

ASSOCIATION OF PACIFIC ISLANDS
PUBLIC AUDITORS

July 27, 2018

Stoney S. Taulung
Public Auditor
Kosrae State Government
FSM, 96944

Dear Mr. Taulung,

We have completed the peer review of the Kosrae State Office of Public Auditor (KOPA) for calendar year 2015 to 2017. In conducting the review, we followed the standards and guidelines contained in the *Peer Review Guide* by the Association of Pacific Islands Public Auditors (APIPA).

We reviewed the internal quality control system of your audit organization and conducted tests in order to determine whether your internal quality control system operated to provide reasonable assurance of compliance with *Government Auditing Standards (GAS)* issued by the Comptroller General of the United States. Our procedures included:

- Reviewing the audit organization's written audit manual, policies and procedures.
- Reviewing internal monitoring procedures.
- Reviewing a sample of audit engagements and working papers.
- Reviewing documents related to independence, training, and development of auditing staff.
- Interviewing auditing staff, management, to assess their understanding of, and compliance with, relevant quality control policies and procedures.

Due to variances in individual performance and judgment, compliance does not imply adherence to standards in every case, but does imply adherence in most situations.

We selected a sample and tested the engagement documentations using a checklist of standard requirements from the latest 2011 GAGAS Revision.

Based on the results of our review, it is our opinion that, except for the deficiencies noted below, the KOPA internal quality control system was suitably designed and operating effectively to provide reasonable assurance of compliance with *Government Auditing Standards* for audits and attestation engagements during the 2015-2017 calendar periods.

We found that the internal quality control system in use was based on 2007 and not on 2011 GAS Revision. As such it may not include some quality standards required by the latest GAS.

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For example, KOPA did not completely documented using the GAGAS Conceptual approach for assessing independence.

We offer the following observations and suggestions to help your organization achieve full compliance with *Government Auditing Standards*:

1. Independence

GAS 3.08 requires that...*the auditors should apply the conceptual framework at the audit organization, audit, and individual auditor levels...*

We found that there was no documentation evidencing that all threats to independence were evaluated according to conceptual framework approach to independence.

As an alternative procedure, we interviewed the KOPA staff to understand your actual practice of evaluating independence. The Peer Review Team was satisfied that the KOPA process ensures that threats identified and evaluated; and safeguards and controls are implemented. However, the process of identifying, evaluating, and safeguarding of threats was not documented.

We recommend that the KOPA Management should ensure that the process of identifying, evaluating and mitigating threats to independence be documented.

2. Professional Judgment

GAS 3.60 requires that...*Auditors must use professional judgement in planning, and performing audits and in reporting the results.*

We hardly determined whether this principle was appropriately applied in the audit because its compliance was not cross indexed from the quality control checklist to the related working papers. According to the KOPA staff however, they are actually exercising professional judgment during planning specially in the application of significance, in the assessment of the appropriateness and sufficiency of evidence, in the selection of audit sample, and others. However, they were not conscious of cross indexing when the principle (professional judgement) was applied.

We recommend that the auditors should ensure that the application of the professional judgement should be referenced from the quality checklist to the related working papers so that its application could be properly reviewed for correctness and appropriateness.

3. Competencies

GAS 3.27 requires that...*the staff assigned to conduct an audit in accordance with GAS should collectively possess the technical knowledge, skills, and experience necessary to be competent for the type of work being performed before beginning of work on that audit.*

We found that the working paper did not include an assessment of competencies of staff assigned to an engagement.

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As a result of not documenting the assessment, the competence of the staff in performing audit assignment may not be assessed properly and, thus the staff may produce a sub-standard output that would lead to inefficiencies of doing work.

According to the Audit Manager, they were assessing staff competencies based on the record of 'Continuing Profession Education', working experiences and educational attainment but these were not being documented.

We recommend that the KOPA Management to ensure that assessment of the staff competencies be properly documented at the beginning of audit.

4. Quality Assurance Review Checklist (QARC)

Best practice in audit requires that performance of controls in a checklist should be indexed and cross indexed to related working papers to facilitate review and verify performance.

F-1 7/4 The KOPA implemented QARC to assure its compliance with GAS standard requirements. The form was being filled up after completing each audit. However, we noted that the performance of each control was not indexed to corresponding working papers. Thus, it was inefficient for the reviewer to verify compliance.

As a result, the staff might confirm (yes) a particular control without actually complying with a particular GAS requirement.

The KOPA Management is not ensuring that the performance of controls in QARC is indexed and cross indexed.

We recommend the auditors should ensure that the performance of controls in QARC, as one of the important quality document in the Quality Control System, should be indexed/cross indexed against the related working papers to ensure compliance of audit with the standard.

5. Planning

GAS 6.07 requires that *...auditors must plan to reduce audit risk to an appropriate level.* Further, GAS 6.11 requires *...that auditors should assess audit risk and significance within the context of the audit objectives by gaining understanding of the nature and profile of the program, internal controls, provision of laws and regulations by considering the risk of fraud, abuse, misuse and others.*

F-1 7/4 We found that risk assessment is not being documented. During the interview with the KOPA staff, there are actually assessing audit risks of every audit. During the planning stage, they will meet and discuss operational, control and fraud issues related to the assignment. However, these discussions on risk assessment was not recorded and only reflected in the audit program and procedures.

As a result, control or fraud risks may escape evaluation and detection and the audit risk may not be reduced to an appropriate level.

The KOPA staff does not ensure that the audit risk assessment is documented.

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We recommend that the Audit Management to ensure that the risk assessment be documented.

6. Evidence

GAS 6.56 to 6.57 requires that the auditors should obtain sufficient, appropriate evidence. Further GAS 6.58 requires that in **assessing** evidence, auditors **should evaluate** whether the evidence taken as a whole is sufficient and appropriate for addressing the audit objectives and supporting findings and conclusions.

T We found that the assessment of audit evidence supporting audit objectives and conclusion was not documented. As result, there was no assurance that the evidence on file is sufficient and appropriate to support the audit objectives and conclusion.

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T During interview, the Audit Manager said is actually assessing evidence every time a working paper is forwarded to her for review. However, the assessment is documented in form of verbal follow up procedures. On the part of the peer review team, we obtained a sample report and assessed the sufficiency and appropriateness of related evidence and was satisfied that the evidence was sufficient and appropriate.

T We recommend that the auditors and management to ensure that the assessment of sufficiency and appropriateness of evidence be documented to assure that the audit objectives and conclusions are properly addressed and supported by evidence.

7. Documentations

GAS 6.79 requires that... auditors should prepare documentation in sufficient detail to enable experienced auditor, having no previous connection to the audit, to understand from the audit documentation the nature, timing, extent and results of audit procedures performed, the evidence obtained and its source and the conclusions reached, including evidence that supports the auditor's significant judgements and conclusions.

- We found the following deficiencies during the review of working papers:

- T** A. All working papers especially the working papers for audit evidence were not initialed indicating supervisory review;
- F-1 4/4** B. Inadequate indexing and cross-indexing of working papers to facilitate review;
- T** C. Purpose, source, stamp of date received, audit procedures and conclusions, if necessary, not indicated;

T As a result, the working papers were not prepared completely and properly organized.

The KOPA staffs were not so conscious when it comes to proper preparation of working papers.

We recommend that the auditors should ensure that the documentation be prepared in sufficient detail.

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8. Audit Manual and Quality Control Description

Best practice requires that manual or system be updated to provide an effective guide to the staff in their daily work.

We found that the current audit manual in use and the Description of Quality Control System (APIPA Form) presented to peer reviewer were outdated and based on 2007 version and not on latest GAS 2011 revision.

As a result, the auditors may not be applying the latest audit principles, system of controls, and standards in their audit work.

We recommend that Public Auditor ensures that the Audit Manual and the Description Quality Control System (APIPA Form) to be updated to reflect the latest GAS 2011 Revision.

9. Other Matters

Previous Peer Review Report and Working papers

In the peer review guidelines, the audit organization is responsible for retaining the peer review working paper.

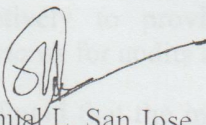
KOPA did not have on file previous peer review working papers and peer review report. As a result, the peer review team was not aware of the peer review history findings. Further, the peer review team was not able to follow up previous peer review recommendations, if any were implemented.

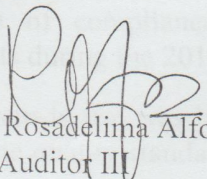
The Public Auditor said that the working paper binder for the previous peer review was not given to him. Further, the previous peer review report cannot be located.

We recommend that the Public Auditor to always request and keep the peer review working papers in a secured place.

We discuss this report with management and staff and they agreed with our observations and recommendations. We forwarded this report to the Public Auditor for formal management response. However, we have not received the management response so we are issuing this report without such response.

We appreciate the cooperation and support of KOPA Management and Staff during this peer review. We also appreciate the support of Drummond Kahn, Consultant, for his valuable advice in conducting of this peer review.


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