



## **Chapter 15**

### **Audit Process Guidance**

#### **A. Objective of the Financial Statement Audit**

An audit is the process of accumulating and evaluating evidence by a competent independent person about quantifiable information of a specific economic entity for the purpose of determining and reporting upon the degree of correspondence between the quantifiable information and established criteria. The financial statement audit applies this concept to the financial statements prepared by the entity.

In the case of the Federal Government there is also increased compliance auditing due to extensive regulation by government authorities and the importance of accountability to the public. Federal compliance audits include compliance with financial laws and regulations and compliance with fundamental internal control procedures.

#### **B. Auditor Responsibilities**

The auditors are responsible for planning, supervising, and completing the procedures necessary to complete the audit in accordance with auditing standards generally accepted in the United States of America, the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, and OMB Bulletin No. 01-02, *Form and Content of Agency Financial Statements*.

As a result of the audit procedures completed, the auditors will issue a combined report that includes the following:

- Their opinion on the financial statements;
- The results of their consideration of internal controls, and
- The results of their tests of compliance with laws and regulations.

##### **1. *Opinion on the Financial Statements***

The opinion is the result of the audit of financial statements conducted to determine whether the overall financial statements are presented in accordance with Generally Accepted Accounting Principles (GAAP). For the Federal Government GAAP are those standards established by the Federal Accounting Standards Advisory Board (FASAB) and issued to the Federal Government by the Office of Management and Budget and the General Accounting Office (GAO.)

##### **2. *Report on Internal Controls***

The auditors will obtain an understanding of the components of internal control, test the design of the controls, and, if designed properly, will test the operating effectiveness of the controls and report on their findings. The scope of internal controls shall include the following controls:



- *Financial reporting controls (including EDP controls)* for each assertion within a class of transactions (i.e. existence, completeness, accuracy, valuation, rights/obligations, presentation and disclosure);
- *Compliance controls* for each key provision of laws and regulations;
- *Budget controls* for each relevant budget restriction;
- *Operations controls* for each operations control relied on in performing financial audit procedures;
- *Performance measure control* for performance measures disclosed in the Management Discussion and Analysis (MD&A); and
- *Required Supplementary stewardship information controls*. The auditors will include reportable conditions and material weaknesses that come to their attention in the internal control section of the combined internal auditors' report. Reportable conditions are significant deficiencies in the design or operation of internal control that, in the auditor's judgment, could adversely affect Interior's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements being audited. Material weaknesses are reportable conditions that have a higher level of risk of a material misstatement in the financial statements.

3. ***Report on Compliance with Laws and Regulations***

The auditors will perform tests to determine compliance with laws and regulations that could have a direct and material effect on the financial statements, required supplementary information, and required supplementary stewardship information, including laws governing the use of budget authority, and any other laws, regulations, and government-wide policies identified in Appendix C of OMB Bulletin 01-02. The auditors will report on their findings.

In addition, auditors will test Interior's compliance with the Federal Financial Management Improvement Act of 1996 (FFMIA), section 803(a) requirements and report on their findings. This includes determining whether Interior's financial management systems comply with the: (1) federal financial management system standards; (2) applicable federal accounting standards; and (3) the standard general ledger at the transaction level.

4. ***Management Discussion & Analysis, Required Supplementary Information, and Required Supplementary Stewardship Information***

The auditors' will perform the procedures described in AICPA's Codification of Auditing Standards AU Section 558, "Required Supplementary Information" for each of the following categories:

- Management discussion and analysis
- Required supplementary information
- Required supplementary stewardship information



The auditors will inquire of management about the methods of preparing information and compare the information for consistency with (1) management's responses to these inquiries, (2) audited financial statements, and (3) other knowledge obtained during the examination of the financial statements.

5. ***Other Accompanying Information***

The auditors will assess whether the following accompanying information or its manner of presentation, is materially inconsistent with the information in the financial statements.

C. **Responsibilities of the Office of Inspector General (OIG)**

The OIG to fulfill its responsibilities under the Chief Financial Officers Act of 1990 and the Government Management Reform Act of 1994 has contracted with KPMG to audit the financial statements of the Department and the bureaus. The OIG is responsible for evaluating the independence, objectivity, and qualifications of KPMG and reviewing the work performed for compliance with generally accepted government auditing standards (GAGAS) and contract terms.

D. **GAO Audit Oversight**

The General Accounting Office (GAO) is responsible for the audit of the Government-wide financial statements. In this capacity, GAO personnel will be reviewing certain audit work papers and audit procedures. However, the OIG remains the sole auditor of bureau financial data. Management of GAO, the OIG and PFM have agreed that any requests for information that GAO might have will be discussed with the OIG and, if necessary, passed on to the bureau by the OIG.

We will continue to work with OIG and GAO to ensure that GAO reviews are performed on a timely basis and do not interfere with timely completion of bureau and Department financial statements

E. **Management Responsibilities**

Management is responsible for identifying and recording all financial transactions in accordance with generally accepted accounting principles, legal requirements and regulations. This includes:

- Establishing and maintaining internal controls over financial reporting; required supplementary stewardship information, required supplementary information, other accompanying information and performance measures.
- Preparing the financial statements in conformity with generally accepted accounting principles.



- Complying with laws and regulations, including Federal Financial Management Improvement Act (FFMIA) requirements.

Management's responsibilities require the coordination between Departmental, program, performance and financial management.

1. ***Departmental Management Responsibilities***

- Prepare the Accountability Report including consolidated financial statements for the Department of the Interior that are subject to independent audit review.
- Prepare and submit interim financial statements to management and OMB.
- Establish and issue financial accounting policy for the Department implementing Federal Accounting Standards Advisory Board standards and other directives from the Office of Management and Budget and the Department of the Treasury
- Provide overall coordination for the financial statement audits
- Submit data to the Department of the Treasury in support of the Consolidated Financial Statements for the Federal Government (FACTS I).

2. ***Performance Management Community Responsibilities***

- Collect performance management information for quarterly and annual performance reporting.
- Prepare the performance report for the Department and its specific entities in coordination with the finance offices.

3. ***Program Manager/Field Location Responsibilities***

- Adhere to financial policies and year-end financial closing instructions on a timely basis related to specific program activity.
- Ensure the integrity of financial transaction processes in field locations.
- Ensure transactions are processed on a timely basis and that all appropriate information is accurate and entered properly into the finance system. Such transactions would include payroll transactions, sale of goods and services, cash receipts, purchase transactions, charge card purchases, acquisition and disposition of property, etc.
- Ensure that complete documentation is maintained to support financial transactions, such as credit card purchases, obligations, other payments, etc. (This documentation must be readily available for review by management and internal or external auditors.)



- Review unliquidated obligations (undelivered orders) on a quarterly basis to ensure validity and accuracy. All obligations that are determined to be invalid or unnecessary should be removed or rescinded in a timely manner.
- Work with finance offices to clear suspense funds (both “budget clearing funds” and “deposit funds”) on a timely basis (at least monthly). At the end of each quarter all suspense funds shall be cleared to zero except when exempt by specific legislation or Treasury guidance.
- Bill customers and record receivables promptly in the financial management systems. Ensure finance offices are notified on a timely basis when deposits are made to lock boxes to ensure transactions are properly reflected in the accounting records.
- Review receivables and loan accounts for accuracy on a quarterly basis.
- Refer delinquent debt to the Department of the Treasury within the timeframes required (180 days) by the Debt Collection Improvement Act.
- Review accounts receivable and loans for write-off on a monthly basis. Ensure allowances for uncollectable accounts receivables are reviewed and updated quarterly.
- Ensure all acquisition, deletions and transfers of property are reflected in the accounting records promptly and accurately at the end of each quarter.
- Working with property managers, ensure that all depreciation for property, plant and equipment shall be booked by the end of each quarter in the accounting system (FFS or ABACIS).

#### 4. ***Bureau Finance Office Responsibilities***

- Ensure the accuracy and completeness of financial information and presentation of financial statements in accordance with applicable standards including accurate and timely adjustments and accruals.
- Prepare quarterly financial statements for use by management.
- Prepare the financial statements and related footnote information for annual financial statements.
- Maintain the internal control environment to ensure accuracy and integrity to financial data maintained in the core accounting and related financial management systems.
- Reconcile cash balances with the U.S. Treasury on a timely basis (preferably monthly).
- Reconcile subsidiary records to control accounts in the core accounting systems on a timely basis (preferably monthly).
- Ensure that vendor codes are accurate and reflect the correct trading partner data in cooperation with the procurement and program communities.



- Implement year end accounting and reporting instructions from the Department of the Treasury, the Office of Management and Budget, and the Department of the Interior.
- Reconcile transactions that occur between bureaus and with other Financial agencies.
- Review budget execution data with bureau budget offices and submit budget execution data to the Department of Treasury (FACTS II) on a timely basis.

## F. **Audit Process**

The audit process requires close cooperation between the OIG, the Independent Public Accountants (IPA), the Office of the Secretary, and individual bureaus, both from a finance office staff, program officials and other interested parties in the bureaus. Coordination between Departmental, bureau, field operations, the IPA and OIG personnel at the Department, regional office and field audit team levels is important for the timely resolution of issues and timely completion of the audits.

The following steps will occur for each audit:

1. The OIG will issue an audit notification letter.
2. The IPA audit team will prepare an audit plan.
3. The OIG and the IPA will meet with bureau personnel in an entrance conference to outline the audit plan and initiate the audit activities.
4. After appropriate review and discussion with the auditors, the bureau, the OIG and the IPA audit team will agree on the dates for delivery of materials associated with the audit process and the expected timing for the audit activities.
5. The Department and the bureaus are responsible for providing accurate information and support to the IPA in a timely fashion to complete the audit work.
6. OIG and IPA staff will be given read-only rights to the Consolidated Financial Statements Application (Hyperion Enterprise) and to the "XA" Server to provide them with immediate access to updated financial data and information/instructions maintained for financial statement preparers in shared directories.
7. Periodic meetings will be held at the bureau level and at the Department level to identify issues that need to resolve, to coordinate activities and to address any other issues that relate to the audit.
8. The OIG and Department personnel will track the issues until resolution between the Department, the OIG and the IPA.
9. Issues included in the Report on Internal Controls, or in the Report on Compliance with Laws or Regulations will be reported to the OIG and the Assistant Secretary for Planning, Management and Budget for tracking as part of the Management Control process.
10. Periodic meetings will be held between the Inspector General and the Assistant Secretary for Planning, Management, and Budget and their staffs will meet periodically to monitor progress on audit activities.



11. The text of issues that will be included in the auditors report will be provided in writing to the Department or individual bureaus as early as possible in the audit process to allow time for adequate discussion and final agreement on the issues and final report text.
12. Upon receipt of the draft report, bureaus or the Department will have no more than 10 working days to respond in writing to the report. With the agreement of both the OIG and the IPA audit teams and Department/bureau management, responses to audit findings may be provided as text to be included in the final opinion, report on internal controls or report on compliance with laws and regulations, as long as the text is provided within 10 working days from receipt of the draft report.

Critical throughout this process is the timely completion of all tasks and the open communication between auditors and annual financial statement preparers. At the end of the audit process for the Department, Department personnel, OIG and the IPA personnel will meet to determine what went well, what areas need to be improved and make recommendation for improvements to the process for the next year.

#### **G. Representation Letters**

As part of the audit of financial statements conducted in accordance with OMB requirements, the auditor obtains written representation from management. In their Management Representation Letter, which must be customized for the circumstances of the audited entity, the agency head and Chief Financial Officer confirm to the Inspector General various representations relating to:

- ❖ The opinion on the financial statements and the required supplementary stewardship information,
- ❖ The effectiveness of internal control,
- ❖ The financial management system's substantial compliance with Federal financial management system requirements, and
- ❖ Compliance with laws and regulations

After bureaus submit their Management Representation Letters, the Assistant Secretary–Policy, Management and Budget submits one applicable to the Department's consolidated financial statements.

Further guidance for preparation of the FY 2001 Management's Representation Letter, including suggested wording for specific representations, will be provided.

**See Appendix Q for the Management Representation Letter.**

#### **H. Audit Management**

The following are recommended procedures, collectively generated by the bureaus, for





## working with KPMG:

- Confirm outstanding PBC items at weekly meetings.
- Consider having KPMG sign or initial for receipt of PCB items.
- Assign right personnel to attend meetings.
- Identify who is responsible for maintaining PCB list (bureaus should consider doing this themselves).
- Assign a staff person and a backup person to monitor the PCB list. This person will act as central point of contact and sign off.
- Keep copies of documentation given to audit team or at a minimum copy the first page to provide an example of the package.
- Discuss approaches agreed upon in weekly FSGT meetings.
- Be forthcoming with audit personnel. The audit is based on mutual trust. The Department and its bureaus are responsible for providing complete and accurate information to its financial statement auditors and ensuring that financial information is accurate.