NSAA

National State Auditors Association

Office of the State Auditor
State of Washington
External Peer Review
For the Period October 1, 2006
through September 30, 2007

449 Lewis Hargett Circle ▪ Suite 290 ▪ Lexington, KY 40503 ▪ (859) 276-1147 ▪ www.nasact.org

National State Auditors Association

November 13, 2007

The Honorable Brian Sonntag, State Auditor
Washington State Auditor's Office
3200 Capitol Boulevard
Olympia, Washington 98504

Dear Mr. Sonntag:

We have reviewed the system of quality control of the Washington State Auditor's Office (the office) in effect for the period October 1, 2006 through September 30, 2007. A system of quality control encompasses the office's organizational structure and the policies adopted and procedures established to provide it with reasonable assurance of conforming with government auditing standards. The design of the system and compliance with it are the responsibility of the office. Our responsibility is to express an opinion on the design of the system, and the office's compliance with the system based on our review.

We conducted our review in accordance with the policies and procedures for external peer reviews established by the National State Auditors Association (NSAA). In performing our review, we obtained an understanding of the office's system of quality control for engagements conducted in accordance with government auditing standards. In addition, we tested compliance with the office's quality control policies and procedures to the extent we considered appropriate. These tests covered the application of the office's policies and procedures on selected engagements. The engagements selected represented a reasonable cross-section of the office's engagements conducted in accordance with government auditing standards. We believe that the procedures we performed provide a reasonable basis for our opinion.

Our review was based on selective tests; therefore it would not necessarily disclose all weaknesses in the system of quality control or all instances of lack of compliance with it. Also, there are inherent limitations in the effectiveness of any system of quality control; therefore noncompliance with the system of quality control may occur and not be detected. Projection of any evaluation of a system of quality control to future periods is subject to the risk that the system of quality control may become inadequate because of changes in conditions, or because the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the system of quality control of Washington State Auditor's Office in effect for the period October 1, 2006 through September 30, 2007 has been suitably designed and was complied with during the period to provide reasonable assurance of conforming with government auditing standards.

Randal L. Sanders, Team Leader
National State Auditors Association
External Peer Review Team

Vickie Rauser, Concurring Reviewer
National State Auditors Association
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National State Auditors Association

LETTER OF COMMENTS

NSAA Letterhead
November 13, 2007

The Honorable Brian Sonntag, State Auditor
Washington State Auditor
3200 Capitol Boulevard
Olympia, Washington 98504

Dear Mr. Sonntag:

We have reviewed the system of quality control of the Washington State Auditor's Office (the office) in effect for the period October 1, 2006 through September 30, 2007 and have issued our report thereon dated November 13, 2007. That report should be read in conjunction with the comments in this letter, which were considered in determining our opinion. The matters described below were not considered to be of sufficient significance to affect the opinion expressed in that report.

Planning and Supervision

Finding: The American Institute of Certified Public Accountants (AICPA) first standard of fieldwork, states "the work is to be adequately planned and assistants, if any, are to be properly supervised." In addition, documentation standards (AU 339) require the auditor to prepare audit documentation in sufficient detail to provide a clear understanding of the work performed. Washington State Auditor's Office (WSAO) Audit Policy Manual Section 6210 – Planning Financial Statement Audits, includes policies for planning audits, including a requirement that auditors will communicate certain matters to the auditee or audit committee. WSAO Audit Policy Manual Section 2220 – Conducting Exit Conferences, requires exit conferences to be held for all engagements prior to report issuance and summarized in the audit documentation.

- For several engagements reviewed, we noted where WSAO audit staff signed off on a quality control assurance certification indicating the exit conference had been held, when documentation indicates the exit conference was actually held at a later date or had not been held as of the date of our review. In some instances, the audit report was issued prior to holding the formal exit conference; however, the results of the audits were communicated to the auditees before the audits were issued.

- For several engagements reviewed, the auditor's opinion on the comprehensive annual financial report (CAFR) financial statements was dated and issued in June 2007. However, the auditor's opinion on the schedule of expenditures of federal awards (SEFA) and the opinion on the related basic financial statements was not issued in a timely manner. Audit documentation did not show that additional procedures were performed to comply with SAS 1, "Subsequent Events", as required by AU 339.23.

- Generally accepted government auditing standards (GAGAS) require the auditor to communicate deficiencies in a management letter unless the deficiencies are clearly inconsequential. For two engagements, the auditor did not issue a management letter nor were the dispositions of audit exceptions documented. For one engagement, audit documentation indicated that testing required a qualified opinion on a compliance requirement. However, an unqualified opinion was issued. Without further information available in the audit documentation, we were unable to determine that the proper audit opinion was issued. In addition, audit documentation indicated that a compliance requirement was not material to a federal program while information in the Catalog of Federal Domestic Assistance (CFDA) appears to indicate this compliance requirement was material. GAGAS requires evidence that support the auditors' significant judgments and conclusions.

Recommendation: We recommend that the Washington State Auditor's Office implement controls to ensure compliance with adopted quality control policies and procedures at the engagement level prior to release of the opinion on the financial statements. In addition, training should be focused on activities to ensure compliance at the Supervisor and Manager levels.

Evidential Matter

Finding: GAGAS and the AICPA require that auditors should obtain a sufficient understanding of internal control to plan the audit and determine the nature, timing, and extent of tests to be performed (AU 319.01). The auditor should also obtain an understanding of the entity's use of information technology and its effect on controls relevant to the audit (AU 319.02). GAGAS and AICPA standards also require auditors to prepare and maintain audit documentation. GAGAS requires that audit documentation contain sufficient information to enable an experienced auditor having no previous connection with the audit to ascertain from the audit documentation the evidence that supports the auditors' significant judgments and conclusions (AU 326.01).

The State Auditor's quality control policies and procedures require auditors, when assessing control risk below the maximum, to identify and test the relevant internal controls to provide sufficient evidence that those controls are effective. However, for some of the Single Audit engagements reviewed, the audit documentation did not adequately identify the controls relied upon to reduce testing. Additionally for the State CAFR, the auditor determined that three information technology systems were significant to a material account balance on the CAFR. Documentation evaluating the results of testing these systems was insufficient, and one of the three systems has not been reviewed since 1999. Another material system had a "significant weakness" identified in the 2005 accountability audit, and referenced in the CAFR workpapers, but there was no evidence of additional tests of controls performed over this material system which would support a conclusion of low internal control risk.

While the State Auditor's quality control policies and procedures address sampling requirements, audit documentation at the engagement level does not demonstrate compliance with required procedures. Professional standards require the audit documentation to contain the sampling criteria used. For several engagements we reviewed the audit documentation did not include evidence of sampling criteria used. Tolerable error or the expected results of sampling when the term sample was used for testing of controls was not provided, or the testing performed clearly indicated a sampling procedure was used. The audit documentation also did not include evidence that results of samples were evaluated and compared to tolerable error or the expected results. We were satisfied, for the audits reviewed, that the audit team had an understanding of internal control and related impact on testing.

Recommendation: We recommend that the State Auditor conduct additional training on the importance of testing internal controls. The State Auditor should also ensure the auditors document the evaluation of the effectiveness of controls relied upon to reduce the level of risk. The audit documentation should also include the evaluation of information technology and its effect on controls relevant to the audit. We also recommend that the State Auditor document the sampling criteria and expected results used to support significant audit judgments and conclusions.

In the attached correspondence dated November 13, 2007, the Washington State Auditor's Office provided its response to the letter of comments recommendations.

Respectfully submitted,

Randal L. Sanders, Team Leader
National State Auditors Association
External Peer Review Team

Vickie Rauser, Concurring Reviewer
National State Auditors Association
External Peer Review Team

Washington State Auditor
Brian Sonntag

November 13, 2007

Randal L. Sanders, Team Leader
Vickie Rauser, Concurring Reviewer

Dear Mr. Sanders and Ms. Rauser:

This letter represents our response to the letter of comments issued in connection with Washington State Auditor's Office's system of quality control for the period October 1, 2006 through September 30, 2007. The matters described in the letter of comments were not considered by the review team to be of sufficient significance to affect the opinion expressed in the peer review report.

> Recommendation: We recommend that the Washington State Auditor's Office implement controls to ensure compliance with adopted quality control policies and procedures at the engagement level prior to release of the opinion on the financial statements. In addition, training should be focused on activities to ensure compliance at the Supervisor and Manager levels.
>
> Response: We will continue to emphasize and monitor the important roles that supervisors and managers play in ensuring full compliance with SAO policies and procedures.
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> Recommendation: We recommend that the State Auditor conduct additional training on the importance of testing internal controls. The State Auditor should also ensure the auditors document the evaluation of the effectiveness of controls relied upon to reduce the level of risk. The audit documentation should also include the evaluation of information technology and its effect on controls relevant to the audit. We also recommend that the State Auditor document the sampling criteria and expected results used to support significant audit judgments and conclusions.
>
> Response: Internal control training (including information technology) will continue to be emphasized for all audit staff along with timely supervisory involvement to ensure proper assessment and documentation of controls. New sampling guidance and a required training class are in the process of being finalized.
>
> Finally, we plan to follow up with standard setting bodies to seek clarification on some technical issues.

Sincerely,

Brian Sonntag, CGFM
Washington State Auditor

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