating to this issue, estimate or judgment.



Discussions to Expect From the Independent Auditors

PURPOSE OF THIS TOOL: Auditing standards¹ require that the auditor communicate, either orally or in writing, certain information to an audit committee of the board, or another designated party that performs oversight of the financial reporting and audit process. This section discusses the type of information independent auditors are required to communicate to an audit committee or other oversight body.

Independent Auditors in the Public Sector

Communications with audit committees have now engendered more legal and regulatory scrutiny. Independent auditors, in the wake of well-documented business failures and new regulatory oversight, are required to increase their documentation and communication efforts as they relate to their interactions with the audit committee. Independent auditors of government organizations may include an elected or appointed auditor or Inspector General or an independent public accounting firm. In addition, at the federal level the Government Accountability Office (GAO—formerly the General Accounting Office) may be statutorily required to act as the independent auditor in certain circumstances. If an independent public accounting firm is used as the independent auditor, it is often required to be under contract with the elected or appointed auditor or Inspector General. The communication guidance discussed in this section relates to whichever of the above parties is acting as the independent auditor.

Auditor's Responsibility Under Generally Accepted Auditing Standards

It is important for audit committees to understand what an audit is and what it is not. Usually, audit committees are most concerned about the system of internal control and that the financial statements are free of material misstatement. The auditor should make sure the audit committee understands the level of responsibility that the auditor assumes for the system of internal control and the financial statements under generally accepted auditing standards (GAAS). It is also important that the auditor makes sure that the audit committee understands that an audit is designed to obtain reasonable rather than absolute assurance about the financial statements.

¹ The term “auditing standards” refers to generally accepted auditing standards (GAAS) issued by the AICPA. These standards are incorporated into government auditing standards (GAS or GAGAS) issued by the Comptroller General of the United States. These terms are also synonymous with the term “Yellow Book.” In addition, OMB Bulletin No. 01-02, *Audit Requirements for Federal Financial Statements*, Section 5 requires open and timely communication between agency management, including the CFO, and the Inspector General (and the audit firm if the audit is contracted out) throughout the audit process. The guidance in this tool is based on Statements on Auditing Standards (SAS) No. 61, *Communication With Audit Committees*, as amended; No. 60, *Communication of Internal Control Related Matters Noted in an Audit* (AICPA, *Professional Standards*, vol. 1, AU sec. 325) as amended; and No. 54, *Illegal Acts by Clients* (AICPA, *Professional Standards*, vol. 1, AU sec. 317), and amendments thereto, which are in effect as of this writing and *Government Auditing Standards*, issued by the Comptroller General.

Significant Accounting Policies

The auditor should determine that the audit committee is informed about all significant accounting policies and how they are applied in the governmental organization. To make sure, the audit committee should expect that the auditors will communicate the following:

1. All significant accounting policies, including those that applied for the first time during the year
2. How those accounting policies are applied in the organization
3. Methods the organization used to account for significant unusual transactions
4. The effect of significant accounting policies in controversial or emerging areas for which there is lack of authoritative guidance or consensus

Management Judgments and Accounting Estimates

Accounting estimates are an integral part of the financial statements prepared by management. These estimates are based on management's judgments (which are normally based on management's knowledge and experience about past and current events), and assumptions about future events.

The auditor should address the following issues with the audit committee:

1. The process used by management in formulating particularly sensitive accounting estimates
2. The basis for the auditor's conclusion about the reasonableness of those estimates

Audit Adjustments

The auditor should inform the audit committee about all audit adjustments arising from the audit that could, in the auditor's judgment, have a significant effect on the organization's financial reporting process. The audit team will keep track of those proposed adjustments for later discussion with management. Management will evaluate those proposed adjustments and decide whether the adjustment should be booked to the account balances as proposed. Bear in mind, however, that the auditor may find it necessary to qualify the audit report if management does not record the adjustments that the auditor deems necessary to record.

As part of its communications, the auditor should:

1. Inform the audit committee about adjustments arising from the audit that could either individually or in the aggregate have a significant effect on the organization's financial reporting process.
2. Address whether the adjustments were recorded.
3. Determine whether the adjustments may not have been detected except through the auditing procedures performed (meaning that the organization's own internal control system did not detect the need for the adjustment).
4. Explain about uncorrected misstatements aggregated by the auditor during the current engagement and pertaining to the most recent period presented in the financial statements, that were determined by management to be immaterial, both individually and in the aggregate, to the financial statements taken as a whole.

Auditor's Judgments About the Quality of the Organization's Accounting Principles

Note: This communication is required for audits of public companies. It is not required for governmental organizations but could be considered a good practice.

Although objective criteria for evaluating the quality of an organization's accounting practices have not been established, the auditor's judgments about the quality, not just the acceptability of the organization's accounting principles as applied in its financial statements, including disclosures, should be discussed. The discussion should be open and frank, and tailored to the organization's specific circumstances. It should include the following topics:

1. Consistency of the organization's accounting principles and their application
2. Clarity of the financial statements and related disclosures
3. Completeness of the financial statements and related disclosures
4. Any items that have a significant impact on the representational faithfulness, verifiability, and neutrality of the accounting information included in the financial statements, examples of which follow:
 - a. Selection of new accounting policies or changes to current ones
 - b. Estimates, judgments, and uncertainties
 - c. Unusual transactions
 - d. Accounting policies relating to significant financial statement items, including the timing of transactions and the period in which they are recorded
5. A discussion of accounting practices that are not specifically addressed in the accounting literature, for example, those that may be unique to a specific industry.

Other Information Contained in Audited Financial Statements

Although the notes to the financial statements are an integral part of the financial statements and therefore are included in the scope of the auditing procedures, other information prepared by management that generally accompanies financial statements is not necessarily included in the scope of the auditing procedures, for example, "Management's Discussion and Analysis of the Financial Condition and Results of Operations."

The auditor should discuss the responsibility, if any, that he or she has for other information in documents containing audited financial statements, any procedures performed, and the results.

Disagreements With Management

Disagreements may arise between the auditor and management over the application of accounting principles to specific transactions and events, as well as the basis for management's judgments about accounting estimates, or even the scope of the audit or disclosures to be made in the financial

statements or footnotes. Differences of opinion based on incomplete facts or preliminary information that are later resolved are not considered disagreements for this purpose.

When meeting with the audit committee, the auditors should discuss any disagreements with management, whether or not resolved, about matters that individually or in the aggregate could be significant to the organization's financial statements or the auditor's report.

Consultation With Other Accountants

Sometimes, management of the government organization may consult with other accountants about accounting and auditing matters. If the auditor is aware that such consultation has occurred, the auditor should discuss with the audit committee their views about the significant matters that were the subject of the consultation. The audit committee may wish to ask management whether they have consulted with other accountants about accounting and auditing matters.

Major Issues Discussed With Management Before Retention

The auditor should discuss with the audit committee any major issues that were discussed with management in connection with the initial or recurring retention of the auditor. This includes any discussions regarding the application of accounting principles or auditing standards. For some government organizations, an audit organization is mandated by federal or state law to perform the government organization's audit. While auditor retention is not an issue, the auditor should nonetheless discuss with the audit committee any major issues regarding the auditor's application of accounting principles or auditing standards.

Difficulties Encountered in Performing the Audit

The auditor should inform the audit committee about any serious difficulties encountered in working with management during the audit. Examples include, but are not limited to:

1. Unreasonable delays by management in allowing the commencement of the audit
2. Unreasonable delays or refusals by management in providing needed information to the auditor
3. Unreasonable timetable set by management for the conduct of the audit
4. Unavailability of client personnel
5. Failure of client personnel to complete client-prepared schedules on a timely basis

Illegal Acts

The auditor has the responsibility to assure himself or herself that the audit committee is adequately informed about illegal acts that come to the auditor's attention (this communication need not include matters that are clearly inconsequential). The communication should describe (1) the act, (2) the circumstances of its occurrence, and (3) the effect on the financial statements.

What is an illegal act for purposes of this communication? Statement on Auditing Standards (SAS) No. 54, *Illegal Acts by Clients* (AICPA, *Professional Standards*, vol. 1, AU sec. 317), defines it as violations of laws or government regulations attributable to the government organization, or acts by management or employees on behalf of the organization. Illegal acts do not include personal misconduct by the organization's personnel unrelated to the government's business activities.

In addition, *Government Auditing Standards*, Auditor Communication, Chapter 5, Section 5.12, issued by the Comptroller General, and OMB Bulletin No. 01-02, *Audit Requirements for Federal Financial Statements*, Section 7, paragraph c.(3)(a) require auditors to report noncompliance with laws and regulations disclosed by the audit, except for those instances of noncompliance that are clearly inconsequential. In meeting this requirement, the auditor shall report all instances of fraud and illegal acts unless clearly inconsequential and significant violations of provisions of contracts or grant agreements and abuse. In some circumstances, auditors are required to report fraud, illegal acts, violations of provisions of contracts or grant agreements, and abuse directly to parties external to the audited organization.

Internal Control Matters

See also the tool, “Internal Control: A Tool for the Audit Committee,” elsewhere in this toolkit.

SAS No. 60, *Communication of Internal Control Related Matters Noted in an Audit* (AICPA, *Professional Standards*, vol. 1, AU sec. 325), requires the auditor to communicate matters relating to the organization’s internal control that are observed by the auditor in the conduct of a financial statement audit. These matters should be discussed with the audit committee because they represent significant deficiencies in the design or operation of the internal control system, which could adversely affect the organization’s ability to initiate, record, process, and report financial data consistent with the assertions of management in the financial statements.

Fraud

See also the tool, “Fraud and the Responsibilities of the Government Audit Committee,” elsewhere in this toolkit.

SAS No. 99, *Consideration of Fraud in a Financial Statement Audit* (AICPA, *Professional Standards*, vol. 1, AU sec. 316), requires that the independent auditor bring any evidence of fraud to the attention of the appropriate level of management (generally seen as one level higher than the level at which a suspected fraud may have occurred), even in the case of an inconsequential fraud, such as a minor defalcation by a low-level employee. The independent auditor should reach an understanding with the audit committee regarding when (nature and scope) an inconsequential fraud conducted by a low-level employee should be brought to the audit committee’s attention.

Fraud involving senior management, and any fraud (whether caused by senior management or other employees) that causes a material misstatement of the financial statements must be reported to the audit committee by the independent auditor.



Anonymous Submission of Suspected Wrongdoing (Whistleblowers)—Issues for Government Audit Committees to Consider

PURPOSE OF THIS TOOL: A key defense against management override of internal controls is a process for anonymous submission of suspected wrongdoing (whistleblowing) that typically incorporates a telephone hotline. Respondents to a 2004 survey by the Association of Certified Fraud Examiners (ACFE) revealed that various forms of fraud are detected 40 percent of the time by tips, the leading method for detecting fraud.¹ Also, ACFE recommends opening the system to suppliers, customers, and others, which can increase the number of reports by approximately 50 percent.²

This tool offers examples of questions to consider when designing an effective whistleblower hotline. It is not intended to be all-inclusive, and some items may not apply to your entity's operations.

To learn more about whistleblower laws and rights, see the document at http://www.aicpa.org/antifraud/business_industry_govt/increasing_awareness/43.htm.

Whistleblower Issues for Audit Committees to Consider Tool	Yes	No	Not Sure	Comments
A. Design Effectiveness				
In assessing the design effectiveness of the hotline, a government audit committee should consider the following questions:				
1. Does the hotline have a dedicated hotline number, fax number, Web site, e-mail address, and regular mail or post office box address to expedite reports of suspected incidents of misconduct?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	

¹ Association of Certified Fraud Examiners, *2004 Report to the Nation on Occupational Fraud and Abuse*, Austin, TX: ACFE, 2004, p 18.

² Association of Certified Fraud Examiners, *2004 Report to the Nation on Occupational Fraud and Abuse*, Austin, TX: ACFE, 2004, p. 19.

Whistleblower Issues for Audit Committees to Consider Tool	Yes	No	Not Sure	Comments
A. Design Effectiveness (cont.)				
2. Does the hotline demonstrate confidentiality, including showing how caller ID, e-mail tracking, and other technologies cannot be used to identify the whistleblower? Has the government considered the use of an independent hotline operator to enhance the perception of confidentiality in addition to any real improvement?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
3. Does the hotline utilize trained interviewers to handle calls to the hotline rather than a voice mail system?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
4. Is the hotline availability 24 hours a day, 365 days a year?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
5. Does the hotline have multilingual capability to support hotline callers with different ethnic backgrounds or those that are calling from different countries?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
6. Are callers provided with a unique identification number to enable them to call back later anonymously to receive feedback or follow-up questions from investigators?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
7. Does the government have a case management system to log all calls and their follow-up, to facilitate management of the resolution process, testing by internal auditors, and oversight by the audit committee? For a sample tracking report that audit committees may use for this purpose, see the “Sample Whistleblower Tracking Report” tool herein.	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	

Anonymous Submission of Suspected Wrongdoing (Whistleblowers)

Whistleblower Issues for Audit Committees to Consider Tool	Yes	No	Not Sure	Comments
A. Design Effectiveness (cont.)				
8. Has the government established protocols for the timely distribution of each type of complaint, regardless of the mechanism used to report the complaint? Are complaints of any kind involving senior management automatically and directly submitted to the audit committee without filtering by management or other government personnel?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
9. Does the government effectively distribute comprehensive educational materials and training programs among potential users to raise awareness of the hotline? Are these materials available in all relevant languages, given the potential user base and taking into consideration cultural differences that may require alternative approaches to achieve the desired goal?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
10. Does the government support outreach to potential stakeholders other than employees?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
11. Do the government's internal auditors periodically evaluate the design and operating effectiveness of the hotline? What were the internal auditors' conclusions regarding (1) how the hotline reflects changes in the government's operations and in best practices; (2) whether the hotline is receiving satisfactory support from management, employees, and other participants; and, (3) whether protocols established for forwarding information to the government audit committee have been followed?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
B. Educating Employees and Others About the Hotline				
In assessing whether management is actively promoting the existence and use of the hotline, a government audit committee should consider the following questions:				
1. Is confidentiality of communications made to the hotline stressed?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	

Whistleblower Issues for Audit Committees to Consider Tool	Yes	No	Not Sure	Comments
B. Educating Employees and Others About the Hotline (cont.)				
2. Is training provided to employees upon hiring and periodically thereafter?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
3. For suppliers, is information incorporated into a vendor approval process, in purchase contracts, and on purchase orders?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
4. Is the hotline number and other contact information provided on the government's Web site, intranet, newsletters, invoices, purchase orders, pay stubs, checks, and even vehicles?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
C. Evaluating Communications Received				
In evaluating the communications received, a government audit committee should consider the following questions:				
1. Is management taking all communications made to the hotline seriously? Are allegations appropriately investigated?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
2. Does the government have a process for reporting back to the whistleblower on a timely basis, where possible, regarding the action taken?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	

Sample Whistleblower Tracking Report

PURPOSE OF THIS TOOL: Government audit committees may vary greatly in their responsibilities in responding to complaints, whether generated internally or externally, regarding fraud, waste, and abuse. For government audit committees with the defined role of responding to complaints, this tool could be used to track complaints received to an appropriate resolution.

Many federal, state, and local government entities have whistleblower laws and regulations. These regulations may require the entity to establish procedures for the confidential receipt, retention, and treatment of complaints received regarding suspected fraudulent activities. The government audit committee should ensure that the entity has established a process to address applicable whistleblower laws and regulations.

If the government audit committee is assigned the responsibility of monitoring the entity's complaint process, this tool can be used as an effective internal record-keeping device to track the types of complaints, current status and actions taken.

Refer to the tool *Anonymous Submission of Suspected Wrongdoing—Issues for Government Audit Committees to Consider* for points the audit committee should consider when designing or evaluating a whistleblower program.

Anonymous Submission of Suspected Wrongdoing (Whistleblowers)

Instructions for Using This Tool: Before using this tool, the government audit committee should review any applicable federal, state, or local laws and/or regulations governing whistleblower activities.

Sample Whistleblower Tracking Report					
Date Submitted	Tracking Number	Description of Complaint	Submitted By Employee (E) Citizen (C) Vendor (V) Other (O)	Current Status: R–Resolved UI–Under Investigation D–Dismissed W–Withdrawn P–Pending/ No Action	Actions Taken
				Date	Comments



Evaluating the Internal Audit Team: Guidelines and Questions

PURPOSE OF THIS TOOL: The sample questions included in this tool are only a starting point to assist the audit committee in evaluating the performance and effectiveness of the internal audit team. Follow-up questions should be considered as appropriate.

Audit Committee Relationship with Internal Audit Team

It is in the best interest of all concerned for the audit committee and the internal audit team to maintain a strong positive relationship. The audit committee should view the internal audit team as their eyes and ears about what is going on within the government organization. The audit committee should promote a relationship of healthy professional skepticism between the chief audit executive and the chief financial officer (CFO) or the government organization's equivalent of a CFO, though it is these two individuals who will likely spend the most time working with the audit committee.

The audit committee chair and the leader of the internal audit team (the chief audit executive or CAE) should have frequent contact between meetings of the audit committee. In fact, the CAE should have a "solid-line" reporting relationship to the audit committee (with a "dotted-line" reporting relationship to a senior executive in the government organization for administrative purposes), and in certain cases, when given the authority, the audit committee would be consulted before the CAE can be hired, fired, or reassigned.

At every audit committee meeting the committee should hold an executive session with the CAE to ask specific questions (see "Conducting an Audit Committee Executive Session: Guidelines and Questions"). It is best for the audit committee to ask specific, yet open-ended questions, and to probe for more detail on answers that might be puzzling or incomplete. The CAE should be forthcoming with information, including the results of audits conducted as well as the audit currently under way. The internal audit team should recognize that it is an agent of the audit committee and not management.

The CAE should be the keeper of the audit committee charter, and should consult with the committee chair and the CFO (or government equivalent) in developing meeting agendas.

Periodically, the CAE should review with the audit committee the staffing needs of the internal audit team, and the competencies of the individuals filling those positions. As a best practice, the internal audit team should not be the victim of rightsizing, often referred to as "downsizing" in the corporate world; in fact, it is at precisely this time that the internal audit team should be doing extra monitoring regarding the safeguarding of assets, the integrity of the internal control system, and related matters.

Discussions between the CAE and the audit committee should also address the competencies of the financial management team. The internal audit team may be in the best position to determine whether the financial management team is able to address complex accounting issues on its own, or whether it relies too heavily on the independent auditor for evaluation and decision-making.

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The audit committee should also promote a positive working relationship between the CAE and the independent auditor. If possible, the independent auditor should rely on the work of the internal auditor to supplement or limit its own testing. Generally accepted auditing standards (GAAS) requires that the independent auditor maintain control of the work being performed on its behalf, and to reperform some of the testing to reach its own conclusion about the work of the internal auditor.

Finally, the audit committee should periodically assess the performance of the CAE and the internal audit team to ensure that they are the appropriate agent of the audit committee in the government organization. The following tool includes some sample questions that the audit committee should ask itself in evaluating the effectiveness of the internal audit team.

INSTRUCTIONS FOR USING THIS TOOL: The sample questions included in this tool are only a starting point to evaluating the performance and effectiveness of the internal audit team. Audit committee members should ask follow-up questions as appropriate.

Evaluation of Internal Audit Team	Yes	No	Not Sure	Comments
1. Does the department or function appear to be using its time and resources effectively and efficiently?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
2. Is the size and structure of the department or function adequate to meet its established objectives?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
3. Is the experience level of the internal auditors adequate?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
4. Does the department or function appear to be objective, and what procedures are performed to ensure objectivity?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
5. Is the technical knowledge of the department or function staff members sufficient to ensure that duties are performed appropriately?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
6. Does the department or function have an appropriate continuing education program?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
7. Are there department or function staff members with sufficient information systems auditing expertise to address the level of technology used by the government organization?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
8. Is the work of the department or function planned appropriately?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
9. Does planning include written audit plans and programs?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
10. What types of reports are issued by the internal audit department or function and to whom?				
11. Are the internal audit reports issued on a timely basis?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	

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Evaluation of Internal Audit Team	Yes	No	Not Sure	Comments
12. Do the internal audit reports include sufficient detail for effective action by management and/or the audit committee?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
13. Does management respond in an appropriate and timely fashion to significant recommendations and comments made by the internal auditors?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
14. Do internal audit procedures encompass operational as well as financial areas?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
15. Was the involvement of the department or function in the annual audit effective?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
16. What could be done in the future to maximize the effectiveness and efficiency of the department or function?				
17. To what extent is outsourcing used in the internal audit function; what areas are outsourced and to whom are they outsourced?				
18. Does the internal audit team have a periodic peer review performed and, if so, what were the results of the latest review?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
19. What criteria are used to establish and prioritize the annual and long-range internal audit plans?				
20. Is the work of the department or function concentrated in areas of high risk, judgment, and sensitivity?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
21. To what extent does the internal audit team keep itself informed about and involved in professional activities?				
22. What are the internal auditors' views regarding controls, the risk of fraud, and compliance matters?				
23. Has the charter of the internal audit department or function been evaluated to determine whether it is still appropriate?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	

<i>Other Questions or Comments</i>	



Evaluating the Independent Auditor: Questions to Consider

PURPOSE OF THIS TOOL: The audit committee (or its equivalent) may have the responsibility to hire, fire, and evaluate the independent auditors. If the audit committee (or its equivalent) has this responsibility, the audit committee should answer a series of questions about its relationship with the independent auditor and should ask key executives in the government organization for their comments as well.

In considering information gathered through the process of evaluating the independent auditors, it is important that the audit committee give consideration to the source of the information. For example, if the chief financial officer (CFO) or controller comments that he or she believes the auditor went too far in certain areas, that would probably carry less weight in your deliberations than if the CFO or controller comments that certain areas were not tested adequately or that auditor independence had been breached. As with all deliberative processes, the different perspectives and motivations of those having input into the deliberations should be considered.

INSTRUCTIONS FOR USING THIS TOOL: The sample questions included in this tool are only a starting point in evaluating the performance and effectiveness of the independent auditors. Audit committee members should ask follow-up questions as appropriate and required.

Evaluation of the Independent Auditor	Yes	No	Not sure	Comments
Questions for Audit Committee Members				
1. Did the auditor meet with the audit committee when requested?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
2. Did the auditor address issues of “tone at the top,” and antifraud programs and controls in place in the government organization?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
3. Did the auditor inform the audit committee of any risks of which the committee was not previously aware?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
4. Did the auditor adequately discuss issues of the quality of financial reporting, including the applicability of new and significant accounting principles? Did the auditor adequately discuss issues relating to the government’s conformance with local laws, regulations, and oversight requirements?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
5. Did the auditor communicate issues freely with the audit committee, or did they seem protective of management?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
6. Does it appear that management exercises undue influence on the independent auditors?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
7. Does it appear that the independent auditors are reluctant or hesitant to raise issues that would reflect negatively on management?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
8. Is the audit committee satisfied with the planning and conduct of the audit, including the financial statements and internal control over financial reporting (as applicable)?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	

Evaluation of the Independent Auditor	Yes	No	Not sure	Comments
Questions for Audit Committee Members (cont.)				
<p>9. Review all audit-related and nonaudit services conducted by the independent auditor in the prior year. Are you satisfied that the independent auditor remains independent and objective both in fact and appearance?</p>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
<p>10. Understand the size of the firm and its total revenues firm-wide, for the office(s) providing a substantial amount of services to the government, and the book-of-business of the partner-in-charge of the audit. Is the firm, the office, or the partner dependent on the government engagement for a material percentage of its fee income? If so, the audit committee should consider whether this impairs the appearance of independence with respect to the government.</p>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
<p>11. Is the audit committee satisfied with its relationship with the auditor? In making this determination, the audit committee should consider (a) whether the partner-in-charge of the audit participated in audit committee meetings, (b) whether the auditor was frank and complete in the required discussions with the audit committee, (c) whether the auditor was frank and complete during executive sessions with the audit committee, (d) whether the auditor was on time in the delivery of services to the government.</p>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
<p>12. Was the audit fee fair and reasonable in relation to what the audit committee knows about fees charged to other government organizations, and in line with fee benchmarking data the audit committee might have available?</p>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	

Evaluation of the Independent Auditor	Yes	No	Not sure	Comments
Questions for Audit Committee Members (cont.)				
13. Did the independent auditor provide constructive observations, implications, and recommendations in areas needing improvement, particularly with respect to the organization's internal control system over financial reporting? How constructive are the key issues communicated in the management letter and other disclosures on audit findings and recommendations?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
<i>Following are some questions the audit committee (or its equivalent) should ask different individuals in the government organization to assist in evaluating the performance of the independent auditors.</i>				
Chief Audit Executive				
1. From your perspective in working with the independent auditors, are you satisfied with the scope, nature, extent, and timing of the testing performed by the independent auditor?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
2. Did the independent auditor work with you to ensure the coordination of audit efforts to assure the completeness of coverage, reduction of redundant efforts, and the effective use of audit resources?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
3. a. Are you satisfied with the knowledge, skills, and abilities of the staff assigned to do the audit work?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
b. Are you satisfied with the engagement leadership assigned, including the partner(s), manager(s), and fieldwork leaders?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
4. a. Did the independent auditors work with the internal auditors according to the plan?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
b. Was the cooperative work conducted in the spirit of professionalism and mutual respect?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	

Evaluation of the Independent Auditor	Yes	No	Not sure	Comments
Chief Audit Executive (cont.)				
5. Are you satisfied that the independent auditors remain independent of the government in spite of any audit-related or nonaudit services the auditor provides to the government?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
6. a. Are you aware of any other information that might impair the independence of the independent audit firm?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
b. Are you aware of any individuals on the audit team that might not be independent with respect to the government for whatever reason?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
7. a. If the choice were yours, would you hire the firm to conduct next year's audit?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
b. What changes would you make?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
CFO and Controller				
1. From your perspective in working with the independent auditor, are you satisfied with the scope, nature, extent, and timing of the testing performed by the independent auditors?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
2. Are you satisfied with the knowledge, skills, and abilities of the staff assigned to the audit work? Did the auditor appear to have sufficient knowledge of the most recent generally accepted government auditing standards (GAGAS) as set forth by the Government Accountability Office (GAO), as well as AICPA auditing standards?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
3. Are you satisfied with the engagement leadership assigned, including the partner(s), manager(s), and fieldwork leaders?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
4. a. If the choice were yours, would you hire the firm to conduct next year's audit?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
b. What changes would you make?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
5. Did the auditor comply with the requirements as set forth in the request for proposal and/or subsequent contract for auditor services?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	

Evaluation of the Independent Auditor	Yes	No	Not sure	Comments
Independent Auditor				
1. What were the results of the firm's peer review?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
2. Does the audit organization have a quality control system for monitoring compliance with independence requirements?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
3. Does the audit organization have a quality control system for monitoring compliance with continuing professional education requirements?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
Other Comments and Further Questions				



Conducting an Audit Committee Self-Evaluation: Guidelines and Questions

PURPOSE OF THIS TOOL: Audit committees should consider conducting a comprehensive self-evaluation on an annual basis. This can be accomplished in a number of evaluation formats and scenarios (for example, through the use of outside evaluators, a 360-degree evaluation format, and other methods). The sample questions included in this tool are only a starting point to evaluating the performance and effectiveness of the audit committee. Follow-up questions are encouraged and the committee should plan for further action as appropriate.

The self-evaluation can take different forms, involve a number of participants, and use diverse techniques. Most important, however, the self-evaluation should adopt a straightforward approach that will aid the audit committee in assessing its strengths and weaknesses and lay a foundation for future improvement. Some guidelines in designing the format for self-evaluation would include the following areas of consideration.

1. *Introspection.* Be introspective. Evaluate the audit committee's performance by asking specific questions about the impact it has had on the organization, and most importantly, its financial reporting process, the annual audit, the relationship with the internal and independent auditors, members of management and elected officials. Consider including a representative of the governing body or an equivalent official in this evaluation process.
2. *Comprehensive.* Conduct 360-degree evaluations of all audit committee members and the committee chair. The chair should consider the result of the audit committee members' evaluations of each other in the context of the chair's evaluation of the members. The chair should consider whether any members of the committee should be rotated off the committee; this should be done in consultation with the representative of the governing body or the equivalent official. The members' attendance record and level of participation should be considered during this process.
3. *Performance improvement.* Ask the chief audit executive, chief financial officer, chief executive officer, and independent auditor for comments on the performance of the audit committee. Include this constructive feedback in the session referred to in item 1 above.
4. *Competency.* Use tools that are available, including the AICPA Competency Self-Assessment Tool (CAT) to evaluate performance. The CAT is available at <https://www.cpa2biz.com/CPE-Conferences/CAT.htm>.
5. *Leadership.* The members should talk about the performance of the committee chair. If the members collectively agree that the committee chair is not performing at the level needed, the members should bring their concerns to the attention of the chair of the governing body or equivalent official.

INSTRUCTIONS FOR USING THIS TOOL: The sample questions provided in this tool are only a starting point to evaluating the performance and effectiveness of the audit committee. Before completion, the committee should determine how it can best ensure that responses reflect a forthright exchange of ideas and opinions among audit committee members. The committee should determine how the process should be completed. The following sample questions can be completed anonymously, before attending an evaluation discussion meeting or during a session of the committee. These questions are intended to provide guidance on assessing the general effectiveness of the audit committee in its roles and relationships, which includes understanding the government’s activities, its risk factors, and acquiring the technical and communication proficiency necessary for proper oversight of the accounting, financial reporting, and internal control environment.

Audit Committee Self-Evaluation Tool	Yes	No	Not Sure	Comments
A. Roles and Relationships				
1. Does the audit committee (committee) have a positive working relationship with management, the internal auditors, and the independent auditors?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
2. Does the committee provide its own view on issues to the chair?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
3. Are differences of opinion on issues resolved to the satisfaction of the committee?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
4. Do all members provide input to the committee chair as appropriate?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
5. Is an audit committee charter used as a document to guide the committee in its efforts, and to help guide the committee’s agenda?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
6. Does the committee engage outside experts as appropriate?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
7. Does the committee conduct executive sessions in a manner that offers a “safe haven” to the individual, while at the same time asking tough and necessary questions, evaluating the answers, and pursuing issues that might arise to a satisfactory resolution?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	

Audit Committee Self-Evaluation Tool	Yes	No	Not Sure	Comments
A. Roles and Relationships (cont.)				
8. Did the audit committee evaluate the internal auditors' overall effectiveness?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
9. Did the audit committee evaluate the independent auditors, including the auditors' responsiveness to the committee's expectations?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
10. Is the size of the committee appropriate for the complexity and operations of the government organization?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
11. Are committee members independent of management?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
12. Do committee members encourage a "tone at the top" that conveys basic values of ethical integrity as well as legal compliance and strong financial reporting and control?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
B. Government Activities				
1. Does the committee understand the organizational structure and programs of the government's activities and programs?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
2. Does the committee evaluate whether management exhibits the proper tone at the top and foster a culture and environment that promotes high-quality financial reporting and appropriate attention to internal controls and compliance with laws and regulations?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
3. Does the committee evaluate management's procedures for monitoring compliance with the government organization's code of ethics?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
4. Does the committee receive the internal and the independent auditors' assessments of the risks for fraud and other risk factors that lead to potential fraudulent financial reporting?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	

Audit Committee Self-Evaluation Tool	Yes	No	Not Sure	Comments
B. Government Activities (cont.)				
5. Is the audit committee aware of reports or other communications received from regulators, and updates from the general counsel on legal and regulatory matters, that may have a material effect on the financial activities and related financial statements, or that may affect related organizational compliance policies?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
C. Risk Factors				
1. Does the committee have discussions with the chief information officer to understand the organization's technology strategy, information systems, and measures taken to protect technology resources, including disaster recovery and emergency preparedness?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
2. Has the audit committee reviewed all significant control deficiencies identified by the internal or independent auditors, as well as management's corrective action plan and timetable to address those recommendations?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
D. Technical Proficiency				
1. Is the committee cognizant of the line between oversight and management, and does it endeavor to respect that line?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
2. Are committee members financially literate?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
3. Has a representative number of committee members attended recent training on governmental accounting, auditing, and financial reporting developments, and current business and industry practices?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
4. Does the committee review reports, financial statements, and related audit results with management, staff, and independent auditors? Does the committee include reviewing interim audit and A-133 Single Audit results?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	

Audit Committee Self-Evaluation Tool	Yes	No	Not Sure	Comments
D. Technical Proficiency (cont.)				
5. Has the committee discussed with management any significant year-end issues that may affect the financial integrity of accounting and reporting practices?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
6. Does the committee have a system to assess whether net assets are being managed effectively?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
7. Are the government's financial reporting processes stronger as a result of management's interactions with the committee?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
8. Does the committee discuss the audit plans with the internal and independent auditors, along with the extent of control testing to be performed and related concerns and challenges?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
9. Did the committee assess whether independence has been maintained by the independent auditors (and internal auditors, if relevant) and discussed the processes used by such auditors to monitor for independence?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
10. Where appropriate, did the committee approve and sign the engagement letter(s) for the annual and A-133 audits and nonaudit services?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
E. Communication Process				
1. Are meeting agendas prepared and distributed in advance to ensure effective and efficient meetings, to allow that necessary topics are addressed, and to comply with open meeting laws?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
2. Are minutes of meetings taken and circulated after the meeting?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	

Audit Committee Self-Evaluation Tool	Yes	No	Not Sure	Comments
E. Communication Process (cont.)				
3. Does the committee review management's response to audit recommendations and whether follow-up audits indicate corrective action is in place, timely, and effective?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	




Resources for Audit Committees

PURPOSE OF THIS TOOL: Audit committees can take advantage of the Internet and find a wealth of resources to assist them in discharging their responsibilities. This Tool provides an overview of organizations and Web sites that contain topical resources for audit committee members to investigate.

Below is a sampling of organizations and Web sites that can assist audit committee members in learning more about government accountability and their roles, responsibilities, and functions.

American Institute of Certified Public Accountants www.aicpa.org

The American Institute of Certified Public Accountants (AICPA) is the national professional association for all certified public accountants. This includes CPAs working as independent auditors, accountants, or consultants in public practice, business and industry (CFOs, controllers, internal auditors, etc.), governments, not-for-profit organizations, and the academic community.

The AICPA has developed *The AICPA Audit Committee Toolkit: Government Organizations* to aid audit committee members in performing their functions. In addition, the AICPA produces publications on accounting and auditing, financial reporting, tax, technology, and many other relevant topics. Some additional online resources useful to audit committees include:

- Audit Committee Effectiveness Center at www.aicpa.org/audcommctr
- Antifraud and Corporate Responsibility Resource Center at www.aicpa.org/antifraud
- Sarbanes-Oxley Implementation Central at www.aicpa.org/sarbanes/index.asp

Association of Certified Fraud Examiners www.cfenet.com

The Association of Certified Fraud Examiners (ACFE) is a global professional organization dedicated to fighting fraud and white-collar crime. With chapters around the globe, the ACFE is networked to respond to the needs of antifraud professionals everywhere. They offer guidance on fraud prevention, detection, and investigation, as well as internal controls.

Association of Government Accountants www.agacgfm.org

The Association of Government Accountants (AGA) is an educational organization dedicated to enhancing public financial management. AGA serves the professional interests of financial managers, from local, state and federal governments, as well as public accounting firms, responsible for effectively using billions of dollars and other monetary resources every day. AGA conducts independent research and analysis of all aspects of government financial management, for the purpose of advocating the improvement in the quality and effectiveness of government fiscal administration.

Committee of Sponsoring Organizations of the Treadway Commission www.coso.org

Committee of Sponsoring Organizations of the Treadway Commission (COSO) is a voluntary private-sector organization dedicated to improving the quality of financial reporting through business ethics, effective internal controls, and corporate governance. Originally formed in 1985 to sponsor the National Commission on Fraudulent Financial Reporting, COSO has released numerous influential publications, including *Internal Control—Integrated Framework*.

Ethics Officers Association www.eoa.org

The Ethics Officers Association (EOA) is the professional association exclusively for managers of ethics, compliance, and business conduct programs. The EOA provides ethics officers with training and a variety of conferences and meetings for exchanging best practices in a frank, candid manner.

Ethics Resource Center www.ethics.org

The Ethics Resource Center (ERC) is a nonprofit, nonpartisan educational organization whose vision is a world in which individuals and organizations act with integrity. Their mission is to strengthen ethical leadership worldwide by providing leading-edge expertise and services through research, education and partnerships. Especially useful are their resources on business and organizational ethics.

Government Finance Officers Association www.gfoa.org

The Government Finance Officers Association (GFOA) serves the state, provincial, and local finance officers in the United States and Canada and is dedicated to the sound management of government financial resources. GFOA administers a broad range of services and programs in the major functional areas of government financial management, including accounting, auditing, and financial reporting; budgeting and financial planning; capital finance and debt administration; cash management and investments; and financial management. Guidance, publications, and programs are available from the GFOA Web site.

Institute of Internal Auditors (IIA) www.theiia.org

The Institute of Internal Auditors (IIA) is a dynamic international organization that meets the needs of a worldwide body of internal auditors. IIA focuses on issues in internal auditing, governance and internal control, information technology (IT) audit, education, and security worldwide. The Institute provides internal audit practitioners, executive management, boards of directors and audit committees with standards, guidance, best practices, training, research, and technological guidance for the profession.

IT Governance Institute www.itgi.org

Established by the Information Systems Audit and Control Association and Foundation (ISACA) in 1998, the IT Governance Institute (ITGI) exists to assist enterprise leaders in understanding and guiding the role of IT in their organizations. ITGI helps senior executives to ensure that IT goals align with those of the business, deliver value, and perform efficiently, while IT resources are properly allocated and its risks mitigated. Through original research, symposia, and electronic resources, ITGI helps ensure that boards and executive management have the tools and information they need to effectively manage the IT function.

National Association of College and University Business Officers www.nacubo.org

The National Association of College and University Business Officers (NACUBO) represents college and university administrative and financial officers through a collaboration of knowledge and professional development, advocacy, and community to establish excellence in higher education business and financial management. NACUBO's Web site includes tools, publications, and guidance for college and university financial management, including guidance on how colleges and universities might implement relevant portions of the Sarbanes-Oxley Act as a best practice.

National Association of Local Government Auditors www.nalga.org

Among the primary objectives of the National Association of Local Government Auditors (NALGA) is improving the quality of auditing in local government, providing a forum for the discussion of issues concerning auditing in local government, and upholding the highest standards of professional ethics. NALGA provides information, guidance, and opportunities for local government auditors about audit standards, related training, peer reviews, and other audit issues.

National Association of State Auditors, Comptrollers and Treasurers www.nasact.org

The National Association of State Auditors, Comptrollers and Treasurers (NASACT) is an organization for state officials who work in the financial management of state government. NASACT assists state leaders enhance and promote effective and efficient management of government resources. NASACT's Web site provides information regarding, among other things, efforts to improve financial management practices at all levels of government, shares expertise and ideas that promote effective financial management, and develops and promotes an exchange of industry best practices.

U.S. Government Accountability Office www.gao.gov

The U.S. Government Accountability Office (GAO) is an independent, nonpartisan agency that works for Congress. With its core values of accountability, integrity, and reliability, ultimately, GAO works to ensure that government is accountable to the American people. GAO issues *Government Auditing Standards* (also known as the Yellow Book), which contains standards for audits of government organizations, programs, activities, and functions. These standards, often referred to as generally accepted government auditing standards (GAGAS), are to be followed by public accounting firms and audit organizations that audit governments and not-for-profit organizations when required by law, regulation, agreement, contract, or policy.

U.S. Office of Management and Budget www.whitehouse.gov/omb/index.html

The U.S. Office of Management and Budget's (OMB) mission is to assist the President in overseeing the preparation of the federal budget; to supervise its administration in Executive Branch agencies; and coordinate the Administration's procurement, financial management, information, and regulatory policies. In each of these areas, OMB's role is to help improve administrative management and, therefore, has an impact on all levels of government. State, local, and special-purpose governments are required to follow OMB's financial management rules and guidance if they receive federal program monies either directly or indirectly. The OMB Web site includes information about these rules and guidance for those charged with responsibility for a government's compliance with financial management laws and regulations.

Resources for Corporate Governance and Publicly Traded Company Audit Committees

Many organizations provide information, tools, and publications about corporate governance and audit committees for publicly traded companies that must follow the requirements of the Sarbanes-Oxley Act. Although government organizations are not subject to the requirements of the Sarbanes-Oxley Act, the following Web sites may provide government audit committees with additional information that could be applied in their environments as best practices.

American Society of Corporate Secretaries www.acsc.org

The American Society of Corporate Secretaries (ASCS) acts as a positive force for enlightened corporate governance whose key mission is to promote excellence in corporate governance. The members of the ASCS address issues of public disclosure under the securities laws and matters affecting corporate governance, including the structure and meetings of the board of directors and its committees, and the proxy process and the annual meeting of shareholders and shareholder relations, particularly with large institutional owners.

Business Roundtable www.brtable.org

The Business Roundtable (BRT) is an association of chief executive officers (CEOs) of leading U.S. corporations. The BRT is committed to advocating public policies that foster vigorous economic growth, a dynamic global economy, and a well-trained and productive U.S. workforce essential for future competitiveness. The BRT's *Corporate Governance Task Force* focuses on issues related to corporate governance and responsibilities, including accounting standards.

Conference Board www.conference-board.com

The Conference Board is a global, independent membership organization that creates and disseminates knowledge about management and the marketplace to help businesses strengthen their performance and better serve society. They conduct research, convene conferences, make forecasts, assess trends, publish information and analysis, and bring executives together to learn from one another. The Conference Board's Blue-Ribbon Commission on Public Trust and Private Enterprise has proposed reforms to strengthen corporate compensation practices and help restore trust in America's corporations and capital markets.

Corporate Board Member www.boardmember.com

Corporate Board Member magazine's Web site, Boardmember.com, serves as a central resource for officers and directors of publicly traded corporations, top private companies, and Global 1000 firms. The Resource Center offers the full-text of *Corporate Board Member* magazine, as well as additional articles, Webcasts, and interviews. Topics include corporate governance, strategic board trends and issues, executive and director compensation, audit committees, risk management, international and technology trends, investor relations, board education, and other critical topics facing today's directors and officers of publicly traded companies. They also offer conferences, director training programs, roundtables, an extensive database, and timely research.

Financial Executives International www.fei.org

Financial Executives International (FEI) is a professional association for senior level financial executives including chief financial officers, vice presidents of finance, controllers, treasurers, and tax executives. FEI provides peer networking opportunities, emerging issues alerts, and personal and professional development and advocacy services.

Harvard Business School's Corporate Governance, Leadership & Values www.cglv.hbs.edu

Harvard Business School's Corporate Governance, Leadership & Values Web site is a comprehensive overview of research, educational programs, and other activities at Harvard Business School aimed at providing new frameworks for thought and practice in the interrelated areas of corporate governance, leadership, and values. It includes links to the ongoing workshop series; background papers; research programs, such as the corporate governance initiative; executive education programs; viewpoints on key issues published in the national press; faculty comments in the media; and an online forum for exchanging views on emerging issues.

National Association of Corporate Directors (NACD) www.nacdonline.org

Founded in 1977, the NACD is the premier educational, publishing, and consulting organization in board leadership and the only membership association for boards, directors, director-candidates, and board advisers. The NACD promotes high professional board standards, creates forums for peer interaction, enhances director effectiveness, asserts the policy interests of directors, conducts research, and educates boards and directors concerning traditional and cutting-edge issues.

New York Stock Exchange www.nyse.com

The New York Stock Exchange (NYSE) is a not-for-profit corporation that provides a self-regulated marketplace for the trading of financial instruments. Its goal is to add value to the capital-raising and asset-management process by providing the highest quality and most cost-effective trading environment. They work to promote confidence in and understanding of the financial trading process and serve as a forum for the discussion of relevant national and international policy issues. They have taken a leadership role in corporate governance issues through their participation in the Blue Ribbon Committee on Improving the Effectiveness of Corporate Audit Committees and more recently in their formation of the NYSE Corporate Responsibility and Listing Standards Committee.

The Corporate Library www.thecorporatelibrary.com

The Corporate Library serves as a central repository for research, study, and critical thinking about the nature of the modern global corporation, with a special focus on corporate governance and the relationship between company management, boards, and shareholders. Most general content on the site is open to visitors at no cost; advanced research relating to specific companies and certain other advanced features are restricted to subscribers only.

