

GUIDE FOR PROCUREMENT OF AUDIT SERVICES

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A. INTRODUCTION

No matter the size of your organization, an effective audit can improve management operations and yield significant dollar savings. It can also help avoid wasting your organization's scarce resources on a substandard audit. This guide can help get the most for your money. An audit:

Verifies financial transactions and determines whether funds were expended according to applicable laws, regulations and procedures.

Provides DECD management with timelier reporting by recipients and IPAs of noncompliance with Laws and Regulations.

Provides the DECD and grantee management with objective appraisals of financial accounting systems and administrative controls; and

Determines reliability of financial records and reports.

A U.S. General Accounting Office (GAO) report showed that entities with ineffective audit procurement systems stood a 46 percent chance of receiving a substandard audit; that figure dropped to 17 percent for entities that followed systematic audit procurement practices.

This guide is based on guidance developed by the GAO, the National Intergovernmental Audit Forum, the Western Intergovernmental Audit Forum, the Single Audit Information Service and the LSC Audit Guide.

B. PLANNING: AN ESSENTIAL FIRST STEP

Planning to obtain a quality audit requires time and attention. However, the resources spent on planning are likely to be rewarded by a smooth, timely and less expensive audit.

Determining the specific audit requirements. To find out your audit requirements – a sometimes difficult task – your organization may want to seek the assistance of knowledgeable persons. An audit committee composed of people with backgrounds in accounting, auditing, finance or management ideally provides this assistance. Grantees without audit committees may want to seek the assistance of DECD or other DECD recipients.

Identifying the attributes necessary in an auditor. We suggest that the personnel doing the audit have experience with audits of other DECD funded recipients or similar entities. Moreover, they must comply with applicable Government Auditing Standards requirements for peer review and continuing professional education.

Deciding how to evaluate prospective audit firms. Developing a systematic procedure for evaluating firms' qualifications is essential. Although price is important, technical qualifications should be a critical measure in selecting an auditor.

Reviewing legal requirements. Review applicable laws, regulations and grant conditions to ensure that the procurement process and the audit meet legal requirements.

Considering a multiyear agreement. The first year of an audit engagement usually involves significant start-up costs for an auditor because of the time needed to learn about an organization and its internal control structure. After completing this groundwork, the auditor usually can work at less cost in the succeeding years. A multiyear agreement has a dual advantage: it enables an auditor to propose a price that considers the savings to be realized in subsequent years and saves your organization the costs associated with repeating the selection process. However, contracts or engagement letters should also contain an escape clause that would allow, without significant penalty, modification or cancellation made necessary by changes in the law.

Evaluating the auditor rotation option. Some people argue that changing auditors at the end of a multiyear contract infuses the audit process with fresh views and new perspectives. Others contend that these benefits can be achieved through internal rotation of audit staff and that maintaining a long-term, ongoing relationship with a particular auditor is more advantageous. A long-term relationship with a firm, however, will not necessarily enable your organization to seek out and take advantage of lower priced audits. Carefully consider the advantages and disadvantages of auditor rotation before setting a policy.

Establish a work schedule. Develop a schedule that sets dates for achieving certain milestones in the audit process. The only way to ensure the timely preparation and issuance of financial statements and related reports is to develop and follow such a schedule.

All these suggestions – especially creating and using an audit committee – can help a small entity achieve a quality audit. Even the smallest organization can appoint a two or three-person audit committee that understands what is to be audited and how the audit should be done.

C. COMPETITION AND SOLICITATION: COMMUNICATING AUDIT REQUIREMENTS

Full and open competition is basic to funds oversight and responsibility. Encouraging as many qualified audit firms as possible to submit audit proposals increases the likelihood of receiving a quality audit at a fair price. The next step, then, is to express your audit needs to potential bidders. This step is critical because bidders who do not clearly understand exactly what services are wanted might not respond.

Solicitation. There are many ways to solicit bids for audits, but the most reliable method – and the one we suggest – is a written request for proposal, or RFP. RFP's should be clearly written; setting forth all terms, conditions and evaluation criteria and the scope of the work required.

All potential bidders must understand the requirements of the audit and environment of your organization. Using your audit committee's advice when writing an RFP is a good idea. Committee members should have a clear understanding of both the audit function and what your organization requires of the audit.

The RFP must be sufficiently distributed and publicized to ensure open competition. Consider compiling a list of potential auditors from general and professional directories and from experiences with audit firms. The Connecticut Society of CPAs, State Board of Accountancy and other DECD funded recipients are excellent sources of potential auditors.

Connecticut Society of CPAs
845 Brook Street, Bldg. 2
Rocky Hill, CT 06067-3405
(860) 258-4800

State Board of Accountancy
30 Trinity Street
Hartford, CT 06106
(860) 509-6179

It is important to design technical and cost proposal instructions that enable consistent evaluation of proposals using applied evaluation criteria. The provisions listed below should be included in an RFP. These provisions can be adapted depending on the size of your entity.

Administrative Information

Background information on your organization
Schedule of funds received and expended by project or grant and Grantor agency
Description and magnitude of your accounting records
Description of your computer system (if applicable)
Fiscal period to be audited
Term of contract engagement
Availability of prior audit reports and working papers

Time Requirements

Date records would be ready for audit
Deadlines for completing interim phases, such as fieldwork and draft report preparation
Contract award date
Final report due date
Working paper retention requirements
Requirements for making work papers available to DECD and other grantors

Work and Reporting Requirements

Auditing standards to be followed
Extent of assistance your organizations will provide the auditor
Specific scope of audit work to be done
Number and types of reports required
Exit conference requirements
Specific audit guide or program to be followed
Additional audit requirements under DECD Compliance Supplement
Minimum audit requirements under applicable laws, such as the Federal and State Single Audit Acts

Proposal Information

Evaluation criteria against which the proposal will be judged
Your right to reject the proposal

Contractual Information

Recourse in case of poor quality work
Equal employment opportunity clause
Termination of contract provisions
Administrative and/or legal remedies for contract violations

Bidders' Conference. Although your organization will have been as thorough as possible in preparing your RFP, some information that prospective bidders will find useful may be overlooked. One effective way of communicating additional information to bidders is a bidders' conference. At a bidders' conference, additional information is provided and prospective bidders can ask any unanswered questions. Letters and individual conversations could serve the same purposes; however, bringing all bidders together simultaneously to hear the same information is efficient and helps ensure all bidders are treated equally.

Small Entities

Obtaining an extensive list of potential bidders may be difficult for small entities in rural areas. Soliciting lists from the state society of CPAs, other larger DECD funded recipients and from CPAs in your region that have experience with similar entities is often helpful. Furthermore, preparing a detailed RFP for a small engagement may be economically impractical. Abbreviated RFP's, designed for small engagements, can be designed through tailoring to meet individual needs. At a minimum, such RFP's should clearly define the work including the reports and opinions required.

D. TECHNICAL EVALUATION

Methods for evaluating the technical merit of each audit firms' proposal should be developed. These should include the evaluation criteria and their importance in choosing the audit firm best able to do the audit. The following are some critical factors for evaluating audit proposals:

Responsiveness of the proposal as demonstrated by the necessity and adequacy of proposed procedures, reasonableness of time estimates and timeliness of expected completion and appropriateness of assigned staff levels;

Qualifications of staff who will be assigned to the engagement;

Size and location of the firm;

The range of activities performed by the firm;

The firm's participation in training and continuing professional education in auditing organizations and programs receiving state and federal funds;

A description of the firm's quality control procedures;

Results of internal and external quality control reviews of the firm;

Time frames for the fieldwork;

The firm's data processing capabilities;

The amount of assistance the firm expects from your organization;

Whether the firm is licensed to practice in the state; and

Assurance that the firm's staff meets the independence standards outlined in *Government Auditing Standards*.

E. WRITTEN AGREEMENT: DOCUMENTING EXPECTATIONS

The lack of a written agreement between your organization and the audit firm can contribute to substandard audits by public accountants. To foster sound and productive communication and to avoid misunderstandings, both parties should agree in writing on important audit-related matters. Make clear at the start – before bidders spend time assessing the nature of the job and estimating its costs – that your organization expects to sign a formal document as the culmination of the proposal process. Audit firms unwilling to commit to signing such a document are better avoided. Appendix C of this Audit Guide provides a Sample Audit Agreement.

What to Include in a Written Agreement

When using an RFP, the written agreement should incorporate by reference the terms of the RFP and those of the successful bidder's last proposal. The written agreement will then clearly specify the:

Audit Scope, objective and purpose;

Deadlines for work to be done;

Audit Cost;

Report format;

Type and timing of support by your organization to the auditor;

Professional auditing standards to be followed in performing the audit; and

Reference to the DECD Audit Guide

Furthermore, the agreement should make the following points about the auditor/entity relationship, changes in the kind or amount of work required, and access to and ownership of audit products.

The relationship of the auditing firm to your organization is that of independent contractor.

At any time, your organization may, by written notice, make changes in or additions to work or services within the general scope of the agreement. If such changes are made, an equitable adjustment will be made in the cost of the audit using the rates specified in the agreement.

If the contractor believes that a change in or addition to work is beyond the general scope of the agreement, it must notify your organization in writing within a specified time and before beginning that work. The agreement should state where the final administrative authority rests in deciding disputes.

The work papers prepared by the contracting auditor during the audit are its own property. These documents should be retained for the period designated in the DECD Audit Guide and available to authorized representatives of your organization and DECD upon request. All reports by the contracting auditor to your organization are the exclusive property of your organization and subject to its use and controls, according to applicable laws and regulations.

Small Entities

Without an RFP, many small engagements are documented with an engagement letter. The engagement letter is typically prepared by the CPA and protects the CPA more than the entity

being audited. If your organization decides to use an engagement letter as the written agreement, the letter must reference that the audit was performed in accordance with the DECD Audit Guide. Contracts or engagement letters should also contain an escape clause that would allow, without significant penalty, modification or cancellation made necessary by changes in the law.

F. ENGAGEMENT CONTRACT MANAGEMENT: ENSURING A QUALITY AUDIT

Because of the needs and expectations of third-party financial statement users, the audit must meet the requirements of the DECD Audit Guide, State Single Audit Act, and the Federal Single Audit Act (OMB Circular A-133), as applicable. Therefore, prudent management of the audit engagement is crucial. Monitoring the progress of the audit is the most effective way to ensure that your organization receives the type and quality of audit services specified in the written agreement. This is a role that your audit committee can carry out most effectively. The committee can evaluate the audit while it is taking place, addressing and resolving problems before the audit is completed. It can also review audit results and assist in post-audit quality evaluation. Thus, not only does the audit product improve but also the working relationship with the auditor is enhanced.

Monitoring is especially beneficial during the first year of a new auditor's contract and during the audit of a particular unit or segment(s) of your organization that is unique or complex. Furthermore, monitoring is beneficial throughout the term of a multiyear contract: It provides status reports and helps coordinate the auditing firm's activities with the audit's requirements. Monitoring can be accomplished through conferences between the auditor and key auditee staff once the contract is awarded, at the completion of audit fieldwork, and at the conclusion of audit fieldwork. Meeting after the completion of the audit to discuss the draft report can help ensure a clear understanding of the report and its findings. While the responsibility for a quality audit rests ultimately with the auditor, monitoring the work being done as a quality assurance measure is a good idea.

Small Entities

Few small organizations have the resources to thoroughly monitor the work of an auditor. When audit committee members are unavailable within an organization, composing a committee of volunteers outside the organization may be the answer.

G. USE OF SMALL AND MINORITY FIRMS

DECD Contracts and OMB Circular A-133 contain policies and standards concerning procurement of audit services from small and minority firms.

The standards are based on several fundamental principles when using public funds to obtain goods and services, including:

1. All offers of services should be accorded equal treatment. There should be no favoritism granted to any firm and the relationship, to the maximum extent possible, should be "arms-length."
2. To the maximum extent possible, recipients of public funds should use free and open competition to provide the necessary services.

3. The relationship between the parties (auditee and auditor) provides rights and remedies. If either party fails to uphold its responsibilities or is forced to do more than is expected under the contract document, legal remedies are available.

H. DECD ASSISTANCE

Use of the procedures recommended in this document should result in a more effective and useful audit. Please direct questions about audit services procurement to the Compliance, Audit and Financial Review Section at (860) 270-8210, (860) 270-8209 or (860) 270-8202.