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*UNITED STATES
GENERAL ACCOUNTING OFFICE*

Ways The Department Of Health, Education, And Welfare Can increase Benefits From Auditing

The new Office of Inspector General in the Department of Health, Education, and Welfare would likely receive more benefits from its Audit Agency if it:

Compares information on the results of audits with the reasons for starting such audits, to find out which produced the best results.

More thoroughly evaluates auditing by non Federal auditors.

Improves its information system for management by making sure that all required information is included.

Modifies the way audits are followed up on, to better assure that audit findings reported by operating officials to be corrected actually are.

Changes existing methods of gathering information, to make implementing the new Inspector General law easier.

This report contains recommendations to the Secretary to achieve these improvements.

HRD-77-11

OCTOBER 25, 1977



UNITED STATES GENERAL ACCOUNTING OFFICE
WASHINGTON, D.C. 20548

HUMAN RESOURCES
DIVISION

B-164031(3)

The Honorable
The Secretary of Health,
Education, and Welfare

Dear Mr. Secretary:

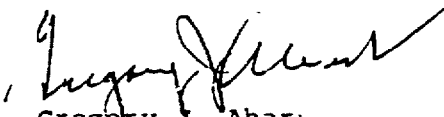
This report discusses ways to increase benefits from auditing and is based on our review of selected activities of the HEW Audit Agency--before its incorporation into the new Office of Inspector General by Public Law 94-505, October 15, 1976.

The report recognizes the Inspector General's comments of July 25, 1977, which are generally supportive of our conclusions and recommendations. We are particularly pleased that the Inspector General concurs in our assessment that the Department's corrective actions following the issuance of audit reports could be strengthened.

As you know, section 236 of the Legislative Reorganization Act of 1970 requires the head of a Federal agency to submit a written statement on actions taken on our recommendations to the House Committee on Government operations and the Senate Committee on Governmental Affairs not later than 60 days after the date of the report and to the House and Senate Committees on Appropriations with the agency's first request for appropriations made more than 60 days after the date of the report.

We are sending copies of this report to the Chairmen of the House Committee on Government Operations and its Subcommittee on Intergovernmental Relations and Human Resources, the Senate Committee on Governmental Affairs, the House Committee on Appropriations, and the Senate Appropriations Subcommittee on Labor and Health, Education, and Welfare. In addition, we are sending copies to the Director, Office of Management and Budget.

Sincerely yours,


Gregory J. Ahari
Director

GENERAL ACCOUNTING OFFICE
REPORT TO THE SECRETARY OF
HEALTH, EDUCATION, AND WELFARE

WAYS THE DEPARTMENT OF
HEALTH, EDUCATION, AND
WELFARE CAN INCREASE
BENEFITS FROM AUDITING

D I G E S T

The Office of Inspector General in the Department of Health, Education, and Welfare conducts and supervises audits and investigations of HEW programs and operations to promote economy and efficiency and to prevent and detect fraud and abuse.

Two previously existing units--the HEW Audit Agency and the Department's Office of Investigations--were made components of the Office of Inspector General, established in October 1976 by Public Law 94-505.

Subject to HEW audit are:

--Federal programs and activities administered by HEW, which promote general welfare in health, education, and income security. In fiscal year 1975, administration and operation of HEW's various programs cost \$112.4 billion.

--Two hundred and ninety-two HEW programs involving about 50,000 grantees and contractors--colleges and universities, nonprofit organizations, hospitals and nursing homes, school districts, and State and local agencies. HEW also administers 24 intramural programs, 40 regulatory programs, and 13 international programs.

GAO analyzed information about 269 completed reviews made by the New York, Philadelphia, Chicago, and San Francisco regional audit offices, as well as by the Washington area and the Social Security audit offices.

Because the Audit Agency's workload has exceeded its staff, subjects for audit should be selected that will produce the best results with available resources. (See p. 8.) GAO demonstrated a method for showing whether one reason for beginning an

audit, such as a request from an operating component, produced better results than other reasons.

This method could be valuable in developing future audit plans and in selecting audits. (See pp. 10 to 12.) The Agency should also:

- More effectively monitor and evaluate audits by non-Federal auditors. (See pp. 13 to 18.)
- Make its automated information system, which was designed to help monitor the corrective actions taken or promised on audits findings, more accurate by establishing controls to guarantee that all reported findings are included. (See pp. 22 to 25.)
- Strengthen the procedures for monitoring corrective actions made after audit reports are issued. This could be done by (1) providing guidance to HEW operating officials to limit their discretion in closing audit findings as resolved and (2) establishing guidance for Audit Agency evaluation of the basis for operating components' closing audit findings. (See pp. 27 to 39.)

Audit Agency findings are often classified as resolved although information is incomplete or unverified. (See p. 41.) The need for reliable data on the status of corrective actions is particularly important because of new legal requirements. (See p. 46.)

The new Inspector General law could be implemented easier if the Audit Agency changed its method of gathering information to identify (1) whether the purpose of its audits is to review financial and compliance matters or to improve the economy and efficiency of HEW operations and (2) the relative importance of nonmonetary findings for the guidance of program officials responsible for acting on audit recommendations. (See pp. 49 to 52.)

During GAO's review, the Audit Agency and/or HEW took action to

- eliminate unnecessary risks to the auditors' independence (see pp. 12 and 13) and

--eliminate one source of imprecise reporting by establishing accounting controls over amounts to be recovered as a result of audit recommendations (see pp. 23, 24, 38, and 39.)

HEW's Inspector General generally supported GAO's conclusions and recommendations, except for concern that the additional costs of establishing controls over entries to the automated information system might not be warranted.

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C o n t e n t s

		<u>Page</u>
DIGEST		i
CHAPTER		
1	INTRODUCTION	1
	Purpose of audit	2
	Audit standards	2
	Auditing at HEW	3
	Establishment of HEW Office of Inspector General	6
2	SOME CONDITIONS MIGHT HAVE INHIBITED EFFECTIVENESS	8
	Audit resources less than workload requirements emphasizes importance of planning audits	8
	Actions taken should eliminate unnecessary risks to independence	12
	Insufficient monitoring of audits by non-Federal auditors	13
	Conclusions	18
	Recommendations	18
	HEW comments	19
3	AUDIT INFORMATION CAN BE REPORTED MORE ACCURATELY	20
	Automated audit information system	20
	Time reporting and audit control system	21
	Some reported findings were not recorded in the audit information system as required	22
	Number of times entities audited could not be identified from automated information	23
	System improvements to facilitate more precise reporting of accomplishments	23
	Conclusions	24
	Recommendations	24
	HEW comments	24

CHAPTER		<u>Page</u>
4	ACTIONS FOLLOWING ISSUANCE OF AN AUDIT REPORT COULD BE STRENGTHENED	26
	Importance of actions following issuance of an audit report	26
	Too much discretion given to HEW management officials to clear audit findings	27
	Audit Agency not responsible for evaluating bases for clearing audit findings	35
	HEW to establish accounting controls to identify amounts recovered	38
	Audit Agency usually made followup during next scheduled audit	39
	Results of postaudit reviews by the Audit Agency	41
	Conclusions	47
	Recommendations	47
	HEW comments	47
5	MODIFICATIONS OF EXISTING PROCEDURES TO FACILITATE IMPLEMENTATION OF PUBLIC LAW 94-505	49
	Identification of scope by elements of audit	49
	Information showing importance of nonmonetary findings	50
	Conclusions	52
	Recommendations	52
	HEW comments	53
6	SCOPE OF REVIEW	54
	Qualitative effort	54
	Site selection	55
	Selection of audits	55
APPENDIX		
I	Letter of July 25, 1977, from the HEW Inspector General	57

ABBREVIATIONS

AAIS	automated audit information system
DCAA	Defense Contract Audit Agency
DSSA	Division of Social Security Audits
ED	Education Division
GAO	General Accounting Office
GSA	General Services Administration
HEW	Department of Health, Education, and Welfare
OHD	Office of Human Development
OMB	Office of Management and Budget
PHS	Public Health Service
SRS	Social and Rehabilitation Service
SSA	Social Security Administration
TRACS	time reporting and audit control system
WAAO	Washington Area Audit Office

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CHAPTER 1

INTRODUCTION

The Department of Health, Education, and Welfare (HEW) administers Federal programs and activities which promote the general welfare in the fields of health, education, and income security. HEW comprises the Office of the Secretary and five principal operating components: the Public Health Service (PHS), the Office of Human Development (OHD), the Education Division (ED), the Social and Rehabilitation Service (SRS),^{1/} and the Social Security Administration (SSA).

Financial assistance is also provided by HEW to the following institutions pursuant to special legislation: American Printing House for the Blind, Gallaudet College, Howard University, and the National Technical Institute for the Deaf.

HEW is one of the largest Federal departments and has the largest budget. In fiscal year 1975, HEW's outlays for the administration and operation of its various programs totaled \$112.4 billion, classified by major category as follows:

	(millions)
PHS	\$ 5,406.0
OHD	1,623.7
ED	6,514.7
SRS	14,479.5
SSA	a/ 88,546.9
Departmental management	126.2
Special institutions	123.9
Deduction for offsetting receipts and interfund transactions	<u>-4,410.1</u>
Total	<u>\$112,410.8</u>

a/Includes payments of \$79.4 billion from the social security trust funds which SSA is responsible for administering.

^{1/}In a March 8, 1977, reorganization, the Social and Rehabilitation Service was abolished and the Health Care Financing Administration was created. This reorganization has no major effect on the content of this report.

HEW administers 292 programs involving grantees and contractors--colleges and universities, nonprofit organizations, hospitals and nursing homes, school districts, and State and local agencies. These programs involve about 50,000 grantees or contractors which are subject to audit. HEW also administers 24 intramural programs (such as, Public Health Service Hospitals, National Health Service Corps, health statistics, and National Institutes of Health in-house research), 40 regulatory programs (such as, food and drug safety and Center for Disease Control laboratory improvement), and 18 international programs (such as, the National Institutes of Health Fogarty Center and the Center for Disease Control tropical diseases and smallpox).

In addition to the headquarters offices of the operating components, there are 10 regional offices, 662 Public Health Service installations, and more than 1,300 SSA district and branch offices. The activities and operations of all of these offices, including the Office of the Secretary, are subject to review by the HEW Audit Agency.

PURPOSE OF AUDIT

The Budget and Accounting Procedures Act of 1950 (31 U.S.C. 66a) requires each Federal agency to establish and maintain management systems that provide effective control over and accountability for all funds, property, and other assets for which the agency is responsible. One of those systems is an audit organization which uniquely supplements routine management controls through its independent approach and review methods. The overall auditing objective is to help agency management attain its goal by furnishing information, analyses, appraisals, and recommendations on (1) how management responsibilities are being carried out and (2) how fully management is achieving its objectives.

AUDIT STANDARDS

In 1972 we published the "Standards for Audit of Government Organizations, Programs, Activities and Functions." The standards widened the scope of governmental auditing so that it is no longer concerned primarily with financial operations. A major concern now is whether governmental organizations are:

--Achieving the purposes for which programs are authorized and funds are made available.

--Operating economically and efficiently.

--Complying with applicable laws and regulations.

The standards were developed to apply to audits of this wider scope. In August 1974 the standards were incorporated in a revised statement, "Internal Auditing in Federal Agencies."

The General Services Administration's (GSA's) Federal Management Circular 73-2, "Audit of Federal Operations and Programs by Executive Branch Agencies," dated September 27, 1973, sets forth policies to be followed in auditing Federal operations and programs.^{1/} The circular's primary objectives are to promote improved audit practices, achieve more efficient use of manpower, improve coordination of audit efforts, and emphasize the need for early audits of new and substantially changed programs. GSA, the Office of Management and Budget (OMB), and HEW have accepted the standards as the basic criteria for the conduct of audit activities.

AUDITING AT HEW

Until 1965 HEW had 15 audit organizations. On July 1, 1965, the 15 were reorganized into 3 audit organizations: the HEW Office of Audit; the Division of Internal Audit, PHS; and the Division of Audit and Investigations, SSA.

In November 1965, responsibility for the Office of Audit was transferred to the Office of the Comptroller and the name of the organization was changed to the HEW Audit Agency.

The responsibility for the entire HEW audit function was vested in a single organization in March 1968 when the audit functions in PHS and SSA were transferred to the HEW Audit Agency in the Office of the Assistant Secretary, Comptroller. From that position the Audit Agency Director had the right of direct access to the Secretary. That organizational structure existed during our fieldwork. On October 15, 1976, the Office of Inspector General was established within HEW by Public Law 94-505, and the Audit Agency was reassigned to that Office from the Office of the Assistant Secretary, Comptroller.

^{1/}Effective Dec. 31, 1975, the financial management functions of executive branch agencies were transferred from GSA to the Office of Management and Budget.

Within HEW, the responsibility for audits of grants and other financial arrangements with third parties (external audits) and the audits of the Department's operation and performance (internal audits) has been vested in the HEW Audit Agency. The Office of Child Support Enforcement was an exception to the centralization of auditing responsibility. It was established on January 4, 1975, within SRS pursuant to Public Law 93-647, which required annual audits of State plans for the child support program.^{1/} This Office, which is responsible for seeing that the required annual audits are performed, is subject to review by the Audit Agency but operates independent of it.

The HEW organization manual states that the Audit Agency is:

" * * * responsible for the development and maintenance of a comprehensive audit program for the Department and its operating agencies."

" * * * to determine whether the Department's operations are being conducted economically and efficiently, and to provide a reasonable degree of assurance that Federal funds are being expended properly and for the purpose for which they were appropriated."

In addition, the Audit Agency has been assigned responsibility by OMB for auditing (1) direct and indirect costs charged against all Federal grants and contracts by about 98 percent of the Nation's 2,400 institutions of higher education and (2) indirect cost allocation plans and proposals prepared by about 950 State and local governments. In accordance with an agreement with the Defense Contract Audit Agency (DCAA), it also performs audits of contractors and subcontractors participating in the Department of Defense's Civilian Health and Medical Program of the Uniformed Services.

The HEW Audit Agency has a headquarters office in Washington, D.C., 10 regional audit offices, a Washington Area Audit Office (WAAO), and a Division of Social Security Audits (DSSA) in Baltimore, Maryland. It had 961 authorized positions--professional and clerical--for fiscal year 1976.

^{1/}The HEW March 1977 reorganization transferred this Office to SSA.

As of December 1975, the professional audit staff numbered 78 at its headquarters offices and 764 at WAAO and its regional audit offices.

The Audit Agency estimates that non-HEW audit organizations annually spend 2,178 staff-years--most of the costs of which do not come from Audit Agency funding--in auditing entities participating in HEW programs.

	<u>Staff-years</u>
Audits of Medicare institutional providers by intermediaries' audit staffs and public accountants	1,900
Audits of Medicare institutional providers dealing directly with SSA by public accountants	75
Student financial aid audits by university audit staffs and public accountants	80
Audits of Head Start program activities by various grantees by public accountants	73
Audits of grant and contract activity at colleges and universities and other profit and non-profit organizations by other Federal organizations	40
Audits (primarily of colleges and universities) by State and local audit organizations	<u>10</u>
• Total	<u>2,178</u>

In fiscal year 1975, the Audit Agency's obligations totaled \$20.8 million. Budget obligations for fiscal year 1976 were expected to be about \$22.9 million.

Records showed that during fiscal year 1975 the Agency issued 7,005 audit reports, using about 510 staff-years of Audit Agency time and about 203 staff-years of other audit staffs' time. The staff-years represent total time charged to each report from start of the audit to issuance of the report. The Audit Agency does not receive copies of reports generated from the 1,975 staff-years spent by other audit staffs for the Medicare program; however, selected reports are evaluated for adequacy. Reports issued by the

Audit Agency are categorized as (1) reports to HEW management and/or HEW grantees and contractors, (2) reports to other Federal agencies, and (3) reports to HEW management and/or HEW grantees and contractors on audits performed by other audit organizations for HEW. The amount of Audit Agency time for each category was:

<u>Report category</u>	<u>Number of reports issued</u>	<u>Total Audit Agency time in staff-years</u>
Prepared for HEW and/or HEW grantees and contractors by the Audit Agency	1,020	422
Prepared for other Federal agencies by the Audit Agency	2,195	84
Prepared for HEW and/or HEW grantees and contractors by other audit staffs	<u>3,790</u>	<u>a/4</u>
Total	<u>7,005</u>	<u>510</u>

a/Consists of time spent reviewing reports prepared by others.

Under cross-servicing agreements the Audit Agency is reimbursed by other Federal agencies for audits it performs for them and in turn reimburses the other Federal agencies for their work.

ESTABLISHMENT OF HEW OFFICE OF INSPECTOR GENERAL

Public Law 94-505, October 15, 1976, established an Office of Inspector General within HEW. This Office was to have no program responsibilities but was to conduct and supervise audits and investigations relating to programs and operations of the Department.

It would provide leadership and coordination and recommend practices to promote economy and efficiency and to prevent and detect fraud and abuse.

The Office is to provide a means for keeping the Secretary and the Congress fully and currently informed about problems and deficiencies in administering programs and operations and the necessity for and progress of corrective actions.

The Inspector General is under the general supervision of, and reports to, the Secretary or the Under Secretary and is not subject to supervision or control by any other officer of the Department.

Two then-existing HEW units--the HEW Audit Agency and the Office of Investigations--were made components of the Office on Inspector General. The act provided for transferring additional units or functions to the Office of Inspector General with the consent of the Inspector General, but no program operating responsibilities are to be transferred.

CHAPTER 2

SOME CONDITIONS MIGHT HAVE

INHIBITED EFFECTIVENESS

Conditions that might have inhibited Audit Agency effectiveness included inadequate staff resources for the perceived workload; unnecessary risks to independence which have been eliminated; and insufficient monitoring of audits by non-Federal auditors.

AUDIT RESOURCES LESS THAN WORKLOAD REQUIREMENTS EMPHASIZES IMPORTANCE OF PLANNING AUDITS

Historically, the Audit Agency's perceived workload has exceeded its available staff resources and, thus, the number of planned audits. In connection with its fiscal year 1977 work plans, an Audit Agency resource analysis showed a shortfall of about 1,400 staff-years. This condition makes decisions as to what audits to plan and perform and the primary thrust of such audits particularly important to achieving optimum results. In our review we applied a method to analyze audit results on the basis of the reasons for selecting audits, which we believe could be a useful tool in developing audit work plans and in selecting entities and/or subjects to audit.

Development of workload requirements

During the past several years, the Audit Agency has developed information on its workload based on the number of entities or units to be audited, the estimated average staff resources needed to audit each type of unit, and assumed "audit cycles" or frequency of audits.

For fiscal year 1977, this process was refined to give recognition to the relative complexity of auditing and the risks of not auditing the groups of entities or programs based on the desired frequency of audits. This process for 1977 substantially increased the difference between the Audit Agency's perceived workload and the available resources and audits planned as shown below.

<u>Fiscal year</u>	<u>Perceived annual workload</u>	<u>Staff-years</u>	
		<u>Planned</u>	<u>Perceived shortfall</u>
1975	1,502	860	642
1976	1,502	<u>a/875</u>	627
1977	2,404	963	1,441

a/Because audit plans were based on the 15-month period, July 1975 through September 1976, the amount was reduced to an annual basis for comparative purposes.

One reason for the increase in the perceived workload was the amount of staff needed to audit State Medicaid and public assistance programs.

Development of annual audit work plans

The Audit Agency is responsible for developing and maintaining a comprehensive audit program for HEW and its operating agencies. Its annual audit work plan was based primarily on (1) suggestions for audit solicited from departmental and operating component officials at both the headquarters and regional levels, (2) matters of interest to the HEW Secretary, and (3) suggestions of the Audit Agency staff. Suggestions for audits from the directors of WAAO and each of the 10 regional offices were contained in plans developed for each director's area of responsibility. The proposed final plan was submitted for comments to the appropriate assistant secretaries and operating components.

Requests for audit coverage by the Secretary and other high Department officials were called mandated audits. In addition, OMB has given the Agency responsibility for Federal audits of most of the Nation's institutions of higher learning and the indirect cost allocation plans of State and local governments.

Agency officials said that, before establishing priorities and finalizing the plan, they considered

- whether the program had been in existence for 2 years or less;
- sensitive areas involving congressional or pressure group interest;

- major problems reported in previous review;
- the amount of Federal funds subject to audit; and
- the length of time since the last substantive audit coverage.

The actual audits selected and begun in a given year, however, may differ from those shown in the annual work plan because of changing priorities.

Impact of the reasons for selecting audits on audit results

We developed information for showing the audit results in conjunction with the reasons for actually selecting the audit. We calculated average dollar value of findings and compared this with the average dollar cost of auditing to obtain some indication of the effects of the Agency's basis for audit selection.

For 171 of 269 sampled audits issued in 1972, 1974, and 1975, the bases for initiating the audits were:

<u>Basis for audit</u>	<u>Number of sampled reports</u>	<u>Percent of total</u>	<u>Average dollar findings per report</u> (thousands)	<u>Average audit costs per report</u> (thousands)	<u>Average dollar findings for each dollar of audit costs</u>
Required by GSA, OMB, or other directives	14	8.2	\$ 82.8	\$11.7	\$ 7.00
Request by HEW headquarters	28	16.4	836.6	13.2	63.40
Request by HEW regional offices	17	9.9	1,635.2	11.9	137.40
Request by Audit Agency headquarters	15	8.8	986.0	14.9	66.20
Discretion of Audit Agency regional offices	29	16.9	994.8	15.9	62.60
Congressional request	1	0.6	573.0	27.0	21.20
Could not determine	55	32.2	1,140.4	19.0	60.00
Other	12	7.0	418.6	9.1	46.00
Total	<u>171</u>	<u>100.0</u>			

From a large-dollar-findings viewpoint, the \$1,635 million average dollar findings per report and the \$137 in findings per audit dollar show that regional offices were most able to detect financial weaknesses. While that viewpoint may not be conclusive, it should be considered relevant to the extent that accomplishments were primarily reported by the Audit Agency in terms of dollars questioned. Moreover, such information might be helpful in explaining changes over the years in the basis for selecting audits for the sampled issued reports as shown below.

<u>Basis for audit</u>	<u>Number of sampled reports issued in FY 1972</u>	<u>Percent of total</u>	<u>Number of sampled reports issued in FY 1974</u>	<u>Percent of total</u>
Required by GSA, OMB, or other directives	9	13.4	9	9.0
Request by HEW headquarters	18	26.9	19	19.2
Request by HEW regional offices	3	4.5	10	10.1
Request by Audit Agency head- quarters	7	10.4	0	0.0
Discretion of Audit Agency regional audit offices	4	6.0	19	19.2
Congressional request	1	1.5	0	0.0
Could not determine	24	35.3	31	31.3
Other	<u>1</u>	<u>1.5</u>	<u>11</u>	<u>11.1</u>
Total	<u>67</u>	<u>100.0</u>	<u>99</u>	<u>100.0</u>

If the Audit Agency had attempted to increase the average dollar findings per audit, the increase in the percentage of audits made at the request of regional offices from 4.5 percent in fiscal year 1972 to 10.1 percent in fiscal year 1974 would have been consistent with that objective.

Although mandated audits must be satisfied, a comparison of their results with those of discretionary audits might show that mandated audits tend to be relatively less productive. Such comparison could become a basis for mandate modifications.

As discussed in the next chapter, the Audit Agency has developed an automated audit information system containing information on an audit report from the issue date until the Agency is notified of promised or actual corrective actions.

We believe that information showing the basis for selecting an audit could be integrated into this system to provide management with a view of the effects of past audit selection. Such a view could be a valuable tool in developing work plans and in actually selecting audits.

ACTIONS TAKEN SHOULD ELIMINATE
UNNECESSARY RISKS TO INDEPENDENCE

At the time of our fieldwork, various HEW officials directly responsible for administering or carrying out operations subject to audit had selection or coselection authority for filling various Audit Agency positions. The Assistant Secretary, Comptroller (responsible for directing and coordinating HEW financial management activities), had selection authority for all Audit Agency headquarters positions, and each of HEW's 10 regional directors (responsible for coordinating and supervising all HEW activities for a designated geographic area) had selection authority for field audit positions through the GS-14 level and coselection authority with the Assistant Secretary, Comptroller, for the GS-15 position of regional audit director.

Our principles, standards, and concepts for internal auditing in Federal agencies state that an internal audit organization should be independent of the officials who are directly responsible for the operations it reviews. In our view, the officials who are given selection authority (hiring and promoting) for internal audit positions should not, therefore, be also directly responsible for operations subject to audit.

HEW policy was that personnel management authority and responsibility be delegated to the lowest organizational level consistent with good management practice. Thus, in June 1974, the Assistant Secretary, Comptroller, redelegated selection authority for headquarters positions through the GS-13 level to the Director, Audit Agency. One of the 10 regional directors redelegated selection authority for positions through the GS-14 level to the regional audit director. In the other nine regions, redelegations by the regional directors ranged from no redelegation to full redelegation except for the "second in command" positions, which could be filled by the regional audit director subject to concurrence of the regional director.

We expressed serious reservations to both Audit Agency and Office of the Assistant Secretary, Comptroller, officials about organizational impairments which could affect the inde-

pendence of the Audit Agency. Subsequently, on June 8, 1976, selection authority was revised.

--The HEW Secretary would select the Director and Deputy Director.

--The Assistant Secretary, Comptroller, and the Director, Audit Agency, were delegated authority to coselect the regional audit directors.

--The Director, Audit Agency, was delegated authority to select employees for all headquarters positions except the Deputy Director.

--Each regional audit director was delegated authority to select employees for all positions in his or her respective region.

To strengthen and increase the independence of the Audit Agency, the HEW Under Secretary, on February 12, 1976, removed the Assistant Secretary, Comptroller, from all audit responsibility related to functions for which he had responsibility. All audits of the Comptroller's activities were to be reported directly to the Under Secretary by the Audit Agency.

By Public Law 94-505, the Inspector General, who is to have no program operating responsibilities, was authorized to appoint (in accordance with applicable laws and regulations governing the civil service) an Assistant Inspector General for Auditing who shall have the responsibility for supervising the functions, powers, and duties of what was referred to as the "HEW Audit Agency."

In addition, the Inspector General is authorized to select, appoint, and employ officers and employees of his Office. Because the Inspector General is to report to, and be under the general supervision of, the Secretary or Under Secretary and is not to be under the control of any other officer of the Department, we believe the act clearly intended to make the auditing function independent of the officials who are directly responsible for the operations reviewed.

INSUFFICIENT MONITORING OF AUDITS BY NON-FEDERAL AUDITORS

The Audit Agency needs to improve its monitoring of work for HEW by non-Federal auditors. Except for non-Federal audits of institutional providers, such as hospitals and nursing homes under Medicare, efforts have been generally limited

to a desk review of the reports and have provided little assurance of adequate audit effort. During our review, the Audit Agency recognized the need for more extensive evaluation and revised its procedures to require testing of work by non-Federal audit organizations, including workpaper reviews.

Magnitude of non-Federal audit effort

The Audit Agency estimated that non-Federal auditors annually spend 2,178 staff-years ^{1/} auditing recipients of various HEW funds. During fiscal year 1975 the Agency issued 3,790 reports prepared by other audit staffs, 54 percent of the reports issued. Most of these reports were prepared by non-Federal auditors and pertained to the student financial aid, Head Start, and Upward Bound programs. Audits by non-Federal auditors could increase considerably; the Audit Agency has been emphasizing the identification of additional HEW programs for audit by non-Federal auditors. For example, the Division of University and Nonprofit Audits indicated in December 1975 that it had identified about 167 other HEW programs for which audit guides could be developed for use by public accountants.

Federal management policies

Federal Management Circular 73-2 states that Federal agencies will consider whether grantees participating in administering programs have made or arranged for audits. It also stated that the scope of audit will give full recognition to the non-Federal audit effort and the reports will be used in lieu of Federal audits if (1) the reports and supporting workpapers are available for review by the Federal agencies, (2) testing by Federal agencies indicates the audits are made

^{1/}As shown on p. 5, most of this time is spent performing audits of Medicare providers by intermediaries, such as Blue Cross. However, the Audit Agency does not receive copies of these reports. Our comments describing monitoring of work performed by non-Federal auditors are not applicable to audits of Medicare providers. DSSA developed guidelines for review of work performed by these non-Federal auditors in 1967 and has revised the guidelines, as necessary, since then. Further, DSSA placed special emphasis on these reviews by reviewing the provider audit function at 13 and 22 intermediaries, respectively, during fiscal years 1974 and 1975. We did not attempt to evaluate the quality of these efforts.

in accordance with generally accepted audit standards, including those issued by the Comptroller General, and (3) the audits otherwise meet the requirements of the Federal agencies.

Audit and evaluation responsibilities

The HEW organization manual stated that the Audit Agency was responsible for evaluating the adequacy of audits of HEW-supported activities by organizations outside of HEW.

Grantees that received funds under HEW's student financial aid programs are encouraged, but not required, to arrange audits of their activities by public accountants or State and local government auditors in lieu of Federal audits. Grantees that received funds under HEW's Head Start and Upward Bound programs are required by legislation or regulations to obtain annual audits by public accountants or State and local government auditors. The Audit Agency, with assistance from the American Institute of Certified Public Accountants, has prepared guides for these audits. Regional audit offices furnished these guides to grantees and non-Federal auditors.

In April 1973 the Audit Agency issued procedures to its regional offices for reviewing reports prepared by non-Federal auditors on HEW's student financial aid programs. The procedures stated that, on occasion, the regional audit office may find it necessary to review the workpapers of the non-Federal auditor to satisfy itself as to the adequacy of the work performed except for Medicare. However, it had no uniform procedures for reviewing reports prepared by non-Federal auditors on other HEW programs until March 1976.

Monitoring efforts

Audit reports prepared by non-Federal auditors were submitted by either the HEW grantee or non-Federal auditor to the appropriate HEW regional audit director, who was responsible for evaluating and accepting or rejecting the reports. Accepted reports were reissued to the grantee involved and distributed to the HEW operating component responsible for following up on the reported deficiencies and recommendations.

In fiscal years 1974 and 1975, the 4 regional audit offices we reviewed reissued about 3,700 of these audit reports. During fiscal year 1975, these offices averaged about 4 staff-hours evaluating and processing each report before its reissuance.

Representatives from the four offices in our review advised us that monitoring work by non-Federal auditors was of low priority and that, therefore, little staff time was allocated for this function. They said that, because of the volume of non-Federal reports received each year, evaluations were limited to (1) desk reviews on such matters as adequacy of format or data to support conclusions, (2) reasonableness of recommendations, (3) indications that audit guides were followed, and (4) opinions on compliance with HEW regulations or with the information in financial statements.

During fiscal years 1974 and 1975, none of the four offices reviewed the workpapers prepared by non-Federal auditors. Most believed that such reviews should be made, however. For example, one assistant regional audit director told us that, without reviewing the auditors' workpapers, it was not possible to ascertain whether prescribed audit steps were followed or to evaluate the quality of the work. The regional audit director at another office told us that a review of the auditors' workpapers would be beneficial in evaluating the quality of audits.

None of the four offices compiled data on the number of reports received from each non-Federal auditor (e.g., each public accounting firm) or the cost of each audit. We believe this information would help identify those non-Federal auditors that do quality work at the lowest cost. Only one of the four offices--San Francisco--compiled data on the number of reports it rejected.

The San Francisco office rejected 21 of 210 reports prepared by non-Federal auditors, which it reviewed in fiscal year 1974. Principal reasons for rejection were that the reports did not (1) state what audit guides were used, (2) contain a statement of the grantee's compliance with HEW regulations, or (3) include information showing that costs claimed by the grantee were reconciled to its financial records.

Of the 21 rejected reports, 11 were reissued after revision. The San Francisco office staff did not know the status of the remaining 10 reports because it had no procedures to follow up on rejected reports. In March 1976, the regional audit director said the San Francisco office was initiating procedures to follow up on rejected reports.

Personnel responsible for reviewing reports in 2 other offices estimated they rejected no more than 12 reports annually. These offices issued 971 reports prepared by non-Federal auditors in fiscal year 1975.

Need for better evaluation

As a special project, the Audit Agency tried to ascertain whether improvements were needed in the audit guide for the Head Start program and to evaluate the quality of work by a selected number of public accountants. Its June 4, 1976, report described these needs: (1) an improved audit guide, (2) periodic reviews of workpapers by the Audit Agency (as evidenced by the fact that most of the public accountants reviewed expressed opinions on grantees' compliance with program regulations in their reports that were unsupportable), (3) letters of engagements between grantees and their public accountants identifying the scope of audits, and (4) training of the public accountants who perform audits of the Head Start program.

We have previously reported on the need for better monitoring the work of non-Federal auditors for various Federal agencies. Our April 1973 report to the Congress concerning the Office of Economic Opportunity ^{1/} noted that the inadequacies in public accountants' audits stemmed partly from an ineffective monitoring system by the Office of Economic Opportunity's audit organization. We reported that, for the most part, the organization was making desk reviews of the reports and was not systematically testing the adequacy of the public accountants' work. More recently, our August 25, 1976, report to the Congress, "Using Independent Public Accountants to Audit Public Housing Agencies - An Assessment," concerning the Department of Housing and Urban Development mentioned that, while the public accountants included in the review satisfactorily performed financial opinion work, none of them adequately reviewed all compliance areas called for in their contracts. These deficiencies often were not disclosed by Department monitoring, which included reviewing the public accountants' workpapers.

Two HEW officials responsible for acting on findings and recommendations in reports prepared by public accountants and issued by the Audit Agency told us that many of the reports were not clear and concise and many did not cite adequate data to support conclusions.

We told the Audit Agency Director of our concern about how well the regional audit staff satisfied both the HEW and GSA (now OMB administered) requirements. The Director

^{1/}The agency was renamed the Community Service Administration by Public Law 93-644, Jan. 4, 1975.

said he was also concerned about what kind of jobs the non-Federal auditors were doing, and in March 1976 he issued revised review procedures which required the regional audit offices to test, on a sample basis, non-Federal audit organizations' work--including reviewing the workpapers.

Since Public Law 94-505 gives the Inspector General specific authority to approve or disapprove the use of outside auditors or to take other appropriate steps to insure the competence and independence of such auditors, additional steps may be taken to monitor non-Federal auditing.

CONCLUSIONS

To a large extent, many of the factors which may have inhibited the Audit Agency's effectiveness were recognized and corrective action initiated during our review; however, on the basis of a new calculation of the workload for fiscal year 1977, the gap between the Audit Agency's perceived workload (predicated on some rational basis for measuring that workload) and its staff resources grew. We believe that this condition makes the planning and selection of which audits to perform particularly important to the fulfillment of the Audit Agency's mission.

Although the Audit Agency considers various sources and factors in planning its audits, we believe that quantifiable information on prior reasons for selecting audits could be an additional factor in planning and selecting audits.

Although the Audit Agency began in March 1976 to monitor the work of non-Federal auditors, we did not attempt to evaluate the effectiveness of monitoring activities of the non-Federal Medicare audits. The enactment of Public Law 94-505, gives the Inspector General authority to approve or disapprove the use of outside auditors and to assure their compliance. We believe that it is important that such monitoring should be designed to develop information on those non-Federal auditors doing quality work at the lowest cost, as well as those not meeting Audit Agency standards.

RECOMMENDATIONS

We recommend that the Secretary of HEW direct the Inspector General to consider:

- Modifying the automated audit information system to include the basis for selecting audits in order to compare these bases with audit results to facilitate future planning.

--Strengthening the monitoring of audits by non-Federal auditors with emphasis on developing information to facilitate the identification of those non-Federal auditors doing quality work at the lowest cost.

HEW COMMENTS

In the Department's comments (see app. I), the HEW Inspector General said that, with respect to modifying AAIS to include information on the basis for selecting audits, such a modification would be considered unless such information could be obtained manually with less effort. As to strengthened monitoring of non-Federal auditors, HEW agreed that this function could be further emphasized and outlined several actions to accomplish this.

In this connection, we are making a Government-wide review (including HEW) of the use of public accountants by grantees to audit federally assisted programs. We expect that additional information to deal with the problems associated with monitoring the quality of work performed by non-Federal auditors will be forthcoming.

CHAPTER 3

AUDIT INFORMATION CAN BE

REPORTED MORE ACCURATELY

The Audit Agency has two automated information systems. To the best of our knowledge, only the HEW Audit Agency and one other executive agency audit group have implemented automated systems to facilitate the planning and management of audits.

The automated audit information system (AAIS) contains information concerning an audit report from its issue date until notification of actual or promised corrective actions is received. The time reporting and audit control system (TRACS) contains information on the progress of an audit from the time an audit starts until an audit report is issued. This chapter contains a brief description of these information systems and identifies areas for improving

- the required recording of findings in the audit information system;
- the ability to identify the number of times individual entities have been audited using automated information; and
- the accuracy of reported accomplishments because actual and promised recovery amounts have the same identifier.

AUTOMATED AUDIT INFORMATION SYSTEM

This system, established July 1, 1968, is designed to provide current, accurate, and readily accessible information on workload, reports issued, findings, and management actions taken to correct reported deficiencies by having

- a centralized control over the number and types of reports issued within the Audit Agency and
- a basis for statistical analysis of workload accomplishments.

The Division of Audit Coordination is responsible for implementing and monitoring the system. Data, however, is entered at the regional office. The region issuing each report prepares code sheets showing information about

--the process (e.g. type of audit, program audited, costs audited, advanced audit techniques used) and

--the audit report content (e.g. grantee audited, finding type and amounts).

From the AAIS information, 15 reports are scheduled on a routine basis, either monthly or quarterly, or as requested. The reports can be used by Audit Agency managers for

--measuring progress against production goals,

--identifying potential strengths and weaknesses in audits on the basis of past performance, and

--planning future audit emphasis.

Stewardship Data Bases (printed reports) are produced from this information system and each consists of two parts. One part is a detailed listing of all audit reports with open findings and all audit reports upon which action was taken during the past fiscal quarter. The other part, cross-referenced to the first part, is a listing of all audit reports that have not been cleared and the length of time since the audit report was issued. Each part is prepared in two formats, by operating agency and by region, for a total of four Stewardship Data Bases. These reports, showing the status of audit findings and providing a basis for the annual audit followup plan, are distributed to each Audit Agency division and to each of HEW's operating components.

We discussed the use of AAIS with Audit Agency officials in headquarters and regional audit offices. Of the 15 reports, only the Stewardship Data Bases, a monthly schedule of reports issued, and a monthly production report were being produced and distributed on a regular basis. Regular production of other reports was halted because the Division of Audit Coordination found that (1) regions were not using the data, (2) special request reports were more meaningful to regional and headquarters managers, and (3) the cost of producing the other reports regularly was high.

TIME REPORTING AND AUDIT CONTROL SYSTEM

The Audit Agency implemented a time reporting and audit control system in July 1975 to enable both headquarters and the regional audit directors to evaluate progress being made

in carrying out the annual work plan. This system was to provide Audit Agency management with the means for (1) controlling the number of audits in process, (2) insuring timeliness in the issuance of audit reports, (3) controlling actual with budgeted time, (4) accumulating statistics, and (5) improving administrative reporting capabilities.

SOME REPORTED FINDINGS WERE NOT RECORDED
IN THE AUDIT INFORMATION SYSTEM AS REQUIRED

We compared GAO-extracted and Audit Agency-reported data concerning the types of findings, the number of each type, and the associated dollar value for reports issued by regional audit offices. We excluded information from reports which were essentially byproducts of the major effort (spin-off reports), overhead audit reports, and reports to other Federal agencies because information about those findings was not entered in the audit information system.

Seventeen percent of the value of findings in the reports was not recorded in AAIS for one or more of the following reasons.

--The Audit Agency procedures manual requires that information concerning all findings in reports (except for reports to other Federal agencies and indirect cost rate audits) will be entered using the standard finding codes provided by the Division of Audit Coordination. If the reported finding does not fit a standard code, a request for a standard code must be sent to that division and a code will be created. In our sample, we found instances when (1) a regional auditor did not code a finding because a standard code did not exist, nor did he request that a standard code be created and (2) a regional auditor inadvertently missed a reported finding when manually coding the findings from the issued reports.

--All coded information concerning a report should be transferred to the automated system. We found, however, that not all coded findings and their associated amounts were being processed. The computer was instructed to accept only the first occurrence of a standard finding code; any additional occurrences of the same code associated with the same audit report were not accepted. For example, a report had two findings classified as overstated claims. They had the standard code of 0249 and associated findings

amounted to \$7,000 and \$59,000, respectively. When the data was processed, the \$7,000 finding was processed and the \$59,000 finding was ignored. The relevant stewardship report showed only the \$7,000 finding.

These errors occurred in 11 or about 4 percent of the 269 sampled reports but 17 percent of the number of reports with monetary findings.

NUMBER OF TIMES ENTITIES AUDITED
COULD NOT BE IDENTIFIED FROM
AUTOMATED INFORMATION

The Audit Agency's procedures manual states that reports produced by the audit information system are to be used in planning future audit emphasis. To identify the frequency with which an entity or group of entities were audited over a 5-year period, we randomly selected entities and searched the data contained in the system for the number of times they were audited and the associated report dates. We could not automatically count the number of times selected entities were audited because the entity identifiers in the information system varied among audits. For example, information concerning audits of the University of Maryland sometimes identified that entity as "Univ. of Maryland" and sometimes as the "Univ. of Md." Therefore, to obtain automatically a complete count of the number of times that the University of Maryland was audited, information would have to be retrieved using each identification.

While information on a single entity could be obtained manually, it was our intention to ascertain the audit cycle (frequency of audit) for the 2,000 universities for which the Audit Agency had responsibility. This information could then be compared with the Audit Agency's derived workload criteria of auditing the universities once every 3 years. To facilitate such a comparison of Audit Agency goal and accomplishments, a standard identifier could be established for each entity audited and then the number of times that an entity was audited could be provided in a specially designed computer-generated report.

SYSTEM IMPROVEMENTS TO FACILITATE
MORE PRECISE REPORTING OF ACCOMPLISHMENTS

As discussed in more detail beginning on page 38, the Audit Agency's accomplishments in terms of amounts recovered

were sometimes overstated to HEW management and, in turn, to the Congress. One reason for this was that the audit information system allowed the inclusion of promised as well as actual recovery amounts--on an audit clearance document. In addition, under actions reported in the stewardship reports, the symbol "R" was used to identify either a recovery or other positive clearing action. To eliminate one source of imprecise reporting, reported recovery amounts should have been more precisely identified. In March 1977, HEW initiated changes in its accounting procedures designed to establish accounts receivable when recommendations for recoveries were accepted by the responsible operating officials and for reducing the receivables when amounts were collected or offset.

CONCLUSIONS

Although the HEW Audit Agency has made progress in establishing automated systems to facilitate the management of its audits and the disposition of its findings, we identified three specific areas where the information should be accumulated and reported more accurately. HEW has initiated action to eliminate one source of imprecise information.

RECOMMENDATIONS

We recommend that the Secretary of HEW direct the Inspector General to consider developing

--automated audit information systems controls to assure that all reported findings are included and

--unique identifiers for each entity audited.

HEW COMMENTS

In commenting on our recommendations for improving the accuracy of information being accumulated and reported, HEW expressed concern about the cost effectiveness of these proposals in terms of the need for 100-percent accuracy.

Because our review was based on a random sample which should be representative of the universe and because a majority of the 269 sampled reports did not contain any monetary findings that could be omitted, we believe a 17-percent omission rate in the amount of findings is sufficiently high to justify the development of controls to assure accurate reporting.

With respect to developing unique identifiers for each entity audited, the Inspector General said that the Department had recently developed such multi-digitated-code identifiers for grantees and contractors which could be incorporated into the automated audit information system, but that the time to reprogram the system to accommodate the identifiers would be sizeable and might not be worthwhile because information on individual entities could be identified manually.

Because HEW programs involve about 50,000 grantees or contractors which are subject to audit, the use of unique identifiers in the automated system would facilitate broad analyses of prior audit coverage involving large groups of entities as we attempted to do with universities. We believe such broad analyses could be helpful to Audit Agency management in planning future audit emphasis.

CHAPTER 4

ACTIONS FOLLOWING ISSUANCE OF AN AUDIT

REPORT COULD BE STRENGTHENED

The Audit Agency's procedures manual provides that "The true value of any audit is the degree of action that is taken on the findings raised and recommendations made in the report." We were unable to assess the "true value" of the audits we sampled because of the lack of information concerning (1) the actions taken on the findings and (2) the effects of those actions. In this chapter, we describe problems encountered by both management and the Audit Agency in following up and correcting deficiencies identified in audit reports and many of the steps being taken to deal with those problems.

IMPORTANCE OF ACTIONS FOLLOWING ISSUANCE OF AN AUDIT REPORT

In 1957, 1968, and 1974 the Comptroller General issued statements of basic principles, standards, and concepts to guide Federal agencies in developing internal audit organizations and procedures. The importance of both management's and the internal auditor's actions following issuance of an audit report is reflected in the following excerpts from the statements:

"Top management's role is essential here. By its inattention or inaction, much of the constructive benefit of the internal auditor's work can be lost. On the other hand, its interest in and use of his findings and recommendations can contribute much to the recognition of the importance of his work at all management levels."

"Primary responsibility for action and followup on audit recommendations rests with management. A good control system will include procedures under which management officials will evaluate the effectiveness of actions taken on audit recommendations."

"A desirable procedure is to have regular status reports prepared for the information of management officials and the internal auditors, as to actions taken on audit recommendations. Also, provision should be made

for regular inquiry into whether proposed corrective actions have, in fact, been taken and their effectiveness. The responsibility for such followup should be that of management officials, but the internal auditors should participate."

"Thus, reporting a finding, observation, or recommendation should not end an internal auditor's concern with the matter. From time to time he should ascertain whether his recommendations have received serious management consideration and whether satisfactory corrective action has been taken."

TOO MUCH DISCRETION GIVEN TO HEW
MANAGEMENT OFFICIALS TO CLEAR
AUDIT FINDINGS

For audits of HEW grantees and contractors (except those dealing with proposed overhead rates) performed either by the Audit Agency or by an external audit organization, the Audit Agency coded the reported findings for the stewardship report. The procedures and requirements for grantees, contractors, and HEW management officials in replying to findings included in the stewardship report were as follows.

--Upon issuance of a report with findings and recommendations, the grantee or contractor audited was to respond to each finding within 30 days, addressing the applicable HEW action official (identified in the report transmittal letter). If the grantee or contractor has not responded within 30 days, that official follows up with the entity.

--After receipt and evaluation of the grantee's or contractor's comments, the operating component (action official), in an audit clearance document to the Audit Agency, presents its position on each finding and the actions taken to resolve it. This document enables the Audit Agency to close the findings and remove them from the stewardship report. Reports remain in the stewardship report until the operating component responds to all findings (it could

submit several clearance documents for the same report). Under HEW procedures the operating component's response is considered overdue if the clearance document(s) is (are) not received and the report is not cleared from the stewardship report within 180 days from the date of the report.

HEW management officials designated one or more "action" officials in the respective organizations to (1) assure that the grantee or contractor audited responded to the audit findings and recommendations, (2) evaluate the response, and (3) prepare and submit the audit clearance document to the Audit Agency. Some officials had written procedures for these actions, others did not. Those that did not followed unwritten procedures. For example, one official said that his office (1) telephoned the entity audited when it did not reply to the report within 30 days and (2) reviewed and evaluated the reply (if the reply was not responsive, the official contacted the entity and obtained needed additional information) and prepared an audit clearance document for submission to the Audit Agency.

Most of these written and unwritten procedures were so broad as to permit the action officials to use their own criteria for determining what was sufficient corrective action to close the findings and remove them from the stewardship report. One set of procedures provided that, upon receipt of grantee response, action officials were to discuss significant findings and proposed resolutions with grantee and programs staff, write a closure letter, and prepare stewardship materials. Variations in operating officials' criteria for closing findings resulted in noncomparable information about the status of findings appearing in the stewardship report.

Audited entity's response to operating component frequently exceeded 30 days

From records maintained by "action" officials and discussions with them, we analyzed a total of 66 reports--46 included in our basic data (issued in fiscal year 1974 and the first half of fiscal year 1975) and 20 (5 from each of the 4 regions included in our review) prepared by other audit organizations, such as independent public accountants, State or local auditors, or other Federal auditors (issued by the Audit Agency in fiscal year 1974--with

audit findings and recommendations in the stewardship report.) The audited entity was to respond to the findings and recommendations within 30 days in 55 of the 66 reports.

Details concerning the 11 reports for which no response was requested follow.

--Four reports concerned administrative costs incurred under the Medicare program and five concerned audits of a State's department of public aid. The final reports presented the entities' positions with respect to the findings and recommendations, and the Audit Agency advised them that they could respond again if they wished; otherwise, the regional SSA or SRS representative would initiate actions to settle the findings and recommendations.

--A report of a university audited by DCAA, the cognizant audit group, noted unsupported or questionable costs on PHS projects. The Audit Agency sent the report to PHS commenting that it might wish to contact the university in connection with the findings. PHS corresponded and met with university officials and agreed that the university should remit \$225,000.

--From a report on a nonprofit organization which was defunct at the time of audit, the Audit Agency found a need for improved procedures and internal controls but said any recommendations to that effect would be superfluous. Instead it recommended that SRS initiate action against responsible parties within the defunct organization to recover all funds that were not properly used for grant purposes.

For the other 55 reports, the involved entities were requested to respond to the report within 30 days--22 did; 25 did not; and a formal response was not required from 8. Replies were not necessary from the 8 because the action officials (1) considered, in 5 instances, the replies to the draft reports or responses at the exit conference adequate, (2) met with the entity in 2 instances to resolve the findings and recommendations instead of requiring a

formal response, and (3) in the remaining instance notified the entity audited that a reply was not necessary because the auditor (in this case the "city auditor," not the Audit Agency) did not fully understand the system audited and therefore the auditor's finding was not valid. Details by principal operating component for the 55 are shown below.

Principal operating component	Days to respond				No response required	Total
	0 to 30	31 to 60	61 to 120	Over 120 (range)		
ED	4	2	1	2 (157-279)	2	a/12
SRS	3	4	1	-	1	9
SSA	4	2	-	-	3	9
OHD	2	1	-	3 (155-273)	1	7
PHS	<u>9</u>	<u>4</u>	<u>3</u>	<u>1</u> (197)	<u>1</u>	<u>18</u>
Total	<u>22</u>	<u>13</u>	<u>5</u>	<u>6</u>	<u>8</u>	<u>a/55</u>

a/Includes an undated response (the audit clearance document was submitted to the Audit Agency 440 days after the report was issued).

For entities that responded in the 31- to 60-day period, we did not attempt to determine why they had not responded earlier. In those instances in which the entity took longer than 60 days, we determined that, in most instances, the action officials had not aggressively followed up to obtain a response. For example, the PHS took no followup action until 75 days after the report was issued; the entity immediately responded to his letter. Some action officials said they did not have enough staff to adequately handle the workload at that time. One official said his 4-person staff was later increased to 10.

Audit clearance submissions frequently exceeded 180 days and often relied solely on statements by the audited entity

As shown below, 27 of the 66 action officials completed audit clearance documents and submitted them to the Audit Agency within 180 days, 36 after the 180-day period, and 3 had not completed the documents as of September 1976.

In most instances in which the audit clearance documents were submitted to the Audit Agency after the 180-day period, the findings and recommendations concerned financial adjustments and/or the audited entity disagreed with some or all of the findings and recommendations. We were unable to

identify any relationship among the late submissions of audit clearance documents, the types of action taken by officials to assure that corrective action was taken on the findings and recommendations, and the length of time the entities took to respond to the action officials.

Principal operating component	Days to issuance				No document issued	Total
	0 to 180	181 to 240	241 to 300	Over 300 (range)		
ED	1	1	2	7 (306-608)	1	12
SRS	5	4	3	3 (343-434)	-	15
SSA	6	3	-	2 (346-378)	2	13
OHD	2	3	1	1 (377)	-	7
PHS	<u>13</u>	<u>5</u>	<u>1</u>	<u>-</u>	<u>-</u>	<u>19</u>
Total	<u>27</u>	<u>16</u>	<u>7</u>	<u>13</u>	<u>3</u>	<u>66</u>

No documents issued

Details concerning the three reports for which audit clearance documents had not been submitted to the Audit Agency as of September 1976 are shown below.

Report #1--A report prepared for HEW by the Department of the Interior's audit organization and issued by the Audit Agency's New York regional office on February 26, 1974, concerned HEW grants and contracts at a college from July 1, 1970, through June 30, 1972. The report questioned costs of \$559,213, in addition to \$401,797 questioned in the previous audit (prior report dated February 10, 1972). The prior report had been cleared from the stewardship report based on a January 1973 letter from the college to ED, indicating that schedules and other supporting documentation for questioned costs of \$467,569 would be prepared by February 20, 1973. The February 1974 report indicated that documentation had supported only \$65,772, leaving \$401,797 of claimed costs still unsupported. In a March 26, 1974, response, college officials disagreed with most of the costs questioned during the current audit and did not comment on the \$401,797.

In September 1975, 1-1/2 years after the college responded to the report, ED's audit liaison and coordination staff reassigned responsibility for resolving the report

findings and recommendations from the Bureau of Post-secondary Education in Washington, D.C., to the HEW Regional Commissioner of Education in New York. The New York staff immediately took steps to resolve the findings. A finding concerning an apparent duplicate claim of \$5,713 for architectural-engineering fees was resolved in November.

In December 1975, additional information on another finding was requested from the Department of the Interior's audit organization. This information was received in April 1976, and the college was sent a letter in May 1976 clarifying the report findings. The college responded in June 1976 that the letter had been referred to the accounting section. As Department of the Interior auditors were currently auditing its grants and contracts, the college planned to await the outcome of the audit before responding further. On September 17, 1976, an ED representative said he did not consider the reply responsive and would contact both the college officials and the auditors.

ED's audit liaison and coordination staff attributed the delay in resolving the two audit reports to two factors: Both reports dealt with several HEW operating components and bureaus within ED, and the cognizant bureau and the audit liaison and coordination staffs lacked sufficient personnel. The responsibility for resolving this type of audit report was assigned to the office or bureau having the most program funds involved during the audit period; this office must coordinate its efforts with the other ED offices and HEW operating components. They added that resolving audits of this type was usually not given high priority. Further, the audit liaison and coordinating staff was not large enough to handle the detailed effort necessary. It had recently been elevated organizationally to the Office of the Commissioner, and additional personnel had been recruited. Operating procedures were being developed to expeditiously designate or redesignate, when necessary, cognizant responsibility and to systematically follow up on projected due dates and auditee responses.

Report #2--A report issued by the San Francisco audit office on January 9, 1974, concerned an audit of administrative costs incurred by an intermediary under the Medicare program from January 1, 1969, through December 31, 1970. The report indicated that the intermediary disagreed with most of the \$250,169 questioned by the Audit Agency. In its March 26, 1974, response to the request for refund

of the questioned costs, the intermediary indicated that an earlier audit would affect the current audit findings and should be resolved first. This earlier audit report, dated December 31, 1970, concerned administrative costs for 1968 and was finally resolved in July 1975, more than 4-1/2 years after the report was issued. In February 1976 the action official said that, by that time, the Audit Agency was reviewing the administrative costs incurred for 1971 through 1973 and had raised additional questions which affected the 1969 and 1970 costs. As of September 1976, more than 2-1/2 years after the report was issued, the action official had not resolved the audit findings.

Report #3--A report issued by the New York audit office on October 29, 1974, concerned an audit of administrative costs claimed by an intermediary under the Medicare program for January 1971 through December 1972 and benefit payments claimed for January 1971 through June 1973. The report recommended that financial adjustments totaling \$472,653 be made and three procedural deficiencies be corrected. In a September 1974 response to the draft report, the intermediary disagreed with \$77,181 of the recommended financial adjustments. It also disagreed with one of the procedural findings. We were advised by the action official that all but one of the disputed findings were resolved--in favor of the intermediary--by September 1975 and that in November 1975 a decision was made to "conditionally close" the audit (that is, to set the one finding aside until a decision about it was made at SSA headquarters). He said the intermediary did not agree and wanted the last finding (\$72,800) resolved first. It was resolved in June 1976 and on September 1, 1976, the official forwarded a closing agreement to the intermediary. He indicated that when the agreement is signed by the intermediary and a refund is made, an audit clearance document would be prepared and submitted to the Audit Agency.

Documents issued

For the 63 reports on which audit clearance documents were submitted to the Audit Agency, action officials had:

--Relied on statements by the entities in 28 instances that corrective actions had been or would be taken.

- Assured themselves corrective actions were taken for several findings and relied on statements by the entities for other findings in 22 instances.
- Assured themselves corrective actions were taken in 10 instances.
- Disagreed with the only finding in one instance (OHD).
- Attempted to get the entity to take corrective action but had little success in one instance (PHS); therefore, the document was issued solely to indicate agreement with the Audit Agency's findings. The official advised the entity it could appeal the findings, which it did.
- Initiated in one instance (SRS), as recommended by the Audit Agency, action against responsible parties within the defunct organization to recover all funds not properly used for grant purposes by turning the case over to the HEW Office of the General Counsel.

Details by principal operating component are shown below.

<u>Principal operating component</u>	<u>Relied on statement by entity</u>	<u>Actions taken for some findings and statements made for others</u>	<u>Actions taken</u>	<u>Other</u>	<u>Total</u>
OE	6	2	3	-	11
SRS	6	6	2	1	15
SSA	4	3	4	-	11
OHD	4	2	-	1	7
PHS	<u>8</u>	<u>9</u>	<u>1</u>	<u>1</u>	<u>19</u>
Total	<u>28</u>	<u>22</u>	<u>10</u>	<u>3</u>	<u>63</u>

An example of clearing an audit solely on the basis of statements by the entity audited follows.

An April 19, 1974, report prepared by the Audit Agency concerned practices and procedures relating to income and assets of Medicaid recipients in county and private nursing homes in Pennsylvania for July 1, 1972, to June 30, 1973.

The report contained three findings and five related recommendations for correcting management deficiencies. The entity replied to the SRS action official on May 10, 1974, agreeing with the findings and recommendations and advising of the corrective actions planned. The action official submitted the audit clearance document to the Audit Agency on June 3, 1974, based on the information in the May 10 reply. The clearance document indicated the corrective actions to be taken and said that SRS would monitor their implementation and effectiveness. The document however, did not indicate any milestones for accomplishing the proposed action. The action official met with the entity on June 12, 1974, to discuss the implementation of the proposed corrective actions. At the time of our fieldwork in October 1975 (16 months later), no followup action had been made to determine whether the promised corrective actions were taken. However, the action official said followup was planned for fiscal year 1976.

AUDIT AGENCY NOT RESPONSIBLE
FOR EVALUATING BASES FOR
CLEARING AUDIT FINDINGS

The Audit Agency had no formalized procedures for reviewing and evaluating the documents prior to clearing the audit findings from the stewardship report. It considered these documents to be vehicles to advise of actions taken or planned.

Because the operating components were responsible for program administration, including the resolution of auditing findings, an Audit Agency headquarters representative in the Division of Audit Coordination told us that no real evaluation was made when audit clearance documents were submitted. He compared completed documents with the code sheet listing each finding and recommended financial adjustment, and he considered this as more of a processing than an evaluation function. He said if a document indicated the entity had implemented or planned to implement the recommendations but did not specifically address each finding, and if the findings were minor and procedural in nature (for example, if the entity audited did not reconcile its bank account), he accepted the document.

The representative contacted an action official very infrequently, maybe once or twice a year, to clarify the information on a document. He did not require officials

to submit an amended document and would accept an explanation over the telephone. Further, he relied on the Audit Agency's applicable headquarters division and regional or other audit office to evaluate any disagreement with a finding.

Copies of audit clearance documents were sent to the Audit Agency's applicable headquarters division and to the audit office that issued the report. An official from one of the regional audit offices said his region did not receive copies of all documents and merely filed those it did receive. No one on the staff reviewed them, and the regional office assumed that headquarters staff evaluated them. An official from another regional audit office said the appropriate assistant regional audit director or branch manager reviewed the documents to determine what corrective action was taken by the operating component. He cited an example in which the audit office did not agree with the component's position and, as a result, conducted a followup audit. The audit showed that \$35,825 of the recommended financial adjustments had been improperly waived.

The headquarters divisions--university and nonprofit audits, State and local audits, and SSA audits--had no procedures for reviewing and evaluating the documents. One representative said he considered the documents to be for informational purposes and he relied on the Division of Audit Coordination to evaluate them. Others said they compared the documents with the reports in some instances and contacted the regional audit office for any necessary clarification. However, they seldom found it necessary to contact the regional audit offices.

The Department's stewardship reporting system treated all corrective action situations as equivalent. For example, an audit clearance document completed by an operating component on the basis of statements made by the entity audited was treated the same as one which was not completed until the component was certain that corrective actions had been taken. In fact, the first component could be in compliance with Department procedures for timely submission of the document, whereas the latter component could be criticized for exceeding the time limit for submitting the document.

The audit clearance document was designed to provide a uniform medium through which full information was furnished to involved parties concerning actions taken by operating components on audit findings. When action

was taken on these findings, the operating components were to indicate on the documents, clearly and concisely, the actions taken in clearing audit findings and acting upon recommendations. When several steps are to be taken, the components indicate when each of the steps will be accomplished. When a component disagrees with a finding, it includes a concise explanation as to the basis for disagreement. For findings which remain open because the component either has taken no action or has not completed action, this information is indicated in the section of the document entitled "Findings Remaining Open."

We reviewed audit clearance documents received by the Audit Agency for 63 sampled audit reports covering 348 findings, 365 recommendations for correcting management deficiencies, and 173 recommended financial adjustments totaling \$46.3 million. These reports were issued in fiscal year 1974 or the first half of fiscal year 1975 by the 4 regional audit offices reviewed. Information submitted for 49 of the reports did not indicate

- agreement or disagreement with 63 findings and 73 recommendations,
- the basis for not agreeing with 3 findings and 40 recommendations,
- whether corrective actions were taken for 8 findings that were agreed with,
- the specific corrective measures for 103 findings for which it was indicated that some actions were promised or taken, or
- when promised actions for 48 findings would be accomplished.

During followup reviews, the Audit Agency found similar instances in which the documents did not indicate "the extent of corrective action taken" or when the actions taken were not in accord with the actions reported.

Incomplete clearance document

A November 1974 report prepared by the Audit Agency concerned costs claimed by a college under HEW research and training grants and contracts for the year ended June 30, 1973. The report contained four procedural findings, six

related recommendations, and two monetary findings--one recommending a financial adjustment of \$27,800 and one questioning the propriety of about \$3.8 million. According to the audit clearance document, dated May 30, 1975, the college "has taken appropriate actions to correct the reported deficiencies." It also showed that the operating component settled the recommended financial adjustment of \$27,800 for zero dollars. The document did not indicate (1) whether the component agreed or disagreed with the monetary findings of \$27,800 (we determined that the component did disagree with the finding), (2) the specific corrective measures taken for the four procedural findings and six related recommendations (we determined that the college had only agreed to take appropriate corrective action and that the action official had not followed up to determine the status of these promised actions), and (3) a determination of the propriety of about \$3.8 million (we determined that, after reviewing additional data supplied by the college, the component disallowed \$120,000 of this amount).

HEW TO ESTABLISH ACCOUNTING CONTROLS TO IDENTIFY AMOUNTS RECOVERED

HEW management officials generally did not have written procedures providing for inquiry into whether corrective actions had been taken and the effectiveness of those actions including actual recoveries for recommended and accepted audit adjustments. Several officials from three of the five principal operating components said they relied either entirely or partially on the Audit Agency to follow up during the next audit of that entity. One official advised us that workload and staff size and turnover limited the amount of followup his organization could do.

We interviewed and obtained data from action officials concerning the 63 sampled reports for which audit clearance documents were submitted to the Audit Agency. Of the 365 recommendations for correcting management deficiencies, the operating components agreed with 351 in 53 reports. For 299 (85 percent) of those from 42 reports, they had not followed up to determine whether corrective actions had, in fact, been taken and what their effects were. Reviews had been scheduled by the operating components to follow up on only 18 recommendations from 5 of the 42 reports.

The operating components agreed to fully or partially sustain 105 of the 173 recommendations for financial adjustments of about \$42.6 million in 38 audit reports. Of this amount, adjustments of only \$15.9 million, or 37 percent, had actually

been made by March 1976. The following chart summarizes the status of the remaining \$26.7 million.

<u>Status</u>	<u>Amount</u>
Awaiting decisions or documentation on adjustment amounts to be effected	\$18,591,956
Sustained amount appealed by entity audited--appeal not yet resolved	8,053,652
Adjustments awaiting negotiations with entity audited	35,540
Decision to sustain reversed by operating component	<u>28,583</u>
Total	<u>\$26,709,731</u>

Although the \$26.7 million of recommended financial adjustments had been cleared from the stewardship report, the final amounts to be adjusted had not been firmly established. The stewardship report, therefore, contained imprecise information which has been used by HEW to show Audit Agency accomplishments concerning monetary recoveries. For example, HEW's budget justifications for the Audit Agency for 1976 showed "recoveries" of \$92 million and \$46 million during fiscal year 1974 and the first half of fiscal year 1975. Similarly, HEW's budget justifications for the Audit Agency for 1977 showed fiscal year 1975 "recoveries" of \$84.4 million. In connection with May 1976 hearings before a Subcommittee of the House Committee on Government Operations, an Audit Agency official clarified what was meant by "recovery" and indicated that such amounts represented recommended financial adjustments accepted by the operating agencies and that the Audit Agency did not maintain records on amounts actually recovered.

In March 1977, HEW took steps to correct the data problems and to improve its audit followup system by placing accepted adjustments under accounting controls. We believe this new system will enable the Audit Agency to more precisely identify its accomplishments in terms of amounts actually recovered as a result of its work.

AUDIT AGENCY USUALLY MADE FOLLOWUP
DURING NEXT SCHEDULED AUDIT

Before fiscal year 1975, the Audit Agency's system for ascertaining whether satisfactory corrective action had been taken in response to a prior audit was, for the most

part, based on tasks performed during the next audit of an entity or activity. However, the length of time between audits of the same entity may range from 1 to 4 years, or longer.

Of the 214 entities covered by audits included in our review--about which we gathered information for our analytical effort--125 had been audited previously by either the Audit Agency or other audit organizations. Ninety-eight of the prior reports had findings and recommendations. Our review of the reports, workpapers, and supporting information for the more recent audits of these 98 entities showed that the Audit Agency followed up on the status of all the findings and recommendations in 74 instances, on some in 9 instances, and on none in only 15 instances. Details by audit office are shown in the following table.

<u>Audit office</u>	<u>Findings and recommendations followed up on</u>			<u>Total reports</u>
	<u>All</u>	<u>Some</u>	<u>None</u>	
Chicago	24	2	3	29
Philadelphia	15	3	3	21
New York	7	1	1	9
San Francisco	25	3	1	29
SSAA	1	-	1	2
WAAO	<u>2</u>	<u>-</u>	<u>6</u>	<u>8</u>
Total	<u>74</u>	<u>9</u>	<u>15</u>	<u>98</u>

in most of the 15 instances in which followup was not performed, there appeared to be logical reasons for not doing so. Sometimes it was because the current audit (1) covered matters which were not included in the previous audit or (2) was of a different organizational component of the entity than that audited previously. For example, one current audit covered nonexpendable personal property in the possession of the organization. An audit office representative advised us no previous audit had been made in this area of the organization.

The current audit report oftentimes did not show the status of prior audit findings even though followup effort was performed. However, those 48 reports which contained the status of prior findings showed that, in many instances, entities had not taken corrective action on prior findings.

<u>Audit office</u>	<u>Findings on which corrective action taken</u>			<u>Total reports</u>
	<u>All</u>	<u>Some</u>	<u>None</u>	
Chicago	10	11	2	23
Philadelphia	4	1	2	7
New York	1	-	1	2
San Francisco	3	6	5	14
WAAO	<u>1</u>	<u>1</u>	<u>-</u>	<u>2</u>
Total	<u>19</u>	<u>19</u>	<u>10</u>	<u>48</u>

Prior findings were repeated in the current audit in 28 of the 48 instances. For example, in a November 11, 1974, audit report on a State's statewide cost allocation for the year ended June 30, 1972, the Chicago audit office stated that "while most of the findings and recommendations in the prior report were corrected some were not and repeated in the current report." The findings previously reported in December 1971 concerned (1) inadequate supporting documentation for financial and allocation data related to the proposed cost allocation plan and (2) inclusion of unallowable equipment and capital improvement expenditures in the plan.

RESULTS OF POSTAUDIT REVIEWS
BY THE AUDIT AGENCY

Beginning with fiscal year 1975, the Audit Agency allocated time to postaudit reviews of recommendations included in selected audit reports. Its procedures stated that the objectives of such reviews were to determine whether recommended actions were taken or were in process and whether such actions led or would lead to resolution of the reported deficiencies. Another purpose of the reviews was to evaluate HEW operating components' systems for follow-up and to recommend necessary improvements.

We reviewed all of the reports issued by the Audit Agency in 1975--a total of 23--on its postaudits of findings and recommendations from previously issued reports. As shown below, seven of the reports noted that effective corrective actions had been taken for all the prior findings and recommendations.

<u>Principal operating component</u>	<u>Implementation of prior findings/recommendations</u>		<u>Total</u>
	<u>Adequate</u>	<u>Inadequate</u>	
ED	2	3	<u>a/6</u>
SRS	1	6	7
SSA	2	2	4
OHD	2	2	4
PHS	<u>-</u>	<u>2</u>	<u>2</u>
Total	<u>7</u>	<u>15</u>	<u>a/23</u>

a/Includes a report which did not indicate the status of the findings and recommendations. The report addressed ED's system for resolution and followup of audit findings and recommendations.

The 15 reports on inadequately implemented actions showed that some of the findings and recommendations had been satisfactorily resolved. Examples of the postaudit reports follow.

--The Audit Agency followed up seven findings and recommendations from an audit report issued in September 1971 on a State agency participating in the Vocational Education Program. The followup report, issued in September 1975, stated that the findings had been cleared from the Audit Agency's stewardship report, based upon assurances by the State agency that corrective actions were taken or planned. The auditors found that, while three of the findings were satisfactorily corrected by the State agency, the deficiencies previously reported for four findings had not been adequately corrected. ED had not followed up the findings and recommendations after issuance of the clearance document. It cited the lack of staff as the reason.

--The Audit Agency followed up five findings and related recommendations in an audit report issued in March 1974 on a State agency participating in the Health Insurance Benefits Program, Title XVIII, section 1864, of the Social Security Act.

The followup report, issued in June 1975, stated that the review was limited to determinations as to whether the corrective actions directed by SSA were implemented by the State agency and whether actions taken had led or would lead to the resolution of the deficiencies. The auditors found that satisfactory actions had not been taken to correct three of the five previously reported deficiencies.

Only two of the postaudit reports indicated the Audit Agency reviewed the operating components' followup systems for insuring that corrective actions are taken. In both instances (SRS in the San Francisco region and ED in the New York region), the Audit Agency found that improvements were needed in the components' systems.

The San Francisco regional audit office found that SRS in the San Francisco region had been "very effective in assuring that State agencies make financial adjustments recommended in audit reports" but:

"* * * could improve its audit follow-up procedures by making on-site reviews of corrective action. The SRS Regional Office did not make on-site reviews to assure that state agencies implemented recommendations for procedural or management improvements. Consequently, it was not aware that the state agencies had not implemented 2 of 11 such recommendations."

SRS planned to develop comprehensive written procedures for followup on audit findings which will provide for making onsite reviews of corrective action.

The New York regional audit office found that ED in the New York region cleared audit findings:

"* * * based on inconclusive documentation provided by the grantee, which, in many instances, did not disclose the extent of corrective action taken. Moreover, we noted that follow-up action, in the form of site visits, was not taken to assure that audit recommendations were, in fact, implemented by the grantee. As a result, * * * program officials were generally unaware of the

extent and nature of actions taken by the grantee to improve * * * program operations."

The audit office also found that ED had the grantee complete the audit clearance document in several instances, which it indicated defeated the intent of the document, "namely, to determine the actions taken by the operating agency to followup and resolve outstanding audit findings."

Eight of the 23 postaudit reports we reviewed were issued by the Chicago regional audit office. The director told us his office had not reviewed and did not plan to review the systems used by operating components to follow up on recommendations. Reviews of components' systems were not required as part of postaudit followup by the Audit Agency, and the office did not have sufficient staff to undertake such an effort. The Chicago regional audit office expended an average of 16 staff-days following up on the 8 previously issued reports, with 2 of them requiring 48 and 49 staff-days, respectively.

The San Francisco and New York regional audit offices expended 86 and 69 staff-days, respectively, reviewing the systems used by the operating components to follow up on recommendations. The offices each used 5 previously issued reports containing findings and recommendations as their basis for reviewing the systems. In addition, the San Francisco office determined the extent that the findings and recommendations had been implemented.

In May 1976 the Audit Agency completed an analysis of the results of followup review actions taken on prior findings and recommendations in 110 reports. The 110 reports were those which caused no controversy at the time of closure (that is, corrective action was promised). The analysis showed adequate actions had been taken to correct the previously reported deficiencies in 61 cases; full action had not been taken in the remaining 49 cases. According to the analysis, there were not any cases in which no action was taken.

In connection with testimony before a Subcommittee of the House Committee on Government Operations in May 1976, an Audit Agency official stated that, up to that time, his organization had not detected any general reasons for the incomplete action but that it was clear to him that the operating agencies had to monitor the corrective actions more fully.

In connection with the analysis on June 1, 1976, the Audit Agency issued summary reports to the head of each of the five principal operating components, recommending to one component (ED) and suggesting to the others the need for developing or strengthening written procedures for a systematic followup process. The operating components were requested to respond within 60 days on the actions taken to reemphasize or strengthen their procedures for following up and monitoring corrective actions taken by the entities audited. Four of the five components (ED, SRS, OHD, and PHS) responded that they were in the process of strengthening their procedures and indicated various measures taken or planned. For example, the Administrator of SRS, said

"* * * where your audits include recommendations for the refund of a specific amount of money to the Federal account, SRS Central Office maintains strict follow-up procedures through the audit clearance process to account for all the money involved. Where audit recommendations are strictly 'management' oriented or where no specific amount was indicated for refund, there has not been a high priority given to the follow-up to determine if all recommendations were followed.

"* * * We are currently in the process of updating and revising a guide that outlines the responsibilities and procedures within SRS for handling audit reports. Included in this guide will be a section on 'Follow-Up Action' that will contain reporting procedures to be used to track each audit recommendation, including management and 'non-money' recommendations, until the action has been satisfactorily carried out. These procedures should go a long way towards correcting some of the deficiencies noted in your report."

The fifth operating component (SSA) took exception to parts of the summary report. SSA told the Audit Agency that, contrary to the summary report indicating that an SSA official informed the Audit Agency that the Bureau of Disability Insurance had no procedures for followup on audit findings and recommendations and that the Bureau of Health Insurance had unwritten procedures, the Bureau of Disability Insurance had had written procedures for some time, the Bureau of Health Insurance's division of contractor operations had written procedures, and its

division of State operations had drafted procedures and expected to publish them in a few months.

CONCLUSIONS

Within HEW, the principal operating components are responsible for administering assigned programs, which includes the timely resolution of audit findings. To assist in this function, the Audit Agency's automated audit information system produces quarterly stewardship reports showing, among other things, audit reports with open findings and those reports for which action was taken or promised during the prior quarter. Information entered on actions taken or promised are based on clearance documents submitted by operating officials.

Under the Department's procedures, operating officials have been permitted considerable discretion in classifying an audit finding--on which there is agreement--as resolved, and the Audit Agency is apparently not responsible for evaluating the completeness or the specificity of the related documentation. In many cases, information on corrective action is obtained from third parties, such as universities and State and local governments, with no verification by operating officials. Our review and the Audit Agency's own formalized followup reviews initiated in fiscal year 1975 and its follow-up of prior findings in subsequent audits have shown that audit findings shown as resolved were, in fact, not.

In addition, until March 1977 when HEW established accounting controls over recommended audit recoveries, the Audit Agency did not have information on actual recoveries even though its monetary accomplishments have sometimes been reported in such terms.

In our opinion, too much discretion has been given to HEW management officials to clear audit findings under the stewardship system. Also, we believe that the Audit Agency should be encouraged to evaluate the completeness and specificity of audit clearance documents and to reject those which are incomplete and/or vague.

We believe that the importance of reliable follow-up systems has been emphasized by Public Law 94-505, which requires the Inspector General to submit an annual report to the Secretary and to the Congress which shall include--

" * * * a description of recommendations for corrective action made by the Office with respect to significant problems, abuses, or deficiencies relating to the administration of programs and operations of the Department, and an evaluation of progress made in implementing recommendations described in the report, or where appropriate, in previous reports."

In addition, the Inspector General will report quarterly to the Secretary and to the appropriate committees or subcommittees of the Congress on any significant problems, abuses, or deficiencies concerning which the Office has made a recommendation for corrective action and/or which, in the judgment of the Inspector General, adequate progress is not being made.

RECOMMENDATIONS

To facilitate such reporting, the Secretary of HEW should direct the Inspector General to consider establishing more specific guidance for:

- HEW management officials to use when deciding whether corrective action has been sufficient to warrant ending the stewardship status reporting on audit findings.
- Audit Agency officials to use for evaluating the sufficiency of reporting by management officials about the status of corrective action on reported findings.

HEW COMMENTS

The Department agreed that improvements could be made in the way that HEW's principal operating components handled audit report matters and also agreed that the Audit Agency should take a harder look at proposed closing actions. The Department is proposing that each document closing an audit report be reviewed for adequacy by responsible Audit Agency senior staff--including the agency's regional audit director or designee who issued the report. If the review indicates that action is unsatisfactory or incomplete, the Audit Agency will consider contacting the responsible principal operating component to negotiate more appropriate action.

We believe that these proposed steps satisfy our recommendations with respect to initiatives by the Audit

Agency. We are, however, making a Government-wide review of several agencies (including HEW) of actions taken to resolve audit findings. In our opinion, this will clarify the steps needed to insure that the operating components will properly resolve audit findings.

CHAPTER 5
MODIFICATIONS OF EXISTING PROCEDURES
TO FACILITATE
IMPLEMENTATION OF PUBLIC LAW 94-505

Public Law 94-505, which established an Office of Inspector General for HEW, transferred the functions of the Audit Agency and the investigative function to that Office and prescribed specific duties and responsibilities for the Inspector General. We believe that the capability to fulfill certain of these responsibilities could be enhanced if the Audit Agency modified its methods of accumulating information to (1) identify the principal thrust or scope of its audits and (2) identify the relative importance of nonmonetary findings.

IDENTIFICATION OF SCOPE
BY ELEMENTS OF AUDIT

Federal Management Circular 73-2 issued in September 1973 sets forth policies to be followed in the audits of Federal operations and programs by executive departments and establishments.

"* * *the term 'audit' as used in this circular means a systematic review or appraisal to determine and report on whether:

- "1. Financial operations are properly conducted;
- "2. Financial reports are presented fairly;
- "3. Applicable laws and regulations have been complied with;
- "4. Resources are managed and used in an economical and efficient manner; and
- "5. Desired results and objectives are being achieved in an effective manner.

"The above elements of an audit are most commonly referred to as financial/compliance (items 1, 2, and 3), economy/efficiency (item 4), and program results (item 5). Collectively, they represent

the full scope of an audit and provide the greatest benefits to all potential users of Government audits. In developing audit plans, however, the audit scope should be tailored to each specific program according to the circumstances relating to the program, the management needs to be met, and the capacity of the audit facilities."

Although the Audit Agency has not defined the scopes of its audits in terms of these elements, its officials have estimated that about 75 percent of its effort is devoted to financial and compliance matters, 15 percent to economy and efficiency, and 10 percent to program results.

Our review tended to confirm this estimate. We asked an Audit Agency auditor to classify each audit in our sample as one or a combination of those elements. From the sample of fiscal year 1974 audits, we projected that the audit scopes were 62 percent financial/compliance, 2 percent economy/efficiency, 2 percent program results, and 34 percent a combination of these elements.

In view of the relatively limited activity in economy and efficiency audits and because Public Law 94-505 emphasizes the Inspector General's responsibility in promoting economy and efficiency in the administration of HEW programs and of preventing and detecting fraud and abuse in such programs, we believe that the Office of Inspector General could better monitor the fulfillment of its responsibilities under the new law through the identification of the scope or the principal element of its planned and initiated audits.

INFORMATION SHOWING IMPORTANCE
OF NONMONETARY FINDINGS

The Audit Agency has defined a finding as:

"* * * an 'errant condition' - a condition which, for some reason, did not follow an intended or desired pattern, and had undesirable results or results which were less than expected or hoped for."

Findings were primarily either

--monetary; for example, information that dollars were improperly spent and some recovery should result, or

--nonmonetary; for example, information that some actions should be taken to achieve performance improvements (as reductions in the time that patients spend in hospitals or in the time needed to award a grant) of a Federal program's operations.

For a monetary finding, we considered its relative importance as sufficiently indicated by the amount of dollars involved. However, we were unable to attach similar relative importance to the various nonmonetary findings which accounted for about 40 percent of the 784 reported findings included in our 163 sampled reports to HEW that contained findings. Nor were we able to determine the relative significance that the Audit Agency had attached to them.

The Audit Agency's automated information system has facilitated the identification of the incidence of different kinds of nonmonetary findings by providing separate codes for the more frequently reported finding descriptions. In addition, the element of professional judgment in assessing relative importance is always a determining factor.

Under Public Law 94-505, the Inspector General shall make reports on a quarterly-basis to the Secretary and to appropriate Committees or Subcommittees of the Congress identifying any significant problems, abuses, or deficiencies concerning which the Office has made a recommendation for corrective action and in which, in the judgment of the Inspector General, adequate progress is not being made.

In our view, the importance of having information assigning the relative significance to nonmonetary findings is illustrated by the House Committee report on the Inspector General bill, 1/ which stated that the quarterly

1/Report from the Committee on Government Operations, House of Representatives (H. Rep. 94-1573).

reports to the Secretary and congressional committees should be limited to recommendations that the Inspector General regards as particularly important rather than a listing of all recommendations on which timely action has not been taken.

We believe the implementation of the limited reporting provision could be facilitated if HEW program officials responsible for acting on Audit Agency recommendations were made aware of those nonmonetary findings and related recommendations which were considered by the Audit Agency as sufficiently significant to be potentially eligible for quarterly reporting by the Inspector General unless timely corrective action is taken.

CONCLUSIONS

With the enactment of Public Law 94-505, HEW's auditing and investigative activities--although remaining separate--were brought under the jurisdiction of one senior official with no program operating responsibilities. The prevention and detection of fraud and abuse is a function of audit as well as of investigations, whereas the promotion of economy and efficiency is not ordinarily an investigative function. Further, the investigative activity aimed at developing information to facilitate criminal prosecutions on a case-by-case basis does not necessarily lend itself to broad recommendations for improvements in program operations. Therefore, we believe it is likely that the Office of Inspector General must necessarily look to the HEW Audit Agency for providing coverage in promoting economy and efficiency and for providing information for quarterly reports on significant outstanding recommendations.

RECOMMENDATIONS

To facilitate the implementation of Public Law 94-505, we recommend that the Secretary of HEW direct the Inspector General to consider

--requiring the Audit Agency to identify the scope or principal element of its planned and initiated audits in terms of financial/compliance, economy/efficiency, or program results and

--requiring the Audit Agency to identify those nonmonetary findings and related recommendations which it believes are sufficiently significant

to be potentially eligible for quarterly reporting unless timely corrective action is taken.

HEW COMMENTS

HEW concurred in these recommendations. The Time Reporting and Audit Control System (discussed on p. 21) was revised in January 1977 to require reporting of the planned scope of each audit or combination thereof. Also, HEW stated that a procedure had been initiated for identifying and notifying principal operating components of those audit findings--both monetary and nonmonetary--being considered for inclusion in the quarterly report.

CHAPTER 6

SCOPE OF REVIEW

We developed a means whereby opportunities for assessing and improving performance could be obtained using information about past audits. To facilitate development and application of self-evaluation and improvement efforts, that means is illustrated in a separate case study report and involves

- the audit findings reported in audit reports,
- the reactions of the entities audited and the management officials responsible for changing errant conditions,
- relationships of information about audit staffing (audit staff-days by grade) and practices (identity of what auditors examined and how many) with information about audit results (reported audit findings), and
- a formula for using information about completed audits and their effects in obtaining estimates of anticipated benefits and costs of planned audits.

We also evaluated the Audit Agency's compliance with its federally promulgated policies and regulations.

QUALITATIVE EFFORT

We reviewed the audit activities and functions of the Audit Agency's headquarters divisions in Washington, D.C., DSSA in Baltimore, Maryland; WAAO; and four regional audit offices. We reviewed the Audit Agency's organization, its audit information system; and its policies, procedures, and practices for (1) hiring, training, promoting, and staffing, (2) self-assessment, (3) planning audit assignments, (4) scheduling, staffing, and controlling audit assignments, (5) assisting management in assuring adequate followup of reported audit findings and recommendations, and (6) evaluating work performed by external audit organizations for HEW. We also obtained views from HEW management officials at both the headquarters and regional levels concerning the adequacy of the Audit Agency's performances and services. We obtained views concerning the adequacy of audit reports and performance from HEW officials responsible for followup of reported audit deficiencies and recommendations. We also obtained information

from these officials on followup actions taken to assure effective corrective measures were implemented to resolve reported deficiencies.

SITE SELECTION

To compare information about audits among regions, we selected audits from 4 (Chicago, New York, Philadelphia, and San Francisco,) of the 10 regional audit offices, each selected because it generally

- maintained records showing staff time by work phase (startup and survey; review; report preparation and processing; supervision; and other--to account for effort by persons such as the Audit Manager, and other managerial or support staff) and by work area (for example, travel accounts, equipment accounts),
- issued a large number of reports, or
- had audit responsibility for a large amount of HEW-administered funds.

In addition, we selected audits from the DSSA and WAAO because the regional audit offices' reports pertain primarily to audits of grantees and contractors, whereas the DSSA and WAAO reports pertain to audits of HEW headquarters operations.

SELECTION OF AUDITS

To help us discover and develop explanations for indicated differences in effects of Audit Agency audits, we selected audits for which reports were issued to HEW management and/or HEW grantees and contractors (this category of reports accounted for about 83 percent of the Audit Agency's audit time in fiscal year 1975). The number of audits selected, by regional audit office, staff-days expended, and fiscal year, is shown below.

<u>Regional audit office</u>	<u>0 to 175 staff-days</u>			<u>Over 175 staff-days</u>			<u>Total audits</u>
	<u>1972</u>	<u>1974</u>	<u>1975 (note a)</u>	<u>1972</u>	<u>1974</u>	<u>1975 (note a)</u>	
Chicago	15	15	0	5	6	8	49
New York	0	8	12	0	3	4	27
Philadelphia	15	15	0	8	9	0	47
San Francisco	15	15	0	10	10	0	50
Total	<u>45</u>	<u>53</u>	<u>12</u>	<u>23</u>	<u>28</u>	<u>12</u>	<u>173</u>

a/First half only.

In addition, we selected other Audit Agency audits performed either for other Federal agencies by regional audit offices, or for HEW by DSSA and WAAO, and canceled audits.

The following table shows the number of audits about which we obtained detailed data.

Audits for other Federal agencies

<u>Audit office</u>	<u>Audits for HEW</u>	<u>Colleges and universities</u>	<u>Civilian Health and Medical Program of the Uniformed Services</u>	<u>Canceled audits</u>	<u>Total audits</u>
Chicago	49	49	2	1	101
New York	27	0	0	1	28
Philadelphia	47	0	1	1	49
San Francisco	<u>50</u>	<u>5</u>	<u>2</u>	<u>1</u>	<u>58</u>
Subtotal	<u>173</u>	<u>54</u>	<u>5</u>	<u>4</u>	<u>236</u>
WAAO	15	0	0	5	20
DSSAA	<u>10</u>	<u>0</u>	<u>0</u>	<u>3</u>	<u>13</u>
Total	<u>198</u>	<u>54</u>	<u>5</u>	<u>12</u>	<u>269</u>

APPENDIX I

APPENDIX I



DEPARTMENT OF HEALTH, EDUCATION, AND WELFARE
OFFICE OF THE SECRETARY
WASHINGTON, D.C. 20201

JUL 25 1977

Mr. Robert E. Iffert, Jr.
Assistant Director
Human Resources Division
United States General
Accounting Office
Washington, D.C. 20548

Dear Mr. Iffert:

The enclosed comments represent the tentative position of the Department on your draft report, "Ways to Increase Benefits from Agency Auditing." These comments are subject to reevaluation when the final version of this report is received.

We appreciate the opportunity to comment on this draft report before its publication.

Sincerely yours,


Thomas D. Morris
Inspector General

Enclosure

Comments of the Department of Health, Education, and Welfare on the
General Accounting Office Report, "Ways to Increase Benefits from Agency
Auditing"

OVERVIEW

The Department very much appreciates this assessment by the General Accounting Office on ways in which it can increase its utilization of the work done by the HEW Audit Agency. This assessment comes at a most appropriate time since the Audit Agency is now an integral part of the newly established Office of Inspector General and shares its mandate to attack fraud, waste, and abuse in the Department's programs.

GAO RECOMMENDATION

That the Secretary of HEW direct the Inspector General to consider:
Modifying the Automated Audit Information System to include the basis
for selecting audits in order to compare these bases with audit
results for the purpose of facilitating future planning.

DEPARTMENT COMMENT

We concur. A system modification will be considered for this purpose unless this information can be obtained manually with lesser effort. We believe it is important to note, however, that nonquantifiable audit benefits, such as improved program efficiency and effectiveness, need to be considered along with "dollar findings" in assessing audit results and planning future audits.

GAO RECOMMENDATION

That the Secretary of HEW direct the Inspector General to consider:
strengthening the monitoring of audits performed by non-Federal auditors
with emphasis on developing information to facilitate the identification
of those non-Federal auditors doing quality work at the lowest cost.

DEPARTMENT COMMENT

As noted by GAO, the Audit Agency issued revised procedures in March 1976 requiring regional audit offices to test the work of non-Federal audit organizations on a sample basis--including reviewing supporting workpapers.

We agree that additional emphasis can be placed on this monitoring function since there is a strong probability of a reasonable payoff. The following actions are planned covering not only audits in the university and nonprofit areas, but also those of Medicare intermediaries:

o Medicare intermediaries - Visits will be made to each regional audit office by November 30. These will determine the areas of review of non-Federal audits that are being adequately made and those where further improvement is indicated. At the conclusion of these reviews, recommendations on needed improvements will be furnished the Assistant Inspector General for Auditing. We are considering making these reviews on an annual basis.

o Other - A summary report of six-months experiences with the before-mentioned March 1976 guidelines was developed and has been reviewed by senior staff. Their suggestions and comments will be considered in a forthcoming revision and updating of these guidelines which will include cost/quality factors.

GAO RECOMMENDATION

That the Secretary of HEW direct the Inspector General to consider having: automated audit information systems controls developed to assure that all reported findings are included.

DEPARTMENT COMMENT

We are studying this matter to see whether additional or revised controls over data input are warranted, in terms of cost and need. GAO reports that 17% of the dollar value of findings in 269 reports they reviewed were not recorded in the system. These errors were noted in 11 reports or about 4 percent of the reports tested:

- The first example involved an instance where a regional auditor did not code an audit finding for inclusion in the system--because there was no standard code available that fitted the description of the finding. Under our procedures, a standard code should have been requested.

- The second example (as GAO notes) was caused by an auditor ". . . inadvertently missing a reported finding."

- The third example occurred because the computer's edit routine properly rejected several dollar findings which were being entered into the System under the same finding code. This edit check was woven into the System to preclude acceptance of duplicate entries. In situations such as this, these amounts should have been added and entered as one amount.

The cost of detecting and controlling these types of errors needs to be considered in relation to the necessity for 100 per cent accuracy of this kind of data.

GAO RECOMMENDATION

That the Secretary of HEW direct the Inspector General to consider having: unique identifiers developed for each entity audited.

DEPARTMENT COMMENT

The Department recently developed such unique identifiers which could be incorporated into the Automated Audit Information System. But, the time and effort needed to reprogram to accomodate these multi-digitated codes would be sizeable. As noted by the GAO report, information on the number of times an entity has been audited can be obtained manually, albeit not automatically. We will determine whether incorporating these unique identifiers into the System would be feasible and cost-effective.

GAO RECOMMENDATION

To facilitate such reporting, The Secretary of HEW should direct the Inspector General to consider establishing more specific guidance for:

- HEW management officials to use when deciding whether corrective action has been sufficient to warrant ending the stewardship status reporting relative to involved audit findings; and

- Audit Agency officials to use for evaluating the sufficiency of reporting by involved management officials about the status of corrective action relative to reported findings.

DEPARTMENT COMMENT

The Audit Agency's follow-up reviews--and analyses of information generated by its Automated Information System--confirm GAO's findings that improvements can be made in the way the Department's Principal Operating Component's (POCs) handle audit report matters. Our POCs are responsible for administering assigned programs, including making well-considered and timely resolution of audit findings. Under the Stewardship reporting system, they routinely inform the Secretary on their progress in resolving audit matters. There are well-established in place systems.

GAO's report accurately pinpoints a problem that needs continuing attention. We believe the current division of responsibilities is proper: POCs will administer this function as part of their overall responsibilities with accountability reports to the Secretary. On the other hand, the Audit Agency should take a harder look at POC-proposed closing actions. Our present thinking is every POC-submitted document closing an audit report will be reviewed for adequacy by responsible senior staff--including the Agency's regional audit director or designee who issued the report. If this review indicates that unsatisfactory or incomplete action had been taken or planned, we are considering contacting the responsible POC to negotiate more appropriate action.

APPENDIX I

APPENDIX I

These actions--particularly in conjunction with the Audit Agency's regularly scheduled follow-up reviews--should do much to expedite and improve the quality of POC actions on audit's recommendations.

GAO RECOMMENDATION

To facilitate the implementation of Public Law 94-505, we recommend that the Secretary of HEW direct the Inspector general to consider: requiring the Audit Agency to identify the scope or principal element of financial/compliance, economy/efficiency, or program results.

DEPARTMENT COMMENT

We concur. The Audit Agency's Procedures Handbook (Part II, Section III) covering the Agency's Time Reporting and Audit Control System (TRACS) was revised as of January 1977 to require reporting of the planned scope of each audit under the following definitions:

- Financial/Compliance
- Economy/Efficiency
- Financial/Compliance and Economy/Efficiency
- Program Results
- Financial/Compliance and Program Results
- Economy/Efficiency and Program Results -- or
- All of the Above

TRACS is an automated system designed to provide Headquarters and regional office management with timely and uniform information (both summarized and detailed) regarding: (i) status of audit assignments, (ii) periodic measurement of progress in terms of staffdays expended and audit reports issued in relation to the annual work plan, (iii) preparation of monthly billings to other Federal agencies for reimbursable audit staffhours expended; (iv) utilization of audit staffhours, and (v) audit classification.

GAO RECOMMENDATION

To facilitate the implementation of Public Law 94-505, we recommend that the Secretary of HEW direct the Inspector General to consider: requiring the Audit Agency to identify those non-monetary findings and related recommendations which it believes are sufficiently significant to be potentially eligible for quarterly reporting unless timely corrective action is taken.

DEPARTMENT COMMENT

We concur. A procedure has been initiated for identifying and notifying POCs of audit findings--both monetary and nonmonetary--being considered for inclusion in the quarterly report. We expect to refine this procedure on the basis of report experience.

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