



DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20005

INSPECTOR GENERAL
FOR TAX
ADMINISTRATION

November 28, 2006

The Honorable Thomas F. Gimble
Acting Inspector General
U.S. Department of Defense
400 Army Navy Drive
Arlington, Virginia 22202

Subject: Report on the External Quality Control Review of the Department of
Defense's Inspector General Audit Organization

Dear Mr. Gimble:

This report presents the results of our External Quality Control Review of the Department of Defense's Inspector General Audit Organization. Your response to the draft report is included as Exhibit C with excerpts and our position is incorporated into the relevant sections of the report.

We agree with your proposed corrective action to Recommendations 2, 3, and 4. We continue to believe that additional actions are required for Recommendation 1, and we have provided audit comments.

Sincerely,

J. Russell George
Inspector General

Attachment



DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20005

INSPECTOR GENERAL
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November 28, 2006

To: Thomas F. Gimble, Acting Inspector General
Department of Defense

We have reviewed the system of quality control for the audit function of the Department of Defense (DoD), Office of Inspector General (OIG), in effect from April 1, 2005, through March 31, 2006. A system of quality control encompasses the OIG's organizational structure, and the policies adopted and procedures established to provide it with reasonable assurance of conforming with generally accepted government auditing standards (GAGAS). The elements of quality control are described in GAGAS, promulgated by the Comptroller General of the United States. The design of the system, and compliance with it in all material respects, are the responsibility of the DoD OIG.

Our objective was to determine whether the internal quality control system was adequate as designed and being complied with to provide reasonable assurance that applicable auditing standards, policies, and procedures were met. Our responsibility is to express an opinion on the design of the system and the OIG's compliance with the system based on our review.

Our review was conducted in accordance with the guidelines established by the President's Council on Integrity and Efficiency and the Executive Council on Integrity and Efficiency. In performing our review, we obtained an understanding of the system of quality control for the OIG. In addition, we tested compliance with the OIG's quality control policies and procedures to the extent we considered appropriate. These tests included the application of the OIG's policies and procedures on selected audits. Because our review was based on selective tests, it would not necessarily disclose all weaknesses in the system of quality control or all instances of lack of compliance with it. Nevertheless, we believe that the procedures we performed provide a reasonable basis for our opinion.

Because there are inherent limitations in the effectiveness of any system of quality control, departures from the system may occur and not be detected. Also, projection of any evaluation of a system of quality control to future periods is subject to 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.

Our scope and methodology appears as Exhibit A. General comments appear as Exhibit B.

UNMODIFIED OPINION REPORT

In the Treasury Inspector General for Tax Administration's opinion, the system of quality control for the audit function of the Department of Defense (DoD), Office of Inspector General (OIG), in effect for the year ended March 31, 2006, was designed to meet the requirements of the quality control standards established by the Comptroller General of the United States for a Federal Government audit organization. In addition, the system of quality control was complied with during the year ended to provide the OIG with reasonable assurance of conforming with applicable auditing standards, policies, and procedures. We noted, however, conditions that warrant your attention although they did not impact our opinion. These matters are described in the Findings and Recommendations that follow.

Findings and Recommendations

Finding 1. Reporting Views of Responsible Officials

Generally Accepted Government Auditing Standards (GAGAS) emphasize that one of the most effective ways to ensure that a report is fair, complete, and objective is to request the responsible officials of the audited entity and others, as appropriate, to review the report and provide written comments. When comments are provided by management, auditors are expected to report the views of those responsible officials concerning the auditors' findings, conclusions, and recommendations. By including and addressing the views of responsible officials in the report, the report presents not only the auditors' position but also the responsible official's perspective on the audit results.

The OIG's policies and procedures closely parallel the requirements in GAGAS. The guidance requires that auditors synthesize management's comments in the final report findings and include a complete text of management's comments as an attachment to the report. The synopsis of management's comments should fully and fairly present all nonconcurrence and disagreements with the findings, conclusions, and recommendations. As such, each nonconcurrence or disagreement should be discussed with management, and the report should rebut or accept management's arguments, as needed.

In one audit, the OIG did not include DoD management's comments in the final report. Our review showed that the OIG elected not to include management's written comments or a summary of the comments even though the comments were received over six weeks prior to the issuance of the final report. The OIG omitted management's response because it was received after the extended due date. The report stated, however, that the comments were not included because they were received "*...too late to be incorporated into the final report.*" Since the DoD response was positive, the OIG maintained that there was no harm in excluding it from the report. Nevertheless, the OIG had ample time available to incorporate the response.

In three other reports, DoD management disagreed with some of the draft audit reports' conclusions and recommendations and provided detailed reasons for their disagreements. The OIG concluded that the responses were "unresponsive" and asked management to provide additional comments. Efforts were not made to revise the reports or to adequately rebut management's positions. The OIG then issued the final reports without waiting for the additional comments. As a result, a reader of the report would not know how the disagreements were resolved.

To determine whether this practice was common, we reviewed 55 final reports available on the OIG's website that contained recommendations. The 55 reports were issued between April 2005 and March 2006. In 31 of 55 reports (56 percent), the OIG asked management for additional comments and proceeded to issue the final report without waiting for the revised response. For 19 of the 31 reports, the audit team or a mediation office within the OIG resolved the existing conflicts after the final report was issued. On average, the post final report mediation process took 81 days to complete. For 5 of the 19 reports, the disputed items were resolved by the audit team using the same information provided by management in their original response to the draft report. The 12 remaining reports were issued as early as May 2005 and still remained unresolved as of June 8, 2006.

Instead of resolving these disagreements prior to issuing the final report, the OIG has had a long-standing practice of waiting to resolve some unagreed issues until after the report is finalized. While this practice may expedite the issuance of the final report, the supplemental information can be important and should always be considered before reporting the auditors' final conclusions and recommendations.

If management's comments and corrective actions are not effectively addressed by the OIG, the report user is not provided a sense of the responsible official's perspective on the report issues. This practice also requires DoD management to spend additional resources providing multiple responses to the same issues. During our review, the Deputy Inspector General for Auditing addressed this issue by expanding the responsibilities of the Quality Assurance, Policy, and Electronic Documentation Division to include reviewing final reports after issuance to ensure that management comments are fairly recognized, any disagreements by management are sufficiently addressed, and the audit report is modified when appropriate. We are also recommending the following:

Recommendation 1 – The Deputy Inspector General for Auditing should discontinue the routine practice of issuing final reports without resolving disagreements. If management provides additional information in its response, the Assistant Inspector General should evaluate it before issuing the final report and either appropriately revise the report or adequately rebut management's response. If management's response is not complete, the Assistant Inspector General should either withhold issuance of the final report until additional information is received, or elevate significant disagreements directly to the Deputy Secretary of Defense. Audit reports should not be mediated by the OIG after issuing the final report.

Views of Responsible Official. While disagreeing with the recommendation, the Deputy Inspector General for Auditing recognizes that the current process for addressing management comments and resolving issues can be strengthened. As a result, she is taking several actions in addition to expanding the role of the Quality Assurance, Policy, and Electronic Documentation Division including briefing auditors on strengthening recommendations and responses to management comments. In addition, the Assistant Inspectors General have committed to emphasize use of discussion drafts and other means to resolve differences with clients.

Audit Response. We believe that the additional actions cited by the Deputy Inspector General for Auditing may reduce the number of disagreed responses and will encourage auditors to better rebut management's responses when necessary. However, we continue to believe that if supplemental information is being requested from management, it should be considered by the OIG before issuing the final report. We also believe that issues that can be resolved between the OIG and management without intervention by the Deputy Secretary of Defense should be

resolved prior to final report issuance. Thus, we believe our recommendation to discontinue the practice of issuing final reports with unresolved issues remains valid. However, if the OIG continues this practice, we suggest that the final resolution of issues be associated with the final report and publicly disclosed for the benefit of interested readers.

Finding 2. Report Contents

GAGAS requires that the report contain findings, conclusions, recommendations, and the objective, scope, and methodology. Deficiencies in the contents of the report can result in disagreements, misunderstandings, and unstated assumptions by the reader and damage the credibility of the audit organization. Our review identified report content deficiencies in 5 of the 10 reports we reviewed.

Findings – GAGAS requires that auditors report findings by providing credible evidence that relates to the audit objectives. Three audit reports contained elements of findings that were not supported with sufficient, competent, and relevant evidence.

- In one report, the OIG stated that documentation could not be found to support certain exports. In their response, DoD management officials maintained that the audit's conclusions and recommendations were unfounded because the OIG's audit work was based on incomplete and untimely data. The OIG's audit examined only Fiscal Year (FY) 2004 cases and, according to DoD management officials, they did not have the capability to incorporate all supporting documents and information needed until FY 2005. Since the OIG began its audit work in October 2005, the auditors could have selected a more current sample to assess the revised process.
- One audit report stated that system users did not receive required training because DoD personnel had not clearly established who was responsible for retaining Information Assurance Awareness training records and verifying completion. However, the audit documentation did not contain persuasive evidence to establish that this was the factor responsible for the condition.
- A third report stated that errors made by the contractor's employees were attributed to the lack of training, but the audit team did not establish whether the errors were made by trained or untrained contractors.

GAGAS also requires that the report recognize the positive aspects of the program reviewed since such information allows for a fairer presentation by providing an appropriate balance to the report. The OIG's policies and procedures suggest that the reports provide a balanced presentation by including the results for objectives that did not result in findings or explaining that no problems were found on an objective. When positive results are not included, the report users may question the objectivity and credibility of the report. In addition, management of the audited entity may not be aware of the positive program aspects. The inclusion of positive accomplishments may also lead to improved performance by other government organizations that read the report. In 2 of the 10 reports reviewed, however, the positive results were not included in the issued report nor was an explanation provided stating that no problems were found during the audit regarding the objectives.

Conclusions – GAGAS states that auditors should report conclusions when called for by the audit objectives and results of the audit. Two of the 10 reports we reviewed contained conclusions that were not adequately supported. For example, one report concluded that the

integrity, confidentiality, and availability of DoD operational data and Information Technology systems cannot be guaranteed. The conclusion was drawn from the evaluation of limited evidence (i.e., only five purchase requests¹ associated with four DoD organizations involving only 22 contractor employees). In the second report, the auditors concluded that errors made by contractors may have enabled foreign companies to gain unauthorized access to technology. However, the available audit evidence showed only that the contractors had not cross-referenced exports to the appropriate agreement. Since the risk of the technology being exported had not been assessed during the audit, the audit team could not establish whether inappropriate technology releases had occurred or may have occurred under the program being audited.

Recommendations – GAGAS requires that recommendations flow logically from the findings and conclusions. Two of the 10 reports presented recommendations that did not match the findings and conclusions. One report contained recommendations that were unrelated to the findings reported while both reports contained a recommendation to establish procedures that already existed. In each instance, DoD management nonconcurred with the recommendation and stated that existing procedures and agreements had already been established.

Objective, Scope, and Methodology - GAGAS instructs auditors to report the scope and methodology used to accomplish the audit's objective. As such, the audit objective needs to be communicated in the audit report in a clear, specific, and neutral manner that avoids unstated assumptions. The related audit scope should be described in depth along with the actual work conducted to complete the audit objective. This information should be reported in sufficient detail to assist knowledgeable report users in understanding the overall work performed. Adequately describing the audit's scope and methodology is important because report users need this overall perspective to fully understand the nature and extent of the audit work performed.

Our review found in 2 of the 10 audits reviewed that the report did not sufficiently identify the scope and methodology of the audit. One report did not identify the universe from which the sample was selected, and another report did not sufficiently describe the scope of the work completed to meet the audit objective.

These types of reporting deficiencies could misinform the reader and damage the credibility of the audit organization. The circumstances in each of the audits we reviewed were unique; however, OIG management is ultimately responsible for the accuracy and completeness of the reports. The Quality Assurance, Policy, and Electronic Documentation Division post-reviews a sample of reports; however, the scope of their reviews did not always include the issues we noted.

Recommendation 2: Assistant Inspectors General, Program Directors, and Project Managers should be responsible for ensuring audit tests are logical and designed to gather sufficient, relevant, and competent evidence to meet objectives and support conclusions. To provide this accountability, the Deputy Inspector General for Auditing should require the Quality Assurance, Policy, and Electronic Documentation Division to expand the scope of their reviews of final reports.

Views of Responsible Official. The Deputy Inspector General for Auditing agreed with the recommendation. The Quality Assurance, Policy, and Electronic Documentation Division has increased the number of its quality reviews with emphasis on providing auditors feedback before

¹ A separate DoD OIG report issued July 29, 2005, indicated that DoD submitted approximately 24,000 similar purchase requests to the General Services Administration in Fiscal Year 2004.

reports are final. Report writing training is also being provided to improve content and relationships among findings, conclusions, and recommendations. The OIG disagreed with two of the conditions cited. Specifically, the OIG maintains that for one report the legally mandated deadline of March 30, 2006, for final report issuance made it impractical to use FY 2005 data. For another report, the DoD OIG maintains the auditors appropriately concluded that contractor errors may have enabled foreign companies to gain unauthorized access to technology.

Audit Response. We agree that the OIG's corrective actions are adequate. We maintain our position on the two conditions to which the OIG disagrees. In the first instance, we believe that the OIG could have evaluated FY 2005 data for one report since another agency that participated in the interagency review did use FY2005 data in their analysis. In the second instance, we believe that the audit team could have provided more perspective on the effect of the issue by assessing the risk of the exported technology, particularly those that were not properly cross-referenced to export agreements. Management did not believe that the technology posed a risk. However, the OIG did not conduct tests to support or refute that claim.

Finding 3. Report Accuracy

GAGAS requires that the evidence presented be factual, findings be correctly portrayed, and audit documentation contain sufficient information to enable an experienced auditor, who has had no previous connection with the audit, to ascertain from the audit documentation the evidence that supports the auditors' significant judgments and conclusions. To help assure the credibility and reliability of audit reports, GAGAS suggests "referencing" as a quality control process in which an experienced auditor who is independent of the audit verifies that statements of fact, figures, and dates are correctly reported, and findings are adequately supported by the audit documentation. The overriding concern is that just one inaccuracy in a report could cast doubt on the reliability of an entire report and divert attention from the substance of the report. Also, report inaccuracies could damage the credibility of the issuing audit organization and reduce the overall effectiveness of its reports.

Consistent with GAGAS, the OIG's policies and procedures require the audit team to index and cross-index individual project documentation and summaries to supporting information so that a reviewer may easily locate and reference the supporting information. In addition, all draft and final reports must be indexed, reviewed and independently referenced. The OIG established the independent referencing process to help ensure the credibility and reliability of its audit reports by verifying that all the statements of fact in the report are adequately indexed to supporting evidence in the audit documentation. Per the guidance, the independent referencing process should never be a substitute for supervisory review, and audit supervisors are ultimately responsible for ensuring that audit documentation, including the reports used for referencing, are appropriately indexed and independently referenced.

In 8 of the 10 audits reviewed, we experienced problems verifying sampled statements of fact, figures, and dates contained in audit reports to the supporting documentation using the indexes provided. Most often, this occurred because the index was to a summary project document without additional, adequate cross-indexes to the supporting working papers, or the statement was not directly supported by the index provided. Some of these questioned statements were eventually resolved with additional information provided by the audit teams; however, others remained unsupported. Some of the report statements we had problems verifying were also questioned by the independent referencer; however, the referencer later signed off on the report index without any further comment made by the audit team managers or an explanation provided

by the referencer. Inaccurate and incomplete cross-indexing was also reported in the prior peer review of the DoD OIG conducted by the U.S. Department of Housing and Urban Development (HUD) OIG, on September 15, 2003.

Four of the 10 audit reports we reviewed contained incorrect statements of fact, figures, and dates. For example, one report stated that officials at four DoD organizations had not fully implemented comprehensive Information Assurance controls. However, the support contained in the audit documentation showed that no issues were identified with one of the four DoD organizations. Another report stated that the site data collection processes for three data calls generally complied with applicable internal control plans while the audit documentation showed that for one of the three data calls the auditors did not actually evaluate compliance with applicable internal control plans. A third report contained an amount that was overstated by \$1 billion and a fourth report contained three incorrect dates.

Referencers did not use sufficient care to confirm that statements in the report were supported by workpapers. Our review of five internal quality assurance review reports issued by the Quality Assurance, Policy, and Electronic Documentation Division found that referencing deficiencies were also identified in three of the five internal reviews. In one report reviewed by Quality Assurance, Policy, and Electronic Documentation reviewers, the referencer indicated that due to time constraints, he relied upon the supervisor's reviews of documentation without independently confirming that facts were supported.

Referencing can be an effective quality control process to ensure that issued audit reports meet reporting quality standards. While the Project Leader, Program Director, and Assistant Inspector General are ultimately accountable for the report and project documentation, the independent referencer should make certain that information and conclusions in OIG reports are accurate, supported, and logical. Inaccuracies in a report can divert attention from the substance of the report and damage the credibility of the audit organization.

After our fieldwork, the Deputy Inspector General for Auditing advised that the OIG has re-established its requirement for periodic refresher training on referencing and has expanded availability to junior staff responsible for indexing reports. Four sessions with a total of 44 staff received referencing training since mid-June 2006. Eight sessions are scheduled between August and November 2006. On August 10, 2006, the Deputy Inspector General for Auditing and the Principal Assistant for Auditing issued e-mails that emphasized to senior management the importance of supporting referencing training for all their staff.

Recommendation 3 – The Deputy Inspector General for Auditing should emphasize the need for supervisors to ensure that reports are properly indexed to supporting documentation to enable referencers to more readily confirm the facts and figures.

Views of Responsible Official. The OIG agreed with the recommendation. The Deputy Inspector General for Auditing plans to issue reminders to the staff regarding the need to properly index reports. In addition, the Quality Assurance, Policy, and Electronic Documentation Division will provide presentations on report referencing to Program Directors and Project Managers. Several training initiatives are also being planned.

Finding 4. Supervisory Review of Workpapers

GAGAS explains that supervision involves directing the efforts of staff assigned to the audit to ensure that the audit objectives are accomplished. Elements of supervision include providing

sufficient guidance to staff members, staying informed about significant problems encountered, reviewing the work performed, and providing effective on-the-job training. Supervisors should satisfy themselves that staff members clearly understand what work they are to do, why the work is to be conducted, and what the work is expected to accomplish. GAGAS requires auditors to document the work performed to support significant judgments and conclusions, including descriptions of transactions and records examined and evidence of supervisory reviews, before the audit report is issued. GAGAS requires that supervision of audit work should be documented. The OIG's policies and procedures require timely supervisory review of the project documentation "throughout the audit."

For 1 of the 10 audits reviewed, however, we found no evidence of supervisory review of audit workpapers by the Project Manager until after the discussion draft report was issued to DoD management. The audit survey work started for this assignment on July 1, 2005, and fieldwork ended on December 30, 2005. From a sample of electronic working papers, we determined that the documented audit work was apparently created and maintained by the auditors but, apparently, outside of the electronic file. Because these working papers were not timely placed in the electronic audit file to document the audit work performed, they were not readily available for supervisory review. The Project Manager maintained that no other electronic or hard-copy audit documentation was prepared during the course of the audit that could otherwise evidence the audit process and supervisory review. The electronic working paper file was the only available audit evidence. Untimely supervisory review of workpapers was also reported in the prior DoD OIG peer review conducted by the HUD OIG.

Supervisory review of audit documentation is an integral part of the internal quality control system and helps ensure that audit objectives are fully covered, and evidence is obtained and documented commensurate with potential findings. Also, supervisory review helps ensure that audit conclusions are valid and fully supported, and audit reports are appropriately indexed and referenced to supporting documentation. An untimely supervisory review of audit working papers increases the risk that problems with audit documentation will not be identified prior to issuance of the report.

Recommendation 4 – The Deputy Inspector General for Auditing should reemphasize both the requirement for timely supervisory review of electronic workpapers and that reviews are documented in the workpapers.

Views of Responsible Official. The OIG agreed with the recommendation. The Deputy Inspector General for Auditing will re-emphasize the requirement for timely supervisory review of workpapers and the need to document the review in the working papers. Supervisory reviews will also be emphasized through presentations, staff meetings and training. However, the Deputy Inspector General for Auditing disagreed with the criteria applied for the condition cited. Specifically, the OIG disagreed with the creation of a workpaper as the starting point for supervisory review, instead of when the preparer identifies the working paper as ready for review. Also the OIG maintains that no standards require creating documents solely in an electronic documentation file in a specific timeframe or prior to the end of fieldwork.

Audit Response. We maintain that the audit cited did not meet the OIG's requirements for supervisory review of workpapers. Regardless of the criteria, we found no evidence of supervisory involvement in the working papers until after the discussion draft was issued. Documentation of supervisory review would have been facilitated if the auditors had placed their workpapers in the electronic file as they performed their work.

Peer Review Scope and Methodology (Exhibit A)

Scope and Methodology

We tested compliance with the OIG's system of quality control to the extent we considered appropriate. These tests included a review of 10 of 126 audit reports issued during the September 30, 2005, and March 31, 2006, semiannual reporting periods. In addition, we reviewed five internal quality assurance reviews performed by the DoD OIG.

OIG Offices Reviewed

We visited the DoD IG office in Arlington, Virginia.

Audit Reports Reviewed

1. DoD Organization Information Assurance Management of Information Technology Goods and Services Acquired Through Interagency Agreements (Report Number D-2006-052, dated February 23, 2006)
2. Controls Over Exports to China (Report Number D-2006-067, dated March 30, 2006)
3. Appropriated Funds Distribution Within the Program Budget Accounting System (Report Number D-2006-064, dated March 17, 2006)
4. Internal Controls Over Compiling and Reporting Environmental Liabilities Data (Reference Number D-2006-062, dated March 15, 2006)
5. Controls Over the Export of Joint Strike Fighter Technology (Report Number D-2006-044, dated January 11, 2006)
6. Independent Examination of Valuation and Completeness of U.S. Army Corps of Engineers Buildings and Other Structures (Report Number D-2006-009, dated October 28, 2005)
7. DoD Purchases Made Through the General Services Administration (Report Number D-2005-096, dated July 29, 2005)
8. Procurement Procedures Used for F-16 Mission Training Center Simulator Services (Report Number D-2006-065, dated March 24, 2006)
9. Management of Emergency-Essential Positions in the U.S. European Command (Report Number D-2006-070, dated March 31, 2006)
10. Defense Human Resource Activity Data Call Submissions and Internal Control Processes for Base Realignment and Closure 2005 (Report Number D-2005-076, dated May 31, 2005)

General Comments (Exhibit B)

We observed positive audit practices in the OIG's audit organization to help ensure audits were performed in accordance with professional standards. In particular, OIG policies and procedures require that Project Leaders complete a "Project Quality Control Checklist" throughout the course of an audit as a reminder of the requirements for project planning, supervision, project documentation, and report quality control. In addition, the Quality Assurance, Policy, and Electronic Documentation Division implemented several initiatives based on the identification of trends during the quality assurance reviews of audit reports to increase confidence that the audit work is objective and credible.

Management Response (Exhibit C)



INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
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OCT 24 2006

The Honorable J. Russell George
Inspector General
Treasury Inspector General for Tax Administration
1125 – 15th Street, N.W. (IG:IG, 700A)
Washington, DC 20005

Dear Mr. George:


This is in reply to the letter of September 22, 2006, which provided the draft report from your external peer review of the Office of Inspector General, Department of Defense (OIG DoD) audit operations.

We appreciate the in-depth review that your staff performed on our quality control function. We appreciate the quality and the professionalism of the peer review team and their assistance to our organization. Their suggestions will further enhance our maintaining full compliance with generally accepted government auditing standards.

We are pleased that you determined that our quality control system was sufficiently designed and complied with to support an unmodified opinion. We will address the conditions that you identified as needing attention; however, we do have points of disagreement with your conclusions and in some cases do not agree with your recommendation. Where possible, we have identified positive alternatives to achieving the intent of your recommendations. We also note in this letter where corrective actions have already been taken or where corrective actions are in process. The Office of the Deputy Inspector General for Auditing has held and will continue to hold meetings with audit staff on the issues identified, including executive meetings with our Senior Executive Service and GS-15 Audit Program Directors.

If your staff has any questions on our comments to the official draft report, please have them contact Mr. Keith West, Principal Assistant Inspector General for Auditing, at (703) 604-8905.

Sincerely,


Thomas F. Gimble
Acting

Enclosure: Comments to TIGTA Findings and Recommendations on the "Draft Report on the External Quality Control Review of the Department of Defense Inspector General Audit Organization"

Management Response (Exhibit C)

Finding 1. Reporting Views of Responsible Officials

Our due process procedure used to resolve reports and recommendations is an effective and credible method for addressing management comments on audit reports. Our process satisfies government auditing standards and is consistent with the Inspector General Act of 1978, as amended. The process also satisfies the requirements of OMB Circular A-50, "Audit Followup," September 29, 1982; and DoD Directive 7650.3, "Followup on General Accounting Office (GAO), DoD Inspector General (DoD IG), and Internal Audit Reports," June 3, 2004. None of the aforementioned criteria require agreement before final report issue.

GAGAS 8.31 requires that auditors report the views of responsible officials. GAGAS 8.33 states that comments should be fairly and objectively evaluated and recognized, as appropriate, in the final report and that comments should be noted but should not be accepted as justification for dropping a finding or a related recommendation. GAGAS 8.34 goes further to state auditors' disagreement should be stated in a fair and objective manner and auditors should modify their report as necessary if they find the comments to be valid.

The Inspector General Act, OMB Circular, and DoD Directive all presuppose that there may be disagreements after issue of the final report. Section 5 of the Inspector General Act requires the Inspector General to identify in their semiannual report to Congress each significant recommendation described in previous semiannual reports on which corrective action has not been completed. Therefore, visibility is provided over recommendations that are over 6 months old. OMB Circular A-50 states at paragraph 8.a. (2) that resolution of audit recommendations shall be made within a maximum of six months after issuance of a final report and at paragraph 8.a.(8) that semi-annual reports be provided to the agency head on the status of all unresolved audit reports over six months old, the reasons therefore, and a timetable for their resolution. In accordance with DoD Directive 7650.3, we attempt to resolve all disagreements at a lower management level including senior officials and Heads of DoD Components. Therefore, we would only elevate to the Deputy Secretary of Defense as a last resort on rare occasions for extremely significant disagreements.

We believe that the standards and other mandates provide a strong basis for our process as it is currently configured. Our official draft reports clearly notify

Management Response (Exhibit C)

management of procedures and regulatory guidance associated with responding to our reports in every draft report transmittal memorandum. An example of the transmittal language used follows:

We request that management provide comments that conform to the requirements of DoD Directive 7650.3. If possible, please send management comments in electronic format (Adobe Acrobat file only) to Audacm@dodig.mil. Copies of the management comments must contain the actual signature of the authorizing official. We cannot accept the / Signed / symbol in place of the actual signature. If you arrange to send classified comments electronically, they must be sent over the SECRET Internet Protocol Router Network (SIPRNET).

For us to consider management comments in preparing the final report, we should receive them by August 25, 2006. We normally include copies of the comments in the final report. Matters considered by management to be exempt from public release should be clearly marked for Inspector General consideration.

We provide a date that we expect comments and generally extend that date if management requests it so management has a reasonable opportunity to provide its views; however, we do not believe multiple extensions are advisable as the audit client could use that method to block report publication for congressional and public use or timely deliver of results because of expanding issues. When management comments are received, we consider and discuss the comments in the body of the final report and include copies of the full text of their comments in an appendix to the final report. We disclose disagreements and refute comments when necessary. The final published report may include requests for additional comments and descriptions of changes made as a result of comments to the official draft report. Also, a report reader can contact one of several offices or personnel provided by name and phone number in the report if the report reader is interested in the final resolution to a published report that requests additional comments.

Although we published final reports that included unresolved recommendations and requests for additional management comments, we believe the peer review report as worded does not provide proper perspective on this practice. The total number of recommendations in the 31 reports exceeded 300 for which we requested additional comments from management on 98 (29 percent) of the recommendations. For some recommendations with which management concurred and identified actions taken or planned, we requested additional comments because management did not provide specific actions or completion dates of the actions in their initial response. We proceeded and published the final reports with copies of the full text of management's initial comments because those comments showed management's views on the reported findings, conclusions, and recommendations, as well as management's planned corrective actions as required by GAGAS paragraphs 8.31-8.32.

Management Response (Exhibit C)

TIGTA Recommendation 1. *The Deputy Inspector General for Auditing should discontinue the routine practice of issuing final reports without resolving disagreements. If management provides additional information in its response, the Assistant Inspector General should evaluate it before issuing the final report and either appropriately revise the report or adequately rebut management's response. If management's response is not complete, the Assistant Inspector General should either withhold issuance of the final report until additional information is received, or elevate significant disagreements directly to the Deputy Secretary of Defense. Audit reports should not be mediated by the OIG after issuing the final report.*

DoD Response to Recommendation 1. Strongly disagree with the recommendation. We are concerned that implementing the proposed recommendation as written could have damaging results to the IG DoD mission. Management would be in a position to hold our reports captive to the detriment of our delivering timely information to Congress and the public. We do not agree that waiting for final resolution before publishing a report, discontinuing mediation to resolve issues, or raising significant disagreements (and who would define significant?) directly to the Deputy Secretary of Defense are viable options or in the best interests of the Department. Withholding issue of final reports or discontinuing mediation is contrary to OMB and DoD policy. As previously discussed, our policies and procedures are consistent with GAGAS; however, we recognize that our process for addressing management comments and resolving issues can be strengthened and we are taking the following actions:

- The Deputy Inspector General for Auditing expanded the Quality Assurance, Policy, and Electronic Documentation (QAPED) Division responsibilities to include review and analysis of final reports. By the end of the first quarter FY 2007, QAPED will present to senior management the results of that analysis of whether management comments are fairly recognized, disagreements by management are sufficiently addressed, and the audit report is modified when appropriate. Senior management will then set the course for and timing of continued reviews based on the trend analysis from QAPED.
- The Principal Assistant Inspector General for Auditing has added a question to our customer survey to gauge management concern on fair recognition of their comments.
- On September 20, 2006, representatives from the Inspector General policy functions briefed 60 ODIG senior auditors/team leaders about the external quality control review results and how Audit could improve its processes. One focus area was strengthening recommendations and responses to

Management Response (Exhibit C)

management comments. The briefing will be given throughout Audit by April 20, 2007.

- QAPED prepared a summary report, dated September 29, 2006, of FY 2006 activity that included a discussion of the external quality control review results. One section of the report discussed resolving management disagreements and refuting management comments. The report is available on the intranet site for the Office of the Deputy Inspector General for Auditing (ODIG-Audit) and the staff was notified by email of its availability.
- At the October 10, 2006, weekly senior staff meeting, the Assistant Inspectors General committed to emphasize use of discussion drafts and other early communication as a means of resolving differences with clients and gathering evidence of due process with the client. In addition to the personal emphasis by the Assistant Inspectors General, the topic appeared in the meeting minutes that are disseminated to all of Audit by email.
- QAPED help calls and coaching have recently experienced an increase in calls about handling management comments. The QAPED staff used the discussion draft and draft peer review reports and comments to assist teams with the management comments.

Finding 2. Report Contents

The preponderance of statements in the reports reviewed by the peer review team were supported by sufficient, competent, and relevant evidence that provided a reasonable basis for our auditor's findings and conclusions. The review results indicated isolated report statements lacked sufficient support within the findings of three reports; however, the draft report as worded gives the impression that evidence did not support entire elements (condition, cause, or effect) of the findings.

For one report, management's comment reflected disagreement on the use of FY 2004 data, and the peer review results emphasized that the OIG audit fieldwork started in October 2005 and therefore represented that the OIG auditors could have selected FY 2005 data. We disagree. The OIG auditors used their professional judgment to select the most appropriate data for their audit work. The planning for this audit occurred well before the end of FY 2005 (over 3 months), and at that time, FY 2004 data represented the most recent year of complete data. In addition, the legally mandated deadline of March 30, 2006, for final report issue did not make use of FY 2005 data practical. Management comments to the draft

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audit report represent their disagreement with the period selected for review. However, management did not provide persuasive evidence and documentation to support their comments that use of FY 2004 data was inappropriate, incomplete, or untimely. The GAGAS standard on Professional Judgment at GAGAS paragraph 3.37 states that “[a]uditors neither assume that management is dishonest nor assume unquestioned honesty. In exercising professional skepticism, auditors should not be satisfied with less than persuasive evidence because of a belief that management is honest.”

For another report where concerns were expressed on the adequacy of evidence, we disagree. We maintain that the OIG auditors’ appropriately concluded that contractor errors may have enabled foreign companies to gain unauthorized access to technology. Evidence showed that contractors had not linked exports to the appropriate agreement. This evidence is important because agreements in the case of exports – particularly of military equipment and information technology – specify whether the contractor should certify the release of controlled, unclassified technology to foreign companies. Additionally, our report not only said that the contractors made errors in certifying exports using the agreement, the report went on to say that by doing so the contractors potentially disclosed export-controlled information to foreign companies.

We maintain that our auditors did identify the risks associated with the unauthorized or inadvertent disclosure of the subject technology. GAGAS 7.64 allows auditors to identify the potential consequences of a condition that varies from criteria. DoD Directive 5200.39 identifies the potential consequences associated with the unauthorized or inadvertent disclosure of the subject technology. According to DoD Directive 5200.39, it is DoD policy to provide protection for the subject technology because compromise of that technology would: (i) allow companies to counter or reproduce the technology, (ii) reduce the effectiveness of the program technology, (iii) significantly alter program direction, or (iv) degrade combat effectiveness. Our auditors evaluated compliance with the directive and identified the above as the potential consequences or risks associated with the contractor errors.

TIGTA Recommendation 2. *Assistant Inspectors General, Program Directors, and Project Managers should be responsible for ensuring audit tests are logical and designed to gather sufficient, relevant, and competent evidence to meet objectives and support conclusions. To provide this accountability, the Deputy Inspector General for Auditing should require the Quality Assurance, Policy, and Electronic Documentation Division to expand the scope of their reviews of final reports.*

DoD Response to Recommendation 2. We agree that the Assistant Inspectors General, Program Directors, and Project Managers should be responsible for

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ensuring audit tests are logical and designed to gather sufficient, relevant, and competent evidence to meet objectives and support conclusions. This is documented in the ODIG-Audit Handbook, Chapter 1, Section 4 as part of the quality control system that "Supervisors and team leaders should use the Project Quality Control Checklists throughout the course of audits as a reminder of requirements for project planning, supervision, and project documentation for performance, financial statement, attestation, and oversight of Independent Public Accountants. These checklists provide the technical review to assess compliance with GAGAS and the quality of the report." Additionally, in implementing the National Security Personnel System, we have created performance job objectives for all audit staff that emphasize compliance with GAGAS.

QAPED is reviewing draft reports and final reports to identify concerns or trends and to identify examples of report content for future training to enhance audit product quality. In an email to the Audit Staff dated June 12, 2006, the Principal Assistant Inspector General for Auditing stated:

In response to comments made during the ongoing external peer review, we plan to have the Quality Assurance, Policy, and Electronic Documentation Division (QAPED) review final reports with particular regard to the Audit Response to Management Comments section as well as the summarization of management comments. Previously, in March 2006 we had established a Quality Assurance Review (QAR) process in which QAPED reviews all issued draft reports for consistency with GAGAS reporting. Effective immediately, Program Directors should ensure that QAPED is on distribution for final reports. QAPED will review issued final reports and provide the Audit Front Office with concerns or trends based on the reviews. If the post-issue review indicates trends in reporting on management comments that could be better managed with a pre-issue review, we will modify the procedures accordingly.

Since inception of these quality assurance reviews, QAPED has reviewed 49 draft and 30 final reports and will report the initial results of these reviews to the Assistant Inspectors General in January 2007 and annually thereafter in a report with recommendations for improving operations.

In addition to reviewing reports at various junctures, the Quality Assurance branch of the QAPED Division increased the number of staff and that staff conducted and reported on 28 percent more reviews than in FY 2005. The Quality Assurance branch has increased the ratio of interim reviews to final project reviews to provide auditors feedback before reports are final and the documentation files are not accessible for changes. The branch has also increased the number of products it issues and has included trend reports in its FY 2007 plan.

In FY 2007 we plan to expand the prototype training that the edit staff provided to the financial audit staff and readiness and operational support staff in FY 2006 as a

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stand-down day on report writing. Development of training is described in the report, "Quality Assurance: Efforts, Issues, and Initiatives for the Post Peer Review Organization," September 29, 2006. The objectives of the stand-down day would be to improve report clarity; promote straightforward and proper grammar; and improve content and relationships among finding, conclusions, and recommendations. The proposal is to provide the training as a cooperative effort between the OIG editors and Quality Assurance personnel.

Finding 3. Report Accuracy

The Deputy Inspector General for Auditing has and will continue to re-emphasize the importance of indexing and cross-indexing audit documentation. The DoD ODIG-Audit would like to put into context the overstatement that TIGTA referred to in draft Finding 3. The DoD audit report erroneously attributed a total amount of funding transfers to the General Services Administration instead of the 85 percent of the amount that belonged to the DoD which resulted in the overstatement of DoD funding of purchases through the General Services Administration.

TIGTA Recommendation 3. *The Deputy Inspector General for Auditing should emphasize the need for supervisors to ensure that reports are properly indexed to supporting documentation to enable referencers to more readily confirm the facts and figures.*

DoD Response to Recommendation 3. Agree with the recommendation. The Deputy Inspector General for Auditing will continue to emphasize through memoranda and recurring training the need for supervisors to ensure their staff properly index reports to supporting documentation to facilitate easier independent reviews of report facts, figures, and statements. By November 15, 2006, the Deputy Inspector General for Auditing will prepare and disseminate a memorandum to all audit staff by email, which will be posted on the Intranet for future reference. Also, the Deputy Inspector General for Auditing has tasked QAPED and her audit and support staff development group with providing presentations on proper report referencing and adequate referencing review. Audit Policy and Oversight (APO) staff and QAPED provided an initial presentation on September 20, 2006, on planning, quality, and reporting including emphasizing the indexing and independent reference review problems from the quality control review. APO and QAPED will provide a half-day presentation to GS-15 Program Directors and GS-14 Project Managers on December 7, 2006.

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The Office of the Deputy Inspector General for Auditing has the following training initiatives for FY 2007:

- Expand the current 5-hour training for independent reference reviews to include working paper preparation along with indexing the draft/final report to support documentation. The expanded class would be 2 ½ days and use the objectives from the current “Independent Reference Review” training and an earlier offering, “Working Papers the Right Way.” This training will be offered to all auditors by Division, three teams at a time. One goal is to encourage consistency and continuity in applying the information and procedures presented. After the “first exposure” training is completed, the combined training will be offered annually or more frequently if needed.
- After all auditors have received the combined referencing and working papers training; the classes should be separated and the independent reference review training developed further into two courses, one for performance audits and one for audit teams providing oversight of audits conducted by independent public accountants. The independent reference review classes will be offered quarterly for new hires from other agencies and new employees. Experienced senior auditors are encouraged to take this training which will be offered throughout the year as a refresher every 2 to 3 years.
- The working paper preparation and indexing portion that forms another class will be offered quarterly for new audit employees. This will also be offered to audit staff annually as a refresher.

Finding 4. Supervisory Review of Workpapers

ODIG-Audit disagrees with the peer review team conclusion regarding the one audit that had no electronic history of supervisory until after issue of the discussion draft. GAGAS 7.47 states that the nature and extent of the review of audit work may vary depending on, for example, the experience of the staff. We disagree with the criteria applied to Report No. D2006-067--that was creation of a working paper as the starting point for supervisory review instead of when the preparer identifies the working paper as ready for review. Also, no standards require creating documents solely in TeamMate electronic documentation files or recording documents in TeamMate in a specific timeframe or prior to fieldwork end, as described by the peer review team. For this audit, the Project Manager spent time with new entry-level staff, showing them how to prepare audit documentation. It made more sense to work off-line to address data gathering, analysis, and documentation errors expected with less experienced staff than to

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prematurely place the working papers in the official files after which excessive explanation and revision would have been required. Based on our Audit Handbook requirements, working papers prepared by project managers or program directors do not need to have higher level review because they are senior staff considered to be knowledgeable and experienced persons who ordinarily review the work of others. Of the 12 working papers that the peer review team chose to review, 6 were prepared by the project manager. Therefore, no further review was required by a higher level supervisor, per Audit Handbook requirements which are consistent with GAGAS 7.46 regarding experienced staff. Further, the audit team completed all working papers before issuing the final report, which is the only timing-based requirement in GAGAS. The Audit Handbook established the timeliness criteria to respond to a recommendation from a previous peer review by the Department of Housing and Urban Development. The Audit Handbook caveats the requirement with the experience of the team, the demands of the project, and the involvement of the manager.

TIGTA Recommendation 4. Deleted.

TIGTA Recommendation 5. *The Deputy Inspector General for Auditing should reemphasize both the requirement for timely supervisory review of electronic workpapers and that reviews are documented in the workpapers.*

DoD Response to Recommendation 5. Agree with the recommendation. The Deputy Inspector General for Auditing will re-emphasize the requirement for timely supervisory review of electronic and hard copy working papers and the need to document the reviews in the project working papers. The re-emphasis will be accomplished through a memorandum signed by the Deputy Inspector General for Auditing and disseminated by email and posted on the intranet site. In addition, review within a reasonable timeframe as defined by the Audit Handbook will be emphasized through presentations at off-sites, staff meetings, and Independent Reference Review training. The first presentation took place at the team leader off-site on September 20, 2006. The Deputy Inspector General for Auditing memorandum will be issued by November 15, 2006.