DCAAM 7640.1, DCAA Contract Audit Manual
Chapter 2
Auditing Standards

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2-000 Auditing Standards **

2-001 Scope of Chapter **

This chapter discusses the professional standards applicable to engagements performed by DCAA audit teams. Our professional standards relate to conducting audit and attestation engagements to ensure the quality of the work performed meets the engagement objectives. The professional standards applicable to DCAA provide a framework for performing high-quality audit and attestation engagements with competence, integrity, objectivity, and independence. Ensuring our work adheres to our professional standards directly supports the DCAA mission by allowing us to provide accurate reliable financial information to relevant stakeholders, enabling those stakeholders to make informed decisions with confidence. This helps to ensure the integrity of Department of War (DoW) acquisitions while supporting public trust in the reliability of financial information that supports the defense of our nation.

2-100 Auditing Standards and DCAA Audits **

2-101 Generally Accepted Government Auditing Standards (GAGAS) **

a. DoD Instruction 7600.02, "Audit Policies," incorporates the Government Auditing Standards (GAGAS) issued by the Comptroller General of the United States Government Accountability Office (GAO). These standards are commonly referred to as GAGAS or the "Yellow Book" interchangeably. As prescribed in DoD Directive 5105.36, "Defense Contract Audit Agency," DCAA provides contract audit services for all of DoW and performs audits and attestation engagements in accordance with GAGAS.

b. GAGAS incorporates the American Institute of Certified Public Accountants (AICPA) auditing and attestation standards by reference. Therefore, in order to comply with GAGAS, DCAA auditors must also comply with relevant AICPA standards. The AICPA's Statements on Standards for Attestation Engagements (SSAE) are codified in designated AT-C sections and apply to all attestation engagements conducted by DCAA, including agreed-upon procedures engagements.

c. The current revision of GAGAS was issued in February 2024 and is available on the GAO web site. The 2024 revised standards are effective for attestation engagements and performance audits for periods beginning on or after December 15, 2025.

d. All engagements begin with objectives, and the objectives determine the type of engagement to be performed and the auditing standards to be followed.

- For all engagements performed in accordance with the 2024 GAGAS revision, chapters 1 through 5 apply (see CAM 2-202 – 2-206).
- Standards specific to attestation engagements are included in chapter 7 of the 2024 GAGAS revision (see CAM 2-207). Because the majority of DCAA engagements are attestation engagements, audit teams should familiarize themselves with this chapter, as well as chapters 1 through 5.
- Standards specific to performance audits are included in chapters 8 and 9 of the 2024 GAGAS revision (see CAM 2-400).
- Audit teams should also consider any applicable GAO issued GAGAS interpretive guidance.

e. DCAA uses the terms examination and audit interchangeably when referring to examination-level attestation engagements. DCAA also uses the terms engagement team and audit team interchangeably when referring to the personnel performing and managing audits and attestation engagements.

2-102 AICPA Attestation Standards **

a. For attestation engagements, GAGAS incorporates the AT-Cs unless specifically excluded or modified by GAGAS. The AT-Cs establish requirements and provide application guidance for performing and reporting on examinations and agreed-upon procedures engagements. The AT-C sections that are applicable to work performed by DCAA are AT-C section 105 - Concepts Common to All Attestation Engagements, AT-C section 205 - Assertion-Based Examination Engagements, AT-C section 215 - Agreed-Upon Procedures Engagements, and AT-C section 315 - Compliance Attestation (see CAM 2-300). The codified AT-Cs are available on the AICPA's website.

b. DCAA's attestation engagements are performed either as examinations or agreed-upon procedures engagements in order to report on a subject matter that is the responsibility of another party. It is important to identify the assertion or subject matter being reported on (e.g., incurred cost proposal, price proposal, a contractor's business system; where the assertion is obtained from; and criteria, such as contract terms, legislation, or regulations), and the needs of the intended user, when determining the type of engagement that is appropriate in the circumstances.

2-103 Advisory Services **

a. DCAA also provides advisory services, other than audits or attestation engagements, to federal government agency officials with cognizance over the contractors we audit. DCAA advisory services are not the same as the nonaudit services discussed in GAGAS 3.64–3.106. The nonaudit services discussed in GAGAS are related to services provided by the auditor to the audited entity. We do not provide any services to the entities (e.g., contractors) we audit.

b. An advisory service is not conducted in accordance with GAGAS, does not provide an audit opinion, and provides no level of assurance on the subject matter or assertion.

c. The auditor should clearly communicate to the requestor that the advisory service is not an audit or attestation engagement performed under GAGAS, does not provide an opinion on the subject matter, and provides no level of assurance on the subject matter or assertion. Memorandums with the results of an advisory service performed must include the following statement:

> *The scope of work performed does not constitute an audit or attestation engagement under generally accepted government auditing standards.*

2-104 Communication with the Audited Entity **

a. Auditors must exercise caution when providing input and feedback on contractor submissions to avoid creating an impairment to the auditor's independence or giving the appearance of an impairment to the auditor's independence. Feedback provided to the contractor should be limited to what the contractor is required to do (for example, cite the contract term, FAR, or DFARS criteria with which they need to comply, general information for what is required for an adequate proposal, general discussion of the proposal adequacy checklist, or explaining the requirements for adequate cost or pricing data).

2-200 Government Auditing Standards **

2-201 Introduction **

This section discusses the professional standards in GAGAS applicable to the engagements performed by DCAA. These standards provide a framework for performing high-quality audit work with competence, integrity, objectivity, and independence. Engagements conducted under these standards provide accountability and help to improve government operations and services.

DCAA auditors must also comply with the standards of conduct contained in DoD Directive 5500.07, Ethics and Standards of Conduct, and the Joint Ethics Regulation.

2-202 Foundation and Principles of GAGAS (GAGAS 1.01 – 1.28) **

GAGAS Chapter 1 discusses the foundation and principles of GAGAS. This section provides a brief overview of the types of engagements that can be performed in accordance with GAGAS and the terminology used in GAGAS.

2-202.1 Types of Engagements in GAGAS (GAGAS 1.13 – 1.26) **

The professional standards that comprise GAGAS address three broad categories of engagements: financial audits, attestation engagements, and performance audits. Attestation engagements are further divided into three subcategories, including examinations, reviews, and agreed-upon procedures engagements. Each provides different levels of assurance in relation to the auditor's opinion, findings, or conclusions. DCAA primarily performs examination-level attestation engagements.

2-202.2 Terminology (GAGAS 1.27) **

GAGAS 1.27 includes a description of some common terms used in GAGAS. The terminology addressed in GAGAS 1.27 is not, however, comprehensive. The terminology used throughout GAGAS is often specific and conveys a specific meaning within the requirements intended to facilitate compliance with the professional standards. Audit teams are encouraged to consult the glossary in GAGAS and to pay particular attention to the terminology used in both the GAGAS requirements paragraphs, as well as in the application guidance that relates to the requirements paragraphs to ensure a complete understanding of the intent of the standards.

2-203 General Requirements (GAGAS 2.01 – 2.23) **

GAGAS Chapter 2 addresses general requirements that are applicable to all GAGAS engagements. These include differentiating between unconditional and presumtively mandatory requirements, describing the relevance and applicability of application guidance and interpretive guidance, explaining the relationship between GAGAS and other professional standards, and the requirement to cite compliance with GAGAS in the audit report.

2-203.1 Complying with GAGAS (GAGAS 2.02 – 2.10) **

a. GAGAS includes two categories of requirements – unconditional requirements and presumptively mandatory requirements.

(1) GAGAS uses “must” to indicate an unconditional requirement, and auditors must comply with unconditional requirements when those requirements are relevant.

(2) GAGAS uses “should” to indicate presumptively mandatory requirements. Auditors may, in rare circumstances, determine it necessary to depart from a presumptively

mandatory requirement. If auditors depart from a presumptively mandatory requirement they must (i) understand the intent of the presumptively mandatory requirement, (ii) perform alternative procedures necessary to achieve the intent of that requirement, and (iii) document justification for the departure and how the alternative procedures met the intent of the presumptively mandatory requirement.

b. GAGAS contains explanatory material in the form of application guidance. The application guidance provides further explanation of the requirements and may explain more precisely what a requirement means or is intended to address. While application guidance does not impose a requirement, it is relevant to the proper application of the requirements. Audit teams should have an understanding of the entire text of the relevant GAGAS requirements and related application guidance to understand the intent of the requirements and to apply the requirements properly.

**2-203.2 Relationship Between GAGAS and Other Professional Standards (GAGAS 2.11 – 2.15) **

For attestation engagements, GAGAS incorporates by reference the AICPA's codified attestation standards (AT-Cs). GAGAS does not incorporate by reference any other professional standards for performance audits. Audit organizations may also elect to use standards promulgated by the International Auditing and Assurance Standards Board (IAASB) and the PCAOB in conjunction with GAGAS. However, DCAA has chosen not to adopt IAASB and/or PCAOB standards in the conduct of its attestation engagements.

The AT-C requirements incorporated into GAGAS by reference, including their applicability to DCAA audits, are discussed in more detail in section CAM 2-300.

**2-203.3 Stating Compliance with Generally Accepted Government Auditing Standards (GAGAS 2.16 – 2.23, 7.39 – 7.41, and 9.03 – 9.05) **

a. DCAA reports must include a statement of compliance with GAGAS.

b. When an audit is conducted in accordance with GAGAS, the report should include an unmodified GAGAS compliance statement. An unmodified statement is used when the audit team complied with:

(1) Unconditional and applicable presumptively mandatory GAGAS requirements, or

(2) Unconditional requirements with departure from applicable presumptively mandatory requirements, when the justification for any departures are documented and the alternative procedures achieved the intent of the presumptively mandatory requirements.

c. If GAGAS requirements are not complied with, perform the following:

(1) assess the significance of the noncompliance to the audit objectives;

(2) document that assessment and the reasons the requirement was not followed, whether alternative procedures were performed to meet the intent of the requirement; and

(3) determine the appropriate statement of GAGAS compliance for the report. This determination is a matter of professional judgment and is affected by the significance of the requirement(s) not followed in relation to the audit objectives.

d. When some of the applicable standards are not complied with during the audit, the statement of compliance with GAGAS should be modified depending on the significance of the departure as follows:

(1) The auditor performed the engagement in accordance with GAGAS, except for specific applicable requirements that were not followed, or

(2) Because of the significance of the departure(s) from the requirements, the auditor was unable to and did not perform the engagement in accordance with GAGAS.

e. Other situations that require use of a modified statement of compliance with GAGAS include scope limitations, such as restrictions on access to records, restrictions preventing access to officials or other individuals needed to conduct the audit, time constraints that did not permit completing all necessary audit procedures, etc.

f. When a modified statement of compliance with GAGAS is used, the report should disclose the requirement(s) not followed, the reason for the departure, the impact of not following the requirements and how the departure affects the audit results and assurance provided. This information is included in WP A and in the "Basis for Opinion" section of the audit report.

2-204 Ethics, Independence, and Professional Judgment (GAGAS 3.01 – 3.117) **

GAGAS Chapter 3 addresses ethical principles for auditors in the government environment, independence requirements and the conceptual framework approach to independence, and the standards for professional judgment in all GAGAS engagements.

2-204.1 Ethical Principles (GAGAS 3.02 – 3.16) **

GAGAS includes ethical principles that guide the work of auditors who conduct engagements in accordance with GAGAS. These ethical principles are separate from, and complimentary to, ethics laws and regulations that DCAA auditors are also required to follow. Auditors are encouraged to read GAGAS 3.02 through 3.16 to better understand the GAGAS ethical principles. The ethical principles that guide the work of auditors are found in GAGAS 3.06.

2-204.2 Independence and Conceptual Framework Approach to Independence (GAGAS 3.17 – 3.25 and 3.26 – 3.51) **

GAGAS states that in all matters relating to the audit work, each individual auditor must be independent from the audited entity. GAGAS Chapter 3 establishes a conceptual framework to identify and evaluate threats to independence, apply safeguards, and document the evaluation of independence. DCAA policy related to independence is in DCAA Instruction 7642.9. In addition, audit staff are required to complete annual independence training.

2-204.3 Independence for Government Auditors and Audit Organizational Structure (GAGAS 3.52 – 3.56) **

DoD Directive 5105.36 established DCAA as an independent agency responsible for performing contract audits for the DoW. DCAA is organizationally independent because DCAA does not audit other DoW entities.

2-204.4 Independence Considerations when Performing an Advisory Service **

a. GAGAS recognizes a variety of circumstances, or combinations of circumstances, relevant to identifying threats to independence. In addition to applying the GAGAS conceptual framework for independence to attestation engagements and performance audits, it can also be applied when we are requested to provide advisory services. Identifying and evaluating threats and applying safeguards for advisory services is no different from the process used in applying the conceptual framework for attestation engagements and performance audits.

b. To avoid situations that may result in impairment to independence, DCAA audit teams only perform advisory services that will not impair independence. Audit teams should follow agency procedures when accepting and performing advisory services.

2-204.5 Professional Judgement (GAGAS 3.109 – 3.117) **

a. Professional judgement is used throughout the audit process. Auditors must use professional judgment in planning and performing audits and attestation engagements and in reporting the results.

b. Professional judgment is required to determine the type of engagement or service to be performed, establishing the audit scope, assessing the level of audit risk, and designing the methods and procedures to be used to evaluate the subject matter. The auditor must understand the purpose of the audit and the scope of audit necessary to meet the audit objectives, and remain mentally alert and questioning while performing in all phases of the engagement, including assessing risk, performing tests and procedures to evaluate the subject matter, and in reporting the audit results.

c. Auditors must document their rationale for decisions made based on professional judgment related to matters that are significant to the engagement (e.g., assessing sufficiency of evidence, determining areas of risk, procedures designed to address audit risk, conclusions reached, etc.). This includes developing documentation that is sufficient to permit a third-party reviewer (e.g., the IRR reviewer or external reviewers) to understand the rationale for the decisions reached by reviewing the documentation. Auditors should ensure the documentation includes information that is inherent to the audit team but is an integral part of the rationale for reaching a conclusion (e.g., long experience with the contractor makes some knowledge "common knowledge" among the audit team, but if an outside reviewer would not understand the rationale without this "common knowledge", then the documentation should also include the "common knowledge").

d. Professional judgment is crucial in determining the sufficiency and appropriateness of evidence obtained to support the findings and conclusions and any recommendations reported.

e. GAGAS places responsibility on each auditor and audit organization to exercise professional judgment in planning and performing GAGAS engagements. It does not, however, imply unlimited responsibility or infallibility on the part of the individual auditor or audit organization. Absolute assurance is not attainable because of the nature of evidence and the characteristics of fraud. An audit conducted in accordance with GAGAS may not detect a material misstatement or significant inaccuracy, noncompliance with provisions of contracts or grant agreements, or abuse. Professional judgment does not mean eliminating all possible limitations or weaknesses associated with a specific audit, but rather identifying, considering, minimizing, mitigating, and clearly explaining them.

2-205 Competence and Continuing Professional Education (GAGAS 4.01 – 4.53) **

GAGAS Chapter 4 addresses requirements for competence and continuing professional education (CPE). Competence includes both understanding the specific GAGAS requirements as well as being able to proficiently apply that knowledge on GAGAS engagements. CPE contributes to competence by allowing audit teams to maintain the knowledge, skills, and abilities necessary to conduct GAGAS engagements.

2-205.1 Competence (GAGAS 4.02 – 4.15) **

a. GAGAS requires that those assigned to each audit collectively possess adequate professional competence to address the audit objectives and perform the work, and that prior to beginning work effort, each auditor possesses the competence to perform his or her assigned role. Competence for each engagement must be assessed at both the individual auditor and engagement team levels.

b. Competence is the knowledge, skills, and abilities, obtained from education and experience, necessary to conduct the engagement. Competence enables audit teams to make sound professional judgments and includes possessing specific knowledge about GAGAS, as well as the technical knowledge and skills necessary for the assigned role and the type of work being performed. DCAA policies and procedures for staff competence are an integral element of the DCAA quality management system.

c. The standards do not exclude the use of auditors in a training status, as long as trainees are assigned duties commensurate with their experience, have the competence necessary to perform their assigned role, and are adequately supervised.

d. Auditor proficiency in the knowledge, skills and abilities needed to conduct the engagement in accordance with GAGAS help ensure engagements are performed in compliance with the GAGAS requirements.

e. When assistance from specialists in other disciplines, such as DCAA legal, or the contracting officer's project management team (e.g., engineering or construction specifications, labor hours, etc.) is needed, make arrangements as early in the engagement as possible to help ensure the technical assistance report can be provided timely for consideration in audit findings and the report opinion.

2-205.2 Continuing Professional Education (GAGAS 4.16 – 4.53) **

Continuing education contributes to auditors being competent to plan and perform the engagement in compliance with GAGAS. DCAA Instruction 1400.2 includes the responsibilities of all parties required to comply with these GAGAS requirements.

2-206 Quality Management (GAGAS 5.01 – 5.190) **

a. Each audit organization performing GAGAS engagements must design, implement, and operate a system of quality management sufficient to provide reasonable assurance that the organization and its personnel fulfill their responsibilities in accordance with professional standards and applicable laws and regulations, and perform and report on engagements in accordance with such standards and requirements. DCAA's quality management system encompasses all elements of the Agency's operations dedicated to conducting and supporting our audit and attestation engagements and places emphasis on performing high-quality work.

b. DCAA has designed, implemented, and maintains a comprehensive quality management system. Elements of the Agency's Quality Management System are embedded throughout our internal guidance and processes.

2-207 Standards for Attestation Engagements (GAGAS 7.01 – 7.85) **

This section describes requirements specific to attestation engagements performed in accordance with GAGAS.

2-207.1 Overview of GAGAS Attestation Standards (GAGAS 7.01 – 7.04) **

GAGAS Chapter 7 contains requirements and guidance for conducting and reporting on attestation engagements. The requirements in GAGAS Chapters 1 – 5 are also applicable to all GAGAS engagements, including attestation engagements.

2-207.2 Compliance with Standards (GAGAS 7.05 – 7.06) **

GAGAS establishes requirements for conducting examination-level attestation engagements that are in addition to the standards for examination-level attestation engagements established by the AICPA. Auditors are required to comply with the relevant AT-Cs, in addition to the requirements contained in GAGAS.

2-207.3 Communication (GAGAS 7.09 – 7.12) **

GAGAS requires appropriate communication of information the auditor believes should be conveyed to the contracting officer and the contractor. Also, when a deficiency or noncompliance that is significant or requires urgent corrective action is discovered during the audit, auditors should assess whether early communication of the deficiency or noncompliance is necessary. Early communication of significant or urgent deficiencies or noncompliances does not affect other relevant reporting requirements.

2-207.4 Management Inquiries (GAGAS 7.13 – 7.18) **

a. GAGAS includes requirements for several inquiries of audited entity management, including the expansion of some inquiries also required in the AT-Cs. These include the requirement to ask audited entity management about:

(1) previous audits, attestation engagements, and other studies directly related to the subject matter or assertion about the subject matter, and whether any corrective actions have been taken to address findings from previous engagements;

(2) whether any investigations or legal proceedings significant to the engagement objectives have been initiated or are in process with respect to the period under examination; and

(3) whether audited entity management is aware of any actual fraud, suspected fraud, or alleged fraud, or noncompliances with laws, regulations, or provisions of contracts or grant agreements affecting the subject matter.

b. While audit teams are expected to use this information to evaluate the effect on the current examination engagement in assessing risk and determining the nature, timing, and extent of current work necessary, these inquiries also pose unique challenges associated with addressing fraud and potential fraud in examination engagements. For example, one purpose for the inquiry in GAGAS 7.14 is to identify items that need to be reported to law enforcement or investigatory authorities, and to identify areas where action needs to be taken to avoid interfering with investigations and legal proceedings.

(1) Avoiding interference with investigations or legal proceedings is important in pursuing indications of fraud, noncompliance with provisions of laws, regulations, contracts, or grant agreements. Laws, regulations or policies may require auditors to report indications of certain types of fraud and noncompliance with provisions of laws, regulations, contracts, or grant agreements to law enforcement or investigatory authorities before performing additional audit procedures.

(2) When investigations or legal proceedings are initiated or are in process, auditors should evaluate the impact on the current examination engagement. In some cases, it may be appropriate for the auditors to work with investigators or legal authorities, cancel the engagement, or reduce the scope of the engagement to avoid interfering with the investigation or legal proceeding.

(3) Inquiries made to contractor management to identify other studies or audits that directly relate to the subject matter under audit may assist the auditor in identifying ongoing investigations or legal proceedings that may need to be considered in planning the engagement to avoid interfering with investigations or legal proceedings.

2-207.5 Findings (GAGAS 7.19 – 7.32) **

a. When auditors identify findings, sufficient procedures should be planned and performed to enable the auditor to develop the elements of the findings that are relevant and necessary to achieve the engagement objectives. The elements of a finding should be developed to assist the contracting officer in understanding the finding and the need for corrective action.

b. A finding or set of findings is complete to the extent that the engagement objectives are satisfied. The elements of a finding include the criteria, condition, cause, and effect or potential effect. When developing the cause element, auditors should consider internal control deficiencies. See the Elements of a Finding guidebook for details related to developing and reporting audit findings that are useful to the contracting officer and compliant with auditing standards.

2-207.6 Documentation (GAGAS 7.33 – 7.38) **

Documentation requirements relevant to examination-level attestation engagements are described in AT-C 105.57 – 105.64 and AT-C 205.89 – 205.90. Additional documentation requirements, described in GAGAS 7.33 – 7.38, supplement the requirements included in the AT-Cs. See CAM 2-302.1 for a summary regarding documentation requirements included in the AT-Cs.

2-207.7 Reporting Requirements (GAGAS 7.39 – 7.69) **

The reporting requirements for examination-level attestation engagements in GAGAS 7.39 – 7.69 supplement, and in some cases replace, the reporting requirements in AT-C 205.63 – 205.68 and AT-C 315.20 – 315.22. These include requirements such as reporting the auditor's compliance with GAGAS, presenting findings in the report, and obtaining the views of responsible officials. CAM Chapter 10 provides general guidance regarding preparation and distribution of DCAA audit reports. Audit teams are encouraged to become familiar with the reporting requirements in GAGAS 7.39 – 7.69 to ensure compliance with requirements relevant to their individual engagements and CAM Chapter 10.

2-207.8 Agreed-Upon Procedures Engagements (GAGAS 7.78 – 7.85) **

Agreed-upon procedures engagements are conducted in accordance with GAGAS 7.78 – 7.85, AT-C section 105, AT-C section 215, and the relevant portion of AT-C section 315 related to agreed-upon procedures engagements. An agreed-upon procedures engagement is an engagement in which the auditor performs specific procedures on subject matter or an assertion and reports the findings without providing an opinion or a conclusion. The intended users assess for themselves the procedures and findings reported by the auditor and draw their own conclusions from the work performed by the auditor.

2-300 AICPA Attestation Standards Incorporated by Reference **

2-301 Introduction and Applicability **

As explained in CAM 2-101, GAGAS incorporates the AT-Cs by reference (see GAGAS 2.13.a and 7.01), unless otherwise excluded or modified by specific GAGAS requirements. This section provides information for conducting attestation engagements in accordance with the AT-Cs incorporated into GAGAS. The AT-Cs are a principles-based set of professional standards designed to ensure the engagement team achieves the engagement objectives. As such, audit teams should obtain an understanding of the AT-Cs.

The AT-Cs utilize a "building blocks" approach which scales requirements based on common concepts, the level of service provided, and the specific subject matter of the engagement.

- The Foundation (AT-C section 105, Concepts Common to All Attestation Engagements): Establishes the core requirements applicable to every attestation engagement, including requirements for planning, competence, and professional judgment.
- The Levels of Service (AT-C section 205, Examination Engagements and AT-C section 215, Agreed-Upon Procedures Engagements): These AT-C sections define the auditor's responsibilities based on the level of service being provided. AT-C section 205 is relevant for examination-level attestation engagements when the audit team is required to obtain reasonable assurance to express an opinion on whether a contractor's assertion or subject matter is in compliance with specified criteria (e.g., Incurred Cost or Forward Pricing). AT-C section 215 is relevant when the engagement team is requested to perform specific procedures agreed upon by the engagement team and the requesting party (typically a contracting officer) and report the results as findings without expressing an opinion or conclusion.
- The Subject Matter (AT-C section 315, Compliance Attestation): AT-C section 315 establishes specialized requirements when the subject matter involves compliance. Because DCAA's mission is to determine contractor compliance with FAR, DFARS, CAS, and contract terms, audit teams must integrate these criteria-specific requirements into their examination and agreed-upon procedures engagements.

2-302 The Foundation (AT-C Section 105, Concepts Common to All Attestation Engagements) **

The building blocks approach starts with the AT-C 100 series, which addresses concepts common across all attestation engagements. Its only section, AT-C section 105, establishes the mandatory prerequisites, such as professional judgment and professional skepticism, required for every assignment. By providing this baseline, AT-C section 105 ensures that the subsequent building blocks used to achieve engagement objectives are supported by rigorous professional standards.

2-302.1 Concepts Common to All Attestation Engagements (AT-C Section 105) **

a. This section addresses requirements that are common to all attestation engagements.

b. Conducting Engagements in Accordance with AT-Cs. When performing an attestation engagement, audit teams are required to comply with the AT-C sections that are relevant to the engagement. This means the auditor should comply with:

- For examination-level attestation engagements, AT-C section 105, Concepts Common to All Attestation Engagements, AT-C section 205, Assertion-Based Examination Engagements, and AT-C section 315, Compliance Attestation (limited to the requirements that are relevant to examinations).
- For agreed-upon procedures engagements, AT-C section 105, AT-C section 215, Agreed-Upon Procedures Engagements, and AT-C section 315 (limited to the requirements that are relevant to agreed-upon procedures engagements).

Like GAGAS, the AT-Cs include two categories of requirements – unconditional requirements and presumptively mandatory requirements. Audit teams must comply with unconditional requirements and may depart from a relevant presumptively mandatory requirement in rare circumstances, subject to additional alternative procedures and documentation requirements described in CAM 2-203.1.

c. Suitable Criteria. Examination-level attestation engagements require the underlying subject matter to be measured or evaluated in accordance with suitable criteria. The suitability of criteria is context-sensitive, that is, it is determined in the context of the engagement circumstances. As a result, the auditor must have reason to believe that the subject matter is capable of evaluation against criteria that are suitable and available to users. Criteria are suitable when they exhibit all of the following attributes (AT-C 105.A51):

(1) Relevance –Criteria are relevant to the subject matter.

(2) Objectivity – Criteria are free from bias.

(3) Measurability – Criteria permit reasonably consistent measurements, qualitative or quantitative, of the subject matter.

(4) Completeness – Criteria are complete when subject matter prepared in accordance with them does not omit relevant factors that could reasonably be expected to affect decisions of the intended users made on the basis of that subject matter.

d. Understanding the Requirements. To correctly interpret and apply the intent of any individual requirements paragraphs, audit teams should understand the entire text of each AT-C section, including the application guidance and explanatory material, that is relevant in the engagement circumstances.

e. Acceptance and Continuance of Engagements. DCAA's policies and procedures for the initiation, acceptance, and continuance of engagements are derived from DoD Directive 5105.36, Defense Contract Audit Agency. This directive establishes DCAA as the entity responsible for performing all contract audits for the Department of War. Our policies and procedures related to the initiation, acceptance, and continuance of engagements include annual and multi-year planning processes, work plan and resource monitoring, categorization of specific engagement types around compliance criteria, customer survey and liaison activities, and engagement quality monitoring processes. These processes are designed to ensure the preconditions for an attestation engagement are present when the engagement is initiated or accepted. All DCAA engagements are three-party engagements, and each engagement includes a Government acquisition customer.

f. Acceptance of a Change in the Terms of the Engagement. An examination-level attestation engagement may, under certain circumstances, be converted to an agreed-upon procedure engagement. This is typically due to the requestor's desire to change to an agreed-upon procedure engagement resulting from changes in circumstances that affect the requestor's requirements, or a misunderstanding about the nature of the original services agreed-to or lack of awareness that alternative services were available. However, an examination may not be converted to an agreed-upon procedures engagement merely to avoid disclosing a scope limitation. Before an examination engagement is converted to an agreed-upon procedures engagement, consider the following:

- Are the procedures already performed as part of an examination appropriate for inclusion in an agreed-upon procedures engagement?
- Is the rationale for changing to an AUP engagement sound?
- How much additional effort is required to complete the examination engagement? Is the original engagement substantially complete or is the effort to complete relatively insignificant?

When converting to an agreed-upon procedures engagement, the auditor will issue a revised acknowledgement memorandum to the requestor specifying the scope of engagement and the procedures to be performed and obtain an acknowledgement from the requestor that the procedures are appropriate for the intended purposes. The agreed-upon procedures engagement report should not reference the original engagement or document that the engagement was changed from an examination engagement.

g. Documentation. Engagement documentation, commonly referred to as working papers, should be sufficient to determine:

(1) the auditor's understanding with the requestor/ACO regarding the services to be performed;

(2) the engagement objectives, scope of the examination, methodology for assessing risk and performing field work;

(3) the nature, timing, and extent of procedures performed, including:

- identifying characteristics of specific items or matters tested,
- who performed the engagement work and the date the work was completed,
- discussions with the contractor or requestor/ACO, as applicable, about findings or issues that are significant. The documentation should identify when and with whom the discussions took place,

- who reviewed the engagement work performed and the date and extent of such review,
- results of the procedures performed and the evidence obtained.

(4) evidence supporting all significant findings, conclusions, professional judgments, and recommendations. This includes explanations for the auditor's rationale on all significant findings or issues that require the exercise of professional judgment and related conclusions, to include the relevant facts that were known by the auditor at the time the conclusion was reached;

(5) how the auditor addressed information that was inconsistent with the final conclusion;

(6) documentation that provides the evidence to support the auditors' statement of compliance with GAGAS in the audit report;

(7) if the auditor found it necessary to depart from a relevant, presumptively mandatory requirement, the auditor must document the justification for the departure and how alternative procedures performed in the circumstances were sufficient to achieve the intent of the requirement;

(8) if there is a change in the engagement objectives, the auditor should document the revised engagement objectives and the reasons for the change.

h. Documentation – Additional Considerations.

(1) Engagement documentation should be prepared on a timely basis.

(2) When the timeliness of an audit report is critically important, it may be acceptable to issue the report before non-critical working papers are complete. Non-critical working papers (generally administrative working papers) are those that do not impact obtaining and evaluating sufficient appropriate evidence supporting significant findings, judgments, conclusions, and recommendations. The auditing standards require all working papers to be completed within 60 days of issuing the report.

i. Professional Skepticism and Professional Judgement. Professional skepticism and professional judgment are crucial to performing a GAGAS engagement.

j. Quality Management and Engagement Quality Reviews. The engagement partner should take responsibility for the overall management of, and achievement of quality on, the engagement. In DCAA, the engagement partner is generally the Branch Manager or similar level of management. Taking responsibility for the overall management and achievement of quality on the engagement includes ensuring that sufficient and appropriate resources necessary to perform the engagement are assigned or made available to the engagement team in a timely manner, that the engagement team, collectively, has the appropriate knowledge and competence necessary to complete the engagement, remaining appropriately involved in the engagement throughout the engagement, and ensuring the final report is not issued until the engagement quality review, if applicable, has been completed and all issues resulting from the engagement quality review have been resolved.

k. Proper Supervision and Management. Additional details regarding the responsibilities of managers, supervisors, and other engagement team members are outlined in DCAAI 7642.2, Management Review and Technical Support of Audits.

2-303 The Levels of Service (AT-C Section 205, Examination Engagements and AT-C Section 215, Agreed-Upon Procedures Engagements) **

The AT-C building blocks continue with the AT-C 200 series, which addresses the levels of service that may be provided in attestation engagements. AT-C 200 is comprised of four sections. These AT-C sections are the second level of the AT-C building blocks that set the baseline standards applicable to each level of service that can be provided under the AICPA's attestation standards.

2-303.1 Types of Attestation Engagements **

The attestation standards provide for three levels of service. These are examination engagements, review engagements, and agreed-upon procedures engagements. DCAA performs examination-level attestation engagements and agreed-upon procedures engagements. Requirements for examination-level attestation engagements are addressed in AT-C section 205, Assertion-Based Examination Engagements, and AT-C section 206, Direct Examination Engagements. Requirements for agreed-upon procedures engagements are addressed in AT-C section 215, Agreed-Upon Procedures Engagements. AT-C section 210 covers review-level attestation engagements. However, because the attestation standards prohibit the performance of review engagements for compliance with requirements of specified laws, regulations, rules, contracts, and grants, DCAA does not currently perform any type of review engagement. Auditors should also be aware that while AT-C section 206 provides requirements for direct examination engagements, AT-C section 206 is not applicable to the types of attestation engagements performed by DCAA.

2-303.2 Examination-Level Attestation Engagements (AT-C Section 205) **

a. Objective. The objective of the auditor in conducting an examination-level attestation engagement is to obtain reasonable assurance, expressed in the form of an opinion, about whether the audited entity complied, in all material respects, with the specified requirements. Reasonable assurance is a high level of assurance, and the auditor obtains reasonable assurance by obtaining sufficient appropriate evidence about the subject matter of audit in order to draw reasonable conclusions on which to base the auditor's opinion.

b. Communication. Prior to accepting the engagement, the audit team should communicate with the requestor or responsible government official, as applicable, to agree on the terms of the engagement. The agreed-upon terms should be in writing, and each standard audit program has a proforma acknowledgement letter or memorandum, depending on the type of service being provided.

(1) The written agreed-upon terms should include the following information:

(a) The objective and scope of the engagement,

(b) The level of assurance the report will provide. This will generally be the type of engagement/audit service provided; e.g., examination with an opinion,

(c) The auditor's responsibilities,

(d) A statement identifying whether the engagement will be conducted in accordance with GAGAS,

(e) The requestor or responsible government official's responsibilities,

(f) A statement about the inherent limitations of an examination engagement,

(g) Identification of the criteria that will be used for the measurement, evaluation, or disclosure of the subject matter, and

(h) Restrictions in the audit report regarding use of audit report. For example, DCAA audit reports generally include restrictions regarding the release of the report to other parties due to proprietary information and also warn that the report should not be used for purposes other than those for which the engagement was conducted.

(2) Auditors should also communicate the above information to appropriate representatives of the audited entity. This is generally provided through the contractor notification letter and at the entrance conference.

c. Risk Assessment and Adequate Planning. All DCAA audit engagements must be adequately planned and properly supervised to comply with professional standards and applicable legal and regulatory requirements. Engagements must be planned and performed to obtain sufficient appropriate evidence that provide a reasonable basis for conclusions expressed in the report.

(1) Before beginning an engagement, it is essential to coordinate with contracting officials requesting the audit or those responsible for dispositioning findings and acting on recommendations. The auditor needs to understand the contracting officer/requestor's needs and/or specific concerns, and be familiar with contractual, regulatory, or other factors pertinent to the engagement in order to determine the type of engagement to be performed.

(2) The understanding with the requestor should include reaching an agreement on the objectives of the engagement, responsibilities of the parties, any limitations of the engagement, anticipated time frame for completing the engagement, and how the results will be conveyed (i.e., through an audit report, memorandum, etc.). Communications with the requestor demonstrating the auditor's understanding with the requestor must be documented in the working papers through written communication with the appropriate official. An attestation engagement should be performed only when:

- all relevant ethical requirements, including independence, will be satisfied,
- the engagement team is competent to perform the engagement,
- the engagement meets all the preconditions for an attestation engagement,
- a common understanding with the requestor has been reached in the terms of the engagement, including the auditor's reporting responsibilities.

(3) Proper planning directly influences the selection of appropriate procedures and the timeliness of their application. Planning an examination engagement involves developing an overall strategy that sets the scope, timing, and direction of the engagement and guides the development of the audit plan. The audit team needs to have sufficient knowledge to determine the events, transactions, and practices that have a significant effect on the subject matter or assertion.

(4) Attestation risk is the risk that the auditor will determine that the subject matter or assertion is in compliance with the criteria when it contains material noncompliances. In general, attestation risk is composed of inherent risk, control risk, and detection risk, although all three of

these components may not be present or significant for a given engagement. In order to prepare an appropriately detailed audit program, the audit team must perform a risk assessment to assess the attestation risk relative to the audit objectives.

(5) Because an examination-level attestation engagement provides a high level of assurance on whether the subject matter or assertion is in compliance with the criteria in all material respects, the audit team should establish an appropriately low-level of attestation risk to support the high level of assurance provided.

(6) A properly performed risk assessment should provide information about risk factors relevant to the subject matter of the audit. In planning the engagement, the audit team should use the information obtained during the risk assessment to identify types of potential noncompliances and factors that may impact the risk of material noncompliance in order to appropriately design further procedures (i.e., tests of controls, if relevant, tests of details, and substantive analytical procedures) to obtain sufficient appropriate evidence to achieve the objectives of the audit and form an opinion.

(7) Managers and Supervisors should ensure that audit team members understand their responsibilities, including the objectives of the procedures they are to perform and matters that may affect the nature, timing, and extent of such procedures.

d. Attestation Risk, Inherent Risk, Control Risk, and Detection Risk. As explained in CAM 2-303.2c(4) above, attestation risk is the risk that the auditor expresses an inappropriate opinion when the subject matter or assertion is materially misstated. Attestation risk is comprised of inherent risk, control risk, and detection risk. CAM Chapter 3 discusses these concepts in more detail as part of the audit planning process.

e. Forming the Opinion. In all examination-level attestation engagements, the auditor should form an opinion about whether the subject matter or assertion complies with the specified requirements, in all material respects. Audit teams must document the basis for the audit opinion using the reservations framework (see CAM Chapter 10) in the summary working paper.

(1) When an examination discloses no material findings to be reported, and the auditor followed all applicable GAGAS requirements, the report opinion will be unqualified.

(2) When an examination discloses that the subject matter or assertion is not in conformity with the criteria (i.e., the auditor has reservations about the subject matter, has findings of material noncompliance, etc.), the auditor must issue either a qualified or adverse opinion, depending on the materiality of the departure from the criteria (e.g., considering the nature and significance of the audit exception(s)).

(3) If the auditor did not comply with all applicable GAGAS requirements (e.g., the auditor was not able to perform all the procedures necessary in the circumstances), either a qualified opinion or disclaimer of opinion will be issued, depending on the significance of the potential effects of the departure from the requirements.

(4) A qualified opinion provides assurance that, except for the effects of the matter to which the qualification relates, the subject matter or the assertion materially complies with the established criteria (e.g., FAR/DFARS). A qualified opinion is expressed when:

(a) There are significant reservations about the engagement, such as a lack of sufficient evidence, significant scope limitations, or other departures from GAGAS, and the auditor concludes an unqualified opinion cannot be issued. Additionally, the auditor has determined that a disclaimer of opinion is not warranted.

(b) There are significant reservations about the subject matter or assertion demonstrating that the subject matter contains significant departures from the established criteria, and the auditor has determined that an adverse opinion is not warranted.

(5) An adverse opinion states that the degree of nonconformity of the subject matter with the criteria is significant. To arrive at the decision to express an adverse opinion (rather than a qualified opinion), the auditor must consider the materiality and pervasiveness of the departures from the criteria, with consideration that lower materiality levels may be appropriate because of Government accountability and the visibility and sensitivity of Government programs. An adverse opinion should be expressed only when the auditor has performed an audit of sufficient scope to meet the audit objectives.

(6) A disclaimer of opinion is issued when scope restrictions or departures from GAGAS requirements are so significant that the limitations on the scope of the examination do not enable the auditor to form an opinion. A scope restriction may be imposed by the contractor, the requestor, or by other circumstances, such as the timing of the work or the inability to obtain sufficient evidence.

f. Content of the Audit Report. AT-C section 205 contains requirements related to the content of the examination report. CAM Chapter 10 provides general guidance regarding preparation and distribution of DCAA audit reports. Audit teams are encouraged to become familiar with the reporting requirements in AT-C 205.63 – 205.83 to ensure compliance with requirements relevant to their individual engagements and should refer to CAM Chapter 10 for detailed guidance regarding content, format, and distribution of specific types of DCAA audit reports.

2-303.3 Agreed-Upon Procedures Engagements (AT-C Section 215) **

a. Objective. The objective of the auditor in conducting an agreed-upon procedures engagement is to apply specific procedures to the subject matter and issue a written report that describes the auditor's findings without providing an opinion or conclusion on the subject matter. In an agreed-upon procedures engagement, the engaging party is required to agree to the planned procedures and acknowledge that the procedures performed are appropriate for the intended purpose of the engagement prior to beginning the engagement. The engaging party and intended users assess for themselves the procedures agreed-upon and the findings reported by the auditor and draw their own conclusions from the work performed. This section provides general guidance for conducting agreed-upon procedures engagements in compliance with the AICPA's attestation standards incorporated into GAGAS by reference.

Agreed-upon procedures engagements are conducted in accordance with AT-C section 105, AT-C section 215, and the relevant portions of AT-C section 315.

b. Communication. Before accepting an agreed-upon procedures engagement (AUP), the auditor should document the terms of the engagement agreed-to with the requestor. The requestor best understands his or her own needs and must agree to the procedures to be performed and acknowledge (preferably in writing) that the procedures are appropriate for the intended purpose. The agreed-upon terms of the engagement should be specified in sufficient detail in an engagement letter or other suitable form of written agreement. Audit teams should not agree to perform procedures that are subjective or that would require rendering an opinion or providing any level of assurance. See CAM 2-207.8e and CAM 2-207.8f for guidance related to establishing an understanding with the requestor about the nature and terms of the engagement.

c. Evidence in an Agreed-Upon Procedures Engagement. The auditor should obtain evidence from applying the procedures to provide a reasonable basis for the finding or findings expressed in the audit report. The auditor does not need to perform additional procedures outside the scope of the engagement to gather additional evidence. See CAM 2-207.8j for additional guidance related evidence in an agreed-upon procedures engagement.

d. Reporting Requirements – Agreed-Upon Procedures Reports. Because agreed-upon procedures engagements are substantially less in scope than audits and examination engagements, it is important not to deviate from the required reporting elements contained in the AT-Cs, other than to include the reference to GAGAS. CAM Chapter 10 provides general guidance regarding preparation and distribution of DCAA audit reports. Audit teams are also encouraged to become familiar with the reporting requirements in AT-C section 215 and AT-C section 315 to ensure compliance with requirements relevant to their individual engagements.

2-304 The Subject Matter (AT-C Section 315, Compliance Attestation) **

The final level of the AT-C building blocks is the AT-C 300 series, which is comprised of subject matter specific requirements. There are currently four subject matter sections in the AT-Cs covering prospecting financial information, pro forma financial information, internal controls at a service organization relevant to user entities' internal controls over financial reporting, and compliance over specified requirements.

2-304.1 Compliance Attestation AT-C Section 315 **

AT-C section 315, Compliance Attestation, is the subject matter AT-C section which is applicable to attestation engagements performed by DCAA audit teams. AT-C section 315 includes requirements and application guidance for examinations of an entity's compliance with requirements of specified laws, regulations, rules, contracts, or grant agreements. It also includes requirements and application guidance for agreed-upon procedures related to an entity's compliance with specified requirements.

2-304.2 Examination-Level Compliance Attestation Engagements **

a. The majority of attestation engagements performed by DCAA audit teams are examination-level attestation engagements performed to determine contractor compliance with contract or solicitation terms. AT-C section 315 establishes the AT-C sections that are relevant to attestation engagements performed to determine compliance with specified criteria. These engagements require application of the relevant requirements in AT-C sections 105, 205, and 315.

b. AT-C section 315 also modifies the baseline attestation requirements, moving away from determining whether the subject matter is "materially misstated" to determining whether the subject matter complies with the specified requirements, in all material respects. Reasonable assurance in an examination for compliance represents the auditor's determination about whether the audited entity complied with the specified requirements (criteria), in all material respects. This modification of the baseline attestation standards is relevant to the majority of audits performed by DCAA.

c. This AT-C section also includes a handful of additional requirements paragraphs relevant to examinations for compliance. These requirements paragraphs mostly modify requirements already included in the baseline attestation standards, setting the requirements in the context of determinations of compliance rather than determinations related to misstatements.

d. Finally, AT-C section 315 includes some unique reporting requirements. These unique reporting requirements are embedded in DCAA pro forma draft audit reports and other guidance. Audit teams are encouraged to become familiar with the requirements in AT-C 315.20 and AT-C 315.21, as well as the related application guidance to ensure they understand the required examination report elements.

2-304.3 Agreed-Upon Procedures for Compliance **

a. DCAA audit teams also perform agreed-upon procedures attestation engagements related to contractor compliance with contract or solicitation terms. These engagements require application of the relevant requirements in AT-C sections 105, 215, and 315.

b. AT-C section 315 establishes unique requirements related to preconditions for agreed-upon procedures for compliance, as well as unique reporting requirements. These unique reporting requirements are embedded in DCAA pro forma draft audit reports and other guidance. Audit teams are encouraged to become familiar with the requirements in AT-C 315.26 - 315.29, as well as the related application guidance, to ensure they understand the required agreed-upon procedures report elements.

2-400 Fieldwork Standards for Performance Audits (Operations Audits) **

2-401 Introduction **

a. This section is intended only to provide an overview of performance audits performed under GAGAS. It is not intended to provide audit teams with guidance on how to conduct a performance audit. Audit teams should become familiar with the requirements and application guidance in GAGAS chapters 8 and 9 to ensure their engagements comply with the relevant professional standards.

b. GAGAS performance audits are engagements that provide objective analysis of programs, processes, projects, policies, operations, activities, or functions. Performance audit objectives vary widely and include objectives related to assessing program effectiveness, economy and efficiency, internal control, compliance, and prospective analysis. Performance audit results are presented in the form of findings, conclusions, and recommendations and are based on an evaluation of sufficient appropriate evidence against stated criteria, such as specific requirements, measures, or defined business practices. DCAA performs certain performance audits, which we refer to as operations audits. These are generally economy and efficiency performance audits performed on an element of contractor operations.

c. DCAA performance audits seek to determine if the contractor is operating in an economical and efficient manner. Economy and efficiency relate to the reasonableness of costs charged to Government contracts, and may also impact areas such as program schedules, operations, etc. Inefficient operations can result in schedule slippages and contract overruns. Examples of subject matter covered by operations audits performed by DCAA include labor and facilities utilization, and materials inventory management. GAGAS establishes the field work and reporting standards for performance audits in Chapters 8 and 9 respectively. These standards apply to operations audits performed by DCAA. Audit teams must also follow the requirements in GAGAS Chapters 1 through 5. Fieldwork requirements establish an overall approach for planning and performing the audit to obtain sufficient, appropriate evidence that provides a reasonable basis for findings, conclusions, and recommendations based on the audit objectives.

d. Audit teams must be careful in developing appropriate audit objectives when initiating or accepting a performance audit. The audit objectives are what the audit is intended to accomplish. Audit objectives identify the audit subject matter and performance aspects to be performed in the audit. They can be thought of as questions about the subject matter that the auditor seeks to answer based on the evidence obtained and assessed against suitable criteria. Information addressing the audit objectives should be provided in an objective, understandable manner.

e. All performance audits require the use of suitable criteria. Criteria must be readily available to the auditee and the report user, and can be derived from laws, regulations, contracts, grant agreements, professional standards, specific program requirements, measures, expected performance, defined business practices, benchmarks, etc. Auditors should use suitable criteria that are relevant to the audit objectives and permit consistent assessment of the subject matter. The criteria is used as the basis for evaluating the subject matter under audit. Criteria represent the required or desired state or expectation with respect to a program. (GAGAS defines a program as: processes, projects, studies, policies, operations, activities, entities, and functions of an operation). Criteria provide the context for evaluating evidence and understanding findings, conclusions, and recommendations in the report.

2-402 Fieldwork Standards **

a. Many of the general principles relevant to examination-level attestation engagements are also relevant to GAGAS performance audits. For example, performance audit requirements associated with the principles of sufficient appropriate evidence, professional skepticism and professional judgement, engagement planning and risk assessments, suitability of criteria, evidence gathering procedures, and documentation are similar to the principles relevant to examination-level attestation engagements. This section highlights some of the fieldwork requirements unique to performance audits. However, audit teams should be familiar with the requirements in GAGAS Chapter 8 prior to starting any performance audits.

b. The assessment of audit risk involves both qualitative and quantitative considerations. Factors of audit risk can include such things as: the complexity or sensitivity of the work; size of the program; operations in terms of dollar amounts; adequacy of the audited entity’s systems; the audited entity’s processes to detect inconsistencies, significant errors or fraud, and access to records. Audit risk can be reduced by taking actions such as increasing the scope of work, adding specialists, additional reviewers and other resources to the audit team; changing the methodology to obtain additional evidence, obtaining higher quality evidence, or alternative forms of corroborating evidence; and aligning the findings and conclusions to reflect the evidence obtained.

c. Audit teams must plan the audit to reduce audit risk to an acceptably low level to provide reasonable assurance that the evidence obtained is sufficient and appropriate to support findings and conclusions. Planning is a continuous process throughout the audit. Therefore, auditors may need to adjust the audit objectives, scope, and methodology as work is being completed.

d. Adequate planning for performance audits includes gaining an understanding of the following, within the context of the audit objectives:

(1) the nature and profile of the programs and the needs of potential users of the audit report. The term program as used in GAGAS includes processes, projects, studies, policies, operations, activities, entities, and functions.

(2) internal control as it relates to the specific objectives and scope of the audit,

(3) information systems controls for purposes of assessing audit risk and planning the audit,

(4) provisions of laws, regulations, contracts, and grant agreements and potential fraud that are significant to the audit objectives,

(5) ongoing investigations or legal proceedings, and

(6) the results of previous audits and attestation engagements that directly relate to the current audit objectives.

e. The audit team will perform the following activities during the planning phase:

(1) Identify suitable criteria based on the audit objectives that will enable the auditor to evaluate the subject matter,

(2) identify sources of audit evidence and determine the amount and type of audit evidence needed, given the audit risk and significance,

(3) evaluate whether to use the work of other auditors and specialist to address some of the audit objectives,

(4) assign staff and specialists that collectively possess the professional competence necessary to perform the audit, and identify other resources needed to perform the audit,

(5) communicate about planning and performance of the audit to management officials, those charged with governance (the contractor and contracting officer), and others as applicable.

f. GAGAS 8.36 requires audit teams to obtain an understanding of the program under audit and the potential use that will be made of the audit results. Obtaining this understanding helps audit teams to assess the relevant risks associated with the program and the impact of those risks on the audit objectives to design the scope and methodology for performing the audit. The auditors' understanding may come from previous knowledge about the program, knowledge gained from inquiries, observations, and reviewing documents while planning the audit. The extent and breadth of those inquiries and observations will vary among audits based on the audit objectives, as will the need to understand the individual aspects of the program. The auditor should consider the nature and profile of a program, which include:

(1) visibility, sensitivity, and relevant risks associated with the program,

(2) age of the program or changes in its condition,

(3) size of the program in terms of total dollars or other measures,

(4) level and extent of review or other forms of independent oversight,

(5) the program's strategic plan and objectives, and

(6) external factors or conditions that could directly affect the program.

g. The concept of significance assists auditors throughout an operations audit, including deciding the type and extent of audit procedures to perform, evaluating results of audit work, and developing the report and related findings and conclusions. Significance is defined as the relative importance of a matter within the context in which it is being considered, and includes both quantitative and qualitative factors, such as: the magnitude of the matter in relation to the subject matter of the audit; the nature and effect of the matter; the relevance of the matter; the needs and interests of an objective third party with knowledge of the relevant information; and the impact of the matter to the audited program or activity. The concept of significance in a performance audit is comparable to the concept of materiality in an examination-level attestation engagement.

h. Consideration of internal control in a performance audit begins with determining the significance of internal control to the audit objectives and documenting that determination. See GAGAS 8.41 for factors that may be considered when determining the significance of internal control to the audit objectives. Additionally, GAGAS 8.41 through 8.67 Internal Control provides application guidance related to obtaining an understanding, assessing significance, and reporting deficiencies in internal control as well as considerations related to information systems.

i. Assessment of internal control involves designing and performing procedures to obtain sufficient, appropriate evidence to support and document the findings and conclusions on design, implementation, and/or operating effectives of controls that are significant to the audit objectives. Key controls are generally assessed during the planning phase, which may include controls at both the entity and transaction levels. Changes may be made to the initial determination of key controls based on information gathered during fieldwork. Assessment of the design and implementation of internal control is crucial to determine if the internal control is operating effectively to meet the control objective:

- Design. The design of internal control is assessed by determining whether controls individually and in combination are capable of achieving the objective for the control and addressing the related risk.
- Implementation. The implementation of internal control is assessed by determining if the control exists and has been placed into operation. A control that is not effectively designed cannot be effectively implemented.
- Operating Effectiveness. The operating effectiveness of internal control is assessed by determining whether controls were applied at relevant times during the period under evaluation, the consistency with which they were applied, and by whom or by what means they were applied. If a control is not effectively designed and implemented, it cannot operate effectively.

j. Deficiencies in internal control may be identified during assessment of a control. A deficiency exists when the design, implementation, or operation of a control does not achieve the desired control objectives to address related risks.

- A design deficiency exists when a necessary control is either missing or not properly designed. An improperly designed control would result in the control objective not being met even if the control operates as designed.
- An implementation deficiency exists when a properly designed control is not correctly implemented.

- A deficiency in operating effectiveness exists when a properly designed and implemented control does not operate as designed, or the person performing the control does not have the necessary competence or authority to perform the control effectively.

k. The effectiveness of significant internal controls frequently depends on the effectiveness of information systems controls. When an auditor obtains an understanding of significant internal controls, the auditor should also determine if it is necessary to evaluate the information systems controls. Understanding information systems controls (e.g., general controls, application controls, user controls) is important when information systems are used extensively throughout the program under audit and the fundamental business processes related to the audit objectives rely on information systems.

l. The evaluation of information systems controls may be done in conjunction with the auditors' consideration of internal control within the context of the audit objectives, or as separate audit objectives or procedures. The extent of the audit procedures to obtain such an understanding depends on the significance of the information system controls to the audit objectives. In addition, the nature and extent of audit risk related to information systems controls area affected by the nature of the hardware and software used the configuration of the entity's systems and networks, and the entity's information systems strategy.

m. Auditors should determine which audit procedures related to information systems controls are needed to obtain sufficient, appropriate evidence to support the audit findings and conclusions. The following factors may assist auditors in making this determination.

(1) Understanding the significance of the impact of the system relative to the accessibility and reliability of the information produced, and

(2) Identifying key controls that are critical to providing assurance that the information required for the audit is reliable and evaluating those key controls, e.g. general, application, and user controls.

n. Audit teams should identify any provisions of laws, regulations, contracts, or grant agreements that are significant to the audit objectives and assess the risk that noncompliance could occur. Based on that risk assessment, the auditor should design and perform procedures to obtain reasonable assurance of detecting instances of significant noncompliance with provisions of laws, regulations, contracts, or grant agreements.

o. The assessment of audit risk may be affected by such factors as the complexity of the laws and regulations and provisions of contracts. The assessment of audit risk may also be affected by whether the entity has controls that are effective in preventing or detecting violations of laws, regulations, and provisions of contracts. If auditors obtain sufficient, appropriate evidence of the effectiveness of these controls, they may be able to reduce the extent of their tests of compliance.

p. In planning the audit, audit teams should assess risks of fraud occurring that are significant to the audit objectives. Fraud involves obtaining something of value through willful misrepresentation. There is no requirement for auditors to prove the existence of fraud. Whether an act is in fact fraud is a determination to be made through the judicial or other adjudicative system and is beyond auditors' professional responsibility.

q. The audit team should discuss the contractor's risk of fraud, including factors such as financial incentives, pressures to commit fraud, opportunities for fraud to occur, and rationalizations or attitudes that could allow individuals to commit fraud. Auditors should gather and assess information to identify risks of fraud that are significant to the audit objectives or that could affect the findings and conclusions.

r. Assessing the risk of fraud is an ongoing process throughout the audit. Professional skepticism assists auditors in assessing which factors or risks could significantly affect the audit objectives. If indications of fraud risk, significant to the audit objectives, arise during the course of the audit that were not identified in the planning stage, the auditor should modify the audit program as necessary and perform procedures designed to detect instances of fraud that are material to the subject matter. For example, auditors may obtain information through discussion with officials of the audited entity or through other means to determine the susceptibility of the program to fraud, the extent to which the audited entity has implemented leading practices to manage fraud risks, the status of internal controls the entity has established to detect and prevent fraud, or the risk that individuals in the audited entity could override internal controls.

s. Auditors must obtain sufficient, appropriate audit evidence to provide a reasonable basis for their findings and conclusions. In assessing the appropriateness of evidence, auditors should assess whether the evidence is relevant, valid, and reliable. For example, when the audit objective is to report on the current status or condition of a process, appropriate evidence would provide reasonable assurance that the description of the current status or condition is accurate and reliable and does not omit significant information relevant to the audit objectives.

t. Appropriateness is the measure of the quality of the evidence that encompasses its relevance, validity and reliability in supporting audit objectives and related findings. In assessing the overall appropriateness of evidence, auditors should assess whether the evidence is relevant, valid, and reliable. For oral testimony, the auditor evaluates the objectivity, credibility and reliability of the testimonial evidence. Strength of the oral testimony is generally higher when obtained under circumstances where the person is speaking freely than under conditions where the person may have felt intimidated.

(1) Relevance refers to the extent to which the evidence has a logical relationship and importance to the issue being addressed.

(2) Validity refers to the extent to which evidence is based on sound reasoning or accurate information.

(3) Reliability refers to the consistency of results when information is measured or tested and includes the concepts of being verifiable or supported.

u. Sufficiency is a measure of the quantity of evidence used to support the findings and conclusions related to the audit objectives. In assessing the sufficiency of evidence, auditors should determine whether enough appropriate evidence exists to address the audit objectives and support the findings and conclusions to the extent that would persuade a knowledgeable person that the findings are reasonable. The following presumptions are useful in judging the sufficiency of evidence. The sufficiency of evidence required to support the auditors' findings and conclusions is a matter of the auditor's professional judgement.

(1) Higher audit risk requires a greater quantity and quality of evidence.

(2) Stronger evidence may allow less evidence to be used.

(3) Having a large volume of audit evidence does not compensate for a lack of appropriate evidence, i.e., evidence that is relevant, valid, and reliable to meet the audit objective.

v. Overall Assessment of Evidence. Auditors should perform and document an overall assessment of the collective evidence used to support findings and conclusions, including the results of any specific assessments performed to conclude on the validity and reliability of specific evidence. When assessing the overall sufficiency and appropriateness of evidence, auditors should evaluate the expected significance of the evidence to the audit objectives; available corroborating evidence; and the level of audit risk. Auditors should not use insufficient or inappropriate evidence as support for findings and conclusions.

w. Evidence is sufficient and appropriate when it provides a reasonable basis to support the findings or conclusions within the context of the audit objectives. Evidence is not sufficient or not appropriate when:

(1) using the evidence carries an unacceptability high risk that it could lead the auditor to reach an incorrect or improper conclusion,

(2) the evidence has significant limitations, given the audit objectives and intended use of the evidence, or

(3) the evidence does not provide an adequate basis for addressing the audit objectives or supporting the findings and conclusions.

Auditors should not use insufficient or inappropriate evidence as support for findings and conclusions.

x. Evidence has limitations or uncertainties when the validity or reliability of the evidence has not been assessed in context of the audit objectives or for its intended use. Limitations also include errors identified by the auditors during testing. When auditors identify limitations or uncertainties in evidence that is significant to the audit findings and conclusions, additional procedures should be performed as appropriate. Such procedures include:

(1) seeking independent corroborating evidence from other sources,

(2) redefining the audit objectives or limiting the audit scope to eliminate the need to use the evidence,

(3) presenting findings and conclusions that are based on supporting evidence that is sufficient and appropriate, and describing in the report the limitations or uncertainties with the validity or reliability of the evidence, if such disclosure is necessary to avoid misleading the report users about the findings or conclusions, and

(4) determining whether to report the limitations or uncertainties themselves as a finding, including any related significant internal control deficiencies.

y. Audit teams should plan and perform procedures to develop the elements of a finding necessary to address the audit objectives. In addition, the auditors may develop recommendations for corrective action if they are significant to the audit objectives. The elements needed for a finding are related to the objectives of the audit. Thus, a finding or set of findings is complete to the extent that the audit objectives are addressed and the report clearly relates those objectives to the elements of the finding. The structured note Statement of Condition(s) and

Recommendation(s) (SOCAR) format is used for performance audits.

2-403 Reporting Standards **

a. GAGAS Chapter 9 establishes reporting standards and provides guidance for performance audits. A distinguishing difference between performance audit reports and examination-level attestation reports is that performance audit reports do not express an opinion. Audit teams should become familiar with the requirements in GAGAS Chapter 9 to ensure compliance with requirements relevant to their individual engagements and should refer to the CAM Chapter 10.

b. Auditors should prepare performance audit reports that describe:

- the objectives, scope, and methodology of the audit;
- the audit results with findings, conclusions, and recommendations, as appropriate;
- a statement about the auditors' compliance with GAGAS;
- a summary of the views of responsible officials of the audited entity, and
- if applicable, the nature of any confidential or sensitive information that was omitted from the report.

c. The report should communicate the audit objectives in a clear, specific, neutral and unbiased manner that includes relevant assumptions including the purpose of the audit and report.

d. In reporting the audit scope, auditors should describe the scope of the work performed and any limitations, including issues that are relevant to likely users, so they can reasonably interpret the findings, conclusions, and recommendations in the report without being misled. Auditors should also report any significant constraints imposed on the audit approach by information limitations or scope impairments, including denials or excessive delays of access to records or individuals.

e. In reporting audit methodology, auditors should explain how the completed audit work supports the audit objectives, including the evidence-gathering and analysis techniques, in sufficient detail to allow knowledgeable users of the report to understand how the auditor addressed the audit objectives. Auditors may include a description of the procedures performed as part of their assessment of the sufficiency and appropriateness of the information used as audit evidence. Auditors should identify significant assumptions made in conducting the audit, describe comparative techniques applied, describe the criteria used, and when sampling significantly supports the auditors' findings, conclusions, or recommendations, describe the sample design and state why the design was chosen, including whether the results can be projected to the intended population.

f. The audit report should include a statement of compliance with GAGAS.

(1) When the auditor complies with all applicable GAGAS requirements, an unmodified statement of GAGAS compliance will be included in the audit report. The proforma audit report in the standard audit program provides the language required by GAGAS for the unmodified statement.

(2) When auditors do not comply with all applicable GAGAS requirements, a modified statement of GAGAS compliance will be included in the audit report. For performance audits,

the auditor will modify the statement of GAGAS compliance in the proforma audit report to indicate the requirements that were not followed, or other language indicating the auditors did not follow GAGAS, e.g., because of significant departures from the requirements, the auditor was unable to perform the audit in accordance with GAGAS.

(3) When auditors use modified compliance statements, a scope limitation is also frequently present, such as restrictions on access to records, or access to government officials or other individuals needed to perform the audit. When auditors use a modified statement of GAGAS compliance, the report should disclose the applicable requirement(s) not followed and the impact on the audit objectives and/or scope of the audit resulting from departure from the requirements, and the level of assurance provided.

g. GAGAS 9.17 presents report quality elements to assist the auditor in developing and writing the performance audit report. Report quality elements include being accurate, objective, complete, convincing, clear, concise and timely, as the subject matter permits.

(1) An accurate report is supported by sufficient, appropriate evidence with key facts, figures, and findings that are traceable to the audit evidence.

(2) An objective report presents language in a balanced in content and tone.

(3) A complete report contains sufficient, appropriate evidence to satisfy the audit objectives and promote an understanding of the matters reported. It also does not omit significant relevant information related to the audit objectives.

(4) A convincing report is responsive to the audit objectives, presents findings persuasively, and the conclusions and recommendations flow logically from the facts presented.

(5) A clear report is easy for the user to read and understand.

(6) A concise report is no longer than necessary to convey and support the message.

(7) The auditor’s goal is to provide relevant information within the timeframe to meet the needs of the intended user. Throughout the audit, the auditors should communicate significant matters to appropriate entity and oversight officials. Such communication alerts officials to matters needing immediate attention and allows them to take corrective action before the final report is completed. When corrective action is taken before the report is issued, the auditor will, nonetheless, include the finding in the audit report and may comment on corrective actions taken by the contractor.

h. Audit teams should place findings in perspective by describing the nature and extent of the issues and the extent of the work performed. The report should give the reader a clear basis for judging the prevalence and consequences of the findings. It should describe limitations or uncertainties about the reliability or validity of the evidence to avoid misleading the reader about the findings and to provide relevant background information to establish the context of the findings. Clearly developed findings assist the responsible Federal agency, as well as the contractor’s management, in understanding the need for corrective action.

i. When developing the elements of a finding, the auditors may provide recommendations for corrective action if they are significant to the audit objectives. The extent to which the elements of a finding are developed depends on the audit objectives. The auditor should consider internal control deficiencies in their evaluation of identified findings when developing the cause element of the finding when internal control is significant to the audit objectives. Thus, a finding or set of findings is complete to the extent that the auditors address the audit objectives.

j. The audit report should describe limitations or uncertainties regarding the sufficiency or appropriateness of evidence in conjunction with the findings and conclusions in addition to describing them as part of the objectives, scope and methodology. Describing the limitations and uncertainties provides report users with a clear understanding regarding how much responsibility the audit team is taking for the information. The report should describe limitations or uncertainties with the reliability or validity of the evidence if:

(1) the evidence is significant to the findings and conclusions within the context of the audit objectives; and

(2) such disclosure is necessary to avoid misleading report users about the findings and conclusions.

k. Auditors should obtain and report the views of responsible officials of the audited entity concerning the findings, conclusions, and recommendations included in the audit report, as well as any planned corrective actions.