



**DEPARTMENT OF THE AIR FORCE**  
AIR FORCE AUDIT AGENCY

13 June 2005

MEMORANDUM FOR DEPUTY AUDITOR GENERAL, POLICY AND OPERATIONS  
MANAGEMENT, ARMY AUDIT AGENCY

FROM: HQ AFAA/DOV  
1126 Air Force Pentagon  
Washington DC 20330-1126

SUBJECT: Letter of Comments, 2005 Peer Review of the Army Audit Agency  
(Project F2004-FA1200-2121.000)

1. **Background.** In accordance with the Memorandum of Understanding dated 16 November 2004, we completed an external peer review of the Army Audit Agency (AAA). We reviewed the system of quality control for the audit function of the AAA in effect for (a) the 6-month period ended 30 September 2004 for selected audit reports and (b) the 12-month period ended 30 September 2004 for selected quality assurance (QA) reviews. Our formal report, provided under separate cover, concluded the AAA quality control system met standards established by the President's Council on Integrity and Efficiency (PCIE) and provides the AAA with reasonable assurance that auditors follow professional standards and internal policies. This letter contains observations and suggestions regarding issues that did not warrant inclusion in the formal report.

2. **Objective.** In performing our review, we considered the requirements of quality control standards and other auditing standards contained in the 2003 Revision of the *Government Auditing Standards* issued by the Comptroller General of the United States. We determined whether the AAA internal quality control system complied with government auditing standards and operated effectively to provide reasonable assurance that audit teams followed AAA internal policies and procedures. Specifically, we:

a. Evaluated AAA quality control policies and procedures related to staff qualifications and independence and the design of quality control policies and procedures related to audit performance and internal review.

b. Determined whether the AAA internal QA program was adequately designed to meet established QA objectives.

c. Evaluated two recent QA projects to determine if QA teams performed the reviews in accordance with AAA internal policies and procedures.

d. Determined for a sample of audits (eight performance, one attestation, and one classified) whether auditors adequately planned, executed, and documented procedures in accordance with auditing standards and AAA quality control policies and procedures.

3. **Overall Conclusion.** The AAA internal quality control program complied with government auditing standards, operated effectively, and provided reasonable assurance that audit teams generally followed AAA internal policies and procedures. The AAA designed its overall internal quality control system in accordance with applicable standards, and AAA auditors generally complied with established quality control policies and procedures. Although some areas required improvement, we concluded the projects reviewed complied with government auditing standards and internal policies and procedures. Specifically, AAA:

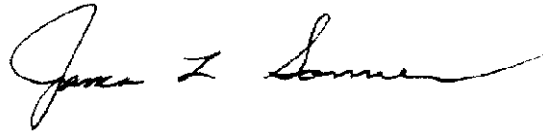
a. Adequately designed its internal quality review program to meet QA objectives, and assigned highly qualified and experienced auditors to conduct internal quality control reviews. Further, during the review, we determined the current internal QA program was considerably more robust than the QA programs reviewed during the Fiscal Years (FYs) 1999 and 2002 peer reviews. All AAA offices issuing reports were included in at least one QA review, and all aspects of auditing were covered by an internal quality control review. The QA program was functioning according to Agency policy, projects appeared to be well designed, and reports were well written and identified conditions that needed improvement. However, the AAA should require that all QA reports include recommendations to correct identified conditions or adequately explain why a recommendation was not required. In addition, management comments included in QA reports should identify specific actions taken or planned and include actual or estimated completion dates. (See Observations 1-2)

b. Policies and procedures related to staff qualifications, education, and independence complied with government auditing standards. In addition, the AAA quality control program and procedures related to audit performance and internal review adequately ensured auditors accomplished their audit projects in accordance with government auditing standards.

c. Quality assurance projects contained adequate evidence to establish that AAA auditors generally complied with government auditing standards and internal policies and procedures. Further, teams generally conducted QA projects in accordance with AAA internal policies and procedures. Consequently, we used these QA reports to support our opinion on the AAA internal quality control system operating effectiveness.

d. Auditors planned and conducted the eight performance audits, one attestation audit, and one classified audit reviewed in accordance with government auditing standards and AAA internal policies and procedures. The project reports and supporting documentation provided ample evidence that auditors properly planned and executed the reviewed audits, and the working papers adequately supported the conclusions reached during the audits. However, AAA audit teams should strengthen independence statement documentation, supervisory reviews, audit documentation, required report elements and timeliness, independent referencing, and internal quality control checklist accomplishment. For the attestation audit, improvements were required in the planning phase and monetary benefit documentation. (See Observations 3-9)

4. We express our thanks to you and your staff for their cooperation and professionalism. Should you have questions, please have your staff contact Mr. Leonard Miceli, Peer Review Project Manager, at (703) 696-7903 or me at (703) 696-7727.

A handwritten signature in black ink, appearing to read "James L. Sommer". The signature is fluid and cursive, with a long horizontal stroke at the end.

JAMES L. SOMMER  
Director, Policy, Oversight, and  
Systems Division  
Operations Directorate

Attachment:  
Observations and Suggestions

cc:  
DoDIG (AIG/APO)

## **OBSERVATIONS AND SUGGESTIONS**

**Observation 1 – Recommendations in QA Reports.** The QA program functioned according to Agency policy, projects appeared well designed, and reports were well written and identified conditions that needed improvement. However, four (three post audit reviews and one functional review) of nine QA reports issued in FYs 2003 and 2004 did not include recommendations to correct identified conditions or adequately explain why recommendations were not required.

**Suggestion 1.** The Director of Policy, Oversight, and Audit Support should require that all QA reports include recommendations to correct identified conditions or adequately explain why a recommendation is not required in the current report (e.g., if this same problem was identified and recommended action was stated in a prior report, but not implemented during the time period of the current review). The explanation should include the title and date of the prior report, recommended action, and date of implementation.

**Management Comments.** “Concur. This situation occurred because of the timing of some quality assurance reviews, the publication dates of the audit reports, and the timeframes of the work performed on those audits. The timelines for some of these overlapped and would have made some recommendations in quality assurance reports unnecessarily repetitive. The situation could have been explained better in the quality assurance reports. By 30 June 2005, the Deputy Auditor General, Policy and Operations Management will issue a memorandum to the Quality Assurance Branch directing them to include recommendations in quality assurance reports to correct all identified conditions as currently required by USAAAR 36-62 (Quality Assurance Program and External Quality Control Review Responsibilities). If recommendations aren’t included, the report will adequately explain why recommendations weren’t included to correct the reported conditions. By 30 September 2005, we will update USAAAR 36-62 to reflect this policy. Also, to prevent the situation caused by overlapping timelines of quality assurance reviews and reports, audit report dates, and the audit work performed; we have changed our procedures for selecting audits included in quality assurance reviews. We will consider both the date of publication of the audit report and the timeframe of when the audit was conducted.”

**Observation 2 – Monitoring Implementation of QA Report Recommendations.** The Chief, Quality Assurance Branch, maintained a schedule to track implementation of QA report recommendations, and the most recent QA plan included a project entitled, “Follow Up Review of Prior QA Report Recommendations.” However, management comments in response to QA report recommendations did not provide estimated completion dates for agreed-to actions. Further, management comments in response to QA report recommendations were not always specific and did not always contain planned corrective actions.

**Suggestion 2.** The Chief, Quality Assurance Branch should:

a. Require management to follow audit policies and procedures when providing comments in response to QA reports. In particular, require that management comments identify clear and specific corrective actions, with actual or estimated completion dates, in response to QA report recommendations.

b. Evaluate as nonresponsive management comments that do not provide clear and specific actions with actual or estimated completion dates.

**Management Comments.** “Concur. By 30 June 2005, the Deputy Auditor General, Policy and Operations Management will issue a memorandum to the Quality Assurance Branch requiring them to use a cover memorandum when transmitting quality assurance reports to Agency management. The memorandum will clearly specify that:

a. “Management comments identify clear and specific corrective actions, with actual or estimated completion dates in responses to recommendations in quality assurance reports.

b. “Replies not in accordance with the instructions will be deemed non-responsive and additional information will be requested.

“We will update USAAAR 36-62 by 30 September 2005 to include more specific guidance on what should be in a reply to recommendations in quality assurance reports. The policy will include the need to provide clear and specific actions, with actual or estimated completion dates. Replies not in accordance with the policy will be deemed non-responsive and additional information will be requested.”

**Observation 3 – Independence Statement Documentation.** We found no indications of external or personal impairments to independence during our review of audit reports, audit working papers, or during interviews with AAA audit personnel. However, 3 of the 10 audits reviewed were missing independence statements as required by USAAAR 36-3, *Audit Survey and Execution*, Appendix C.

**Suggestion 3.** The Deputy Auditor General for Policy and Operations Management should remind all agency personnel of the new requirement for independence statements and require supervisors to review independence statements for completeness on all audits.

**Management Comments.** “Concur. By 15 July 2005, the Deputy Auditor General, Policy and Operations Management will issue a memorandum to all Agency personnel discussing the results of the peer review of the Agency and reminding Agency personnel of the requirements in USAAAR 36-3 (Audit Survey and Execution) relating to documenting auditor independence. On 12 May 2005, we issued guidance on conducting in-process reviews on all audits in a timely manner (25 - 30 percent of planned auditor days expended) with executive level (SES/GS-15) involvement to discuss milestones, resources, and any changes to objectives and/or scope and methodology. Included in the list of required information for the in-process reviews is a requirement to confirm that each team member has signed the Auditor Independence Declaration. We also included this requirement in the Agency’s 16 May 2005 staff notes.”

**Observation 4 – Supervisory Reviews.** The level of instructions provided to the audit staff appeared appropriate considering the knowledge and experience of the staffs. The projects showed sufficient evidence of supervisory involvement. However, 6 of 10 projects did not have higher-level supervisory initials and dates documenting working paper reviews. To illustrate, in one project, 74 percent of working papers did not show evidence of supervisory review while the

other five projects averaged 26 percent. This observation was also identified in the 2002 peer review. Additionally, none of the spreadsheets in any projects reviewed contained the supervisor's signature and date of review.

**Suggestion 4.** The Deputy Auditor General for Policy and Operations Management should:

a. Remind audit supervisors of their responsibility to review, initial, and date working papers and prepare review comments to document their observations as required by USAAAR 36-3, Chapter 7, paragraph 4a.

b. Make this area a special interest item on future QA reviews.

**Management Comments.** "Concur. By 15 July 2005, the Deputy Auditor General, Policy and Operations Management will issue a memorandum to all Agency personnel discussing the results of the peer review of the Agency and reminding Agency personnel of the requirements in USAAAR 36-3 relating to supervisory review of working papers and documenting those reviews. Supervisory review of working papers will continue to be a special interest item on future quality assurance post audit reviews and on FY06 functional reviews. In addition, our new Independent Review Checklist includes a question on whether the working papers have been reviewed. The independent reviewer must comment on whether the working papers have been reviewed. The Independent Review Checklist will be included in USAAAR 36-4 (Report Writing Process). We will issue USAAAR 36-4 by 30 September 2005."

**Observation 5 – Audit Documentation.** The term "working papers" refers to all documents, papers, and records prepared or collected by auditors. We found working papers contained sufficient, competent and relevant evidence to support findings, judgments, and conclusions in the reports. However, improvements could be made to audit documentation. Specifically:

a. None of the spreadsheets reviewed contained purpose, source, scope, and conclusion which are required by USAAAR 36-3, Chapter 6, paragraph 3b.

b. Three of the projects claiming monetary benefits on USAAAR Form 328, **Summary of Potential Monetary Benefit**, were not cross referenced to supporting working papers. In addition, monetary benefits for one project were not clearly associated with a report recommendation as required by USAAAR 36-52, *Interim Guidance Potential Monetary Benefits*.

c. During the review of the selected projects, we noted some electronic working paper files in most projects reviewed were opened and saved after the final report was issued. While we could not determine what or if any changes were made, the working papers we reviewed properly supported the issued report.

**Review Comment.** On 4 April 2005, AAA established policy for archiving working papers which addressed the ability to modify work papers after the final report was issued. The new policy stated, "To help ensure we meet the standards in both fact and appearance, effective immediately, 1 week after the editors send the final report to PMO-L for publication, PMA-T will archive the working papers and the files will become read-only documents. Audit teams

should post any remaining documents to the work paper files during that 1-week window before the files are locked. If the need arises to modify the working papers (for example, the official army position if the final report was published without it) there will be a folder named "Post-Audit Adjustments." This folder will be in the same location and have the same permissions as the original audit files." Since AAA initiated action during the review, we did not suggest any further action.

**Suggestion 5.** The Deputy Auditor General for Policy and Operations Management should require that all agency personnel comply with established guidance for working papers, i.e. spreadsheets, must contain purpose, source, scope and conclusion. Additionally, all monetary benefits claimed should be supported by and cross referenced to supporting working papers and associated with a report recommendation.

**Management Comments.** "Concur. By 15 July 2005, the Deputy Auditor General, Policy and Operations Management will issue a memorandum to all Agency personnel discussing the results of the peer review of the Agency and reminding Agency personnel of the established guidance for working paper preparation and content. The memorandum will also address the requirement for monetary benefits to be supported by and cross-referenced to supporting working papers and associated with a report recommendation. In addition, we will issue our updated Automated Working Paper Manual by 30 June 2005. The manual provides specific guidance on cross-referencing and linking the report (to include monetary benefits) to supporting working papers. The guidance will require that all facts, figures, results, and conclusions in reports be cross-referenced to a working paper with a purpose, source, scope and conclusion. Figures or numbers in working papers should be linked to a spreadsheet where appropriate. In addition, auditors will be required to link all spreadsheets to a working paper with a purpose, source, scope, and conclusion and will also be required to identify in the spreadsheet the working paper that relates to the spreadsheet."

**Observation 6 – Audit Reports.** The auditors accomplished field work in a timely manner, and reports contained the required elements for providing Army management with a quality product. Also, each report's introduction, audit scope, and methodology section properly described the reason for the audit and provided management details on steps performed. The reports' findings included condition, cause, effect, conclusion, and recommendations. Further, reports contained management comments and were signed and dated. However, we noted the following:

a. Missing Elements. One audit report did not include the time period of transactions reviewed, universe of sampled items, nor the cause and effect for one finding.

b. Timeliness. Although fieldwork was accomplished timely, two reports were published 18 and 21 months after command was briefed because the staff was awaiting responsive comments.

**Review Comment.** On 23 February 2005, AAA established policy in USAAAR 36-5, *Report Reply and Followup Process*, for issuing audit reports without Command comments. The new policy stated, "When response officials don't properly reply to the recommendations within the 30-day period, or if the reply doesn't meet all the criteria, the Audit Manager or AIC should

contact the cognizant audit focal point to request assistance in obtaining a fully responsive command reply. All reasonable effort should be taken to obtain fully responsive replies. When responsible officials don't provide a reply, the audit team should add a comment beneath the recommendation, or series of recommendations, indicating that they requested comments, but didn't receive them by the time the report was published." Since AAA initiated action during the review, we did not suggest any further action.

**Suggestion 6.** The Deputy Auditor General for Policy and Operations Management should remind agency personnel of required report elements contained in USAAAR 36-53, *Writing Audit Reports*, Appendix H, paragraph 4, and Appendix L.

**Management Comments.** "Concur. By 15 July 2005, the Deputy Auditor General, Policy and Operations Management will issue a memorandum to all Agency personnel discussing the results of the peer review of the Agency and reminding Agency personnel of the required report elements."

**Observation 7 – Independent Referencing.** Personnel independent from the audit in grades GS-12 and higher verified that statements of fact, figures, and dates were accurately reported; the findings were adequately supported by documentation and conclusions; and recommendations flowed logically from the support. The referencers placed their initials next to each fact and figure referenced on the draft report and completed the USAAA Form 371, **Certification Document**, before the draft report was provided to Command. However, report referencing could be strengthened. Specifically:

a. Four projects had independent referencer markings on the report, but not on the supporting and/or summary working papers. Further, we could not locate a signed USAAA Form 371 for one project.

b. For two projects, the peer reviewers required assistance from the auditor-in-charge or audit manager to validate the potential monetary benefits, and determined the independent referencers could not have verified monetary benefits since the USAAA Form 328 was not linked to supporting working papers.

c. One draft was submitted to Command before the report was independently referenced. For another draft, the independent referencing was started but not completed before the report was submitted to Command. This observation was also identified in the 2002 peer review.

**Suggestion 7.** The Deputy Auditor General for Policy and Operations Management should require that supervisors:

a. Review USAAAR 36-85, *Independent Report Referencing*, requirements with the independent referencer prior to starting each referencing assignment.

b. Periodically review referencers' work to ensure conformance with USAAAR 36-85 referencing requirements.



**Management Comments.** “Concur. By 15 July 2005, the Deputy Auditor General, Policy and Operations Management will issue a memorandum to all Agency personnel discussing the results of the peer review of the Agency and reminding Agency personnel of the requirements in USAAAR 36-85 relating to supervisors reviewing the policy requirements with the independent reviewer before starting the referencing assignment and periodically reviewing the reviewer’s work to ensure conformity with Agency policy. In addition, we’ve included a question in our new Independent Review Checklist on whether supervisors discussed duties and expectations with the independent reviewer before starting the referencing assignment. The Independent Review Checklist and guidance on independent reviewing will be included in USAAAR 36-4 (Report Writing Process), which will be issued by 30 September 2005 and will supersede USAAAR 36-85.”

**Observation 8 – Internal Quality Control.** We determined AAA quality control procedures were generally implemented. Auditors prepared an internal quality control checklist; however, procedures for completing and addressing all entries in the checklist could be improved. For example, different versions of checklists were used, management items not completed or omitted were not always explained, and the program director did not always sign the checklist as required.

**Suggestion 8.** The Deputy Auditor General for Policy and Operations Management should:

- a. Review the various versions of the internal quality control checklists, select the one that best meets AAA needs, and require the use of the selected checklist.
- b. Revise USAAAR 36-3, Chapter 9, paragraph 4b to include the requirement to explain any omitted checklist steps.
- c. Require supervisors to review USAAAR 36-3, Chapter 9, paragraph 4b requirements prior to completing the checklist, and obtain appropriate program director signature and date for the completed checklist.

**Management Comments.** “Concur. By 15 July 2005, the Deputy Auditor General, Policy and Operations Management will issue a memorandum to all Agency personnel discussing the results of the peer review of the Agency and reminding Agency personnel of the requirements to complete the Quality Control Checklist and obtain the appropriate program director’s signature and date for the checklist. The memorandum will inform Agency personnel that the checklist dated 12 February 2004 is the checklist that they should be using. This version of the checklist is currently available in USAAAR 36-62. The checklist can also be obtained from the audit templates file and the quality assurance Web page on the Agency’s intranet. The various sections of the checklist and completing the checklist are discussed in USAAAR 36-2 (Guidance for Planning an Audit Engagement), USAAAR 36-3 (Audit Survey and Execution), (Draft) USAAAR 36-4 (Report Writing Process), and USAAAR 36-5 (Report Reply and Followup Process). By 30 September 2005, we will include a standard policy paragraph on the Quality Control Checklist in the regulations. The policy will direct auditors to find the most current checklist in the templates file on the intranet. The updated Quality Control Checklist will require an explanation for omitted checklist steps.”

**Observation 9 – Attestation Engagements.** An attestation engagement concerns examining, reviewing, or performing agreed-upon procedures on a subject matter or assertion and reporting the results. An assertion is any declaration about whether the subject matter is based on or conforms with the criteria selected. Attestation engagements can cover both financial and nonfinancial objectives. Auditors should perform attestation engagements only if they believe the subject matter is capable of evaluation against criteria that is suitable and available to users. USAAAR 36-3 and USAAAR 36-4, *Audit Reporting*, implement attestation standards. Overall, AAA procedures were adequately followed; however, not all processes complied with established policies. Specifically:

a. The type of attestation (Review, Examination or Agreed-Upon Procedures) to be performed and the client assertion were not included in the engagement planning documentation.

b. The auditors omitted required attestation steps to review and consider prior audit coverage, establish type of attestation engagement, and address internal controls and fraud without documenting the reasons for the omissions in the working papers.

c. Working paper documentation did not contain all the criteria to support a claim of monetary benefits. The working papers did not show where the amount claimed was funded to a program in the Program Objective Memorandum, Program Decision Memorandum, or the Future Years Defense Program. Additionally, documentation was not available to support that management had taken complete corrective action (in lieu of a recommendation) to realize the claimed monetary benefits.

**Suggestion 9.** The Deputy Auditor General for Policy and Operations Management should require auditors and supervisors follow the established attestation guidance.

**Management Comments.** “Concur. By 15 July 2005, the Deputy Auditor General, Policy and Operations Management will issue a memorandum to all Agency personnel discussing the results of the peer review of the Agency and reminding Agency personnel to follow the established guidance when performing attestation engagements. The Agency’s guidance incorporates the Government Auditing Standards on performing attestation engagements. We are currently performing a quality assurance review of attestation engagements which we expect to complete by 30 June 2005. Depending on the results of our review, we may revisit Agency policy on performing attestation engagements.”

**Evaluation of Management Comments.** AA officials agreed with the peer review results, and management’s taken and planned actions are responsive to the report issues and suggestions.