

DOCUMENT RESUME

02818 - [A2093193]

Internal Auditing in the Department of the Army and the Office of the Secretary of Defense. July 27, 1977. 10 pp.

Testimony before the House Committee on Government Operations: Legislation and National Security Subcommittee; by D. L. Scantlebury, Director, Financial and General Management Studies Div.

Issue Area: Internal Auditing Systems (200).

Contact: Financial and General Management Studies Div.

Budget Function: Miscellaneous: Financial Management and Information Systems (4002).

Organization Concerned: Department of the Army; Department of Defense.

Congressional Relevance: House Committee on Government Operations: Legislation and National Security Subcommittee.

The internal audit function of the Department of the Army needs strengthening so its auditors can keep top management informed as to how operations are conducted and how recommendations for improvements are carried out. During fiscal years 1973 through 1976, the Army Audit Agency issued about 3,260 audit reports which identified opportunities for hundreds of millions of dollars in savings to the Department and contained many recommendations for achieving lower costs and increased efficiency. The audit functions should be raised to a higher level in the Army's organization. The auditors should be given freedom to identify and select activities for audit. At present, a committee composed of persons responsible for operations to be audited reviews and revises the Audit Agency's selection of activities to be investigated. In addition, Army auditors are restricted from auditing combat readiness and other tactical activities. These restrictions should be removed. The chief of the Audit Agency should be a civilian rather than a military officer, as is the case at present. There is a need for more effective use of the audit staff. The Army's audit followup system would be strengthened by placing this responsibility with the Army Audit Agency. This would permit auditors who are already located in the field and who are familiar with the reported conditions to evaluate the adequacy of corrective actions taken. (SC)

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UNITED STATES GENERAL ACCOUNTING OFFICE

WASHINGTON, D.C. 20548

FOR RELEASE ON DELIVERY
EXPECTED AT 10 A.M. EDT
WEDNESDAY, JULY 27, 1977

STATEMENT OF

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FINANCIAL AND GENERAL MANAGEMENT STUDIES DIVISION

BEFORE THE

SUBCOMMITTEE ON LEGISLATION AND NATIONAL SECURITY

COMMITTEE ON GOVERNMENT OPERATIONS

HOUSE OF REPRESENTATIVES

CONCERNING INTERNAL AUDITING IN THE DEPARTMENT

OF THE ARMY AND THE OFFICE OF THE

SECRETAR' OF DEFENSE

Mr. Chairman and Members of the Committee:

We are pleased to be with you today to discuss the results of our reviews of the internal audit activities of the Office of the Secretary of Defense and the Department of the Army. With me are Mr. George Egan and Mr. Richard Nygaard, both from the Financial and General Management Studies Division of GAO.

My testimony will summarize two reports. One report, which was issued to you on July 14, 1977, concerns the authority and staff resources available to the Deputy Assistant Secretary of Defense (Audit). The other, which is being issued to the Congress today, discusses a number of issues relating to the internal audit activities of the Army Audit Agency.

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Mr. Chairman, as you requested, the report dealing with the audit activities of the Deputy Assistant Secretary was not made available to the Department of Defense officials for comment. The report on Army Audit Agency was submitted to the Secretary of Defense for comments and contains the Departments of Army and Defense positions on our findings and recommendations.

RESULTS OF OUR REVIEW OF
THE ARMY AUDIT AGENCY

Let me say at the outset, Mr. Chairman, that the Army Audit Agency enjoys a high level of competence and professionalism among its staff. The benefits of its service greatly outweighs its cost. During fiscal years 1973-1976 the Audit Agency issued about 3,260 audit reports. These reports identified opportunities for hundreds of millions of dollars in savings to the department and contained many recommendations for achieving lower costs and increased efficiency. In fiscal year 1975 alone, the Audit Agency identified total potential savings amounting to about \$171 million that could accrue to the Army through implementation of audit recommendations. Considering the Audit Agency's annual operating costs, which totaled about \$21 million in fiscal year 1975, these accomplishments are noteworthy.

Despite these accomplishments, Mr. Chairman, the internal audit function of the Department of the Army needs strengthening so its auditors can keep top management better informed on how operations are conducted and recommendations for improvements

are carried out. Our report contains recommendations to:

- raise the audit functions to a higher level in the Army's organization,
- remove restrictions on the scope of audit work,
- appoint a civilian to the position of Chief of the Army Audit Agency,
- use the audit staff more effectively, and
- revise the system for followup on audit findings.

At this time, I would like to discuss each of these areas in more detail and summarize the Department of Defense's comments on the report.

INDEPENDENCE OF THE AUDIT AGENCY

As I indicated, at the time of our review the Army Audit Agency reported to a relatively low level within the Department of the Army. The Audit Agency reported to the Inspector General with two reporting levels between the Audit Agency and the Secretary of the Army. This placement was inconsistent with our audit standards relating to independence which require the audit function to be located at the highest practical organizational level. We believe the chief auditor should have the kind of relationship with the head of the agency that (1) will enable him to report his findings directly to the agency head when warranted, (2) meet with the agency head when he has problems that merit the agency head's attention, and (3) be used by the agency head to ferret out and help solve problems

the agency head is concerned about. Reporting to the highest practical level ensures that top management is made aware of problems and can take appropriate action to correct these situations.

Audit Scope Restrictions

Another aspect of independence relates to the auditors' freedom to select areas for audit. Army's auditors did not have such freedom because their plans were reviewed and revised by an Audit Inspection and Priority Committee comprised of persons responsible for operations to be audited. This practice resulted in the cancellation of audits of activities identified by the Audit Agency as needing its attention. We believe that the auditors themselves are in a better position to identify and select activities for audit and should be free to do so.

Restrictions also resulted from an Inspector General policy of not allowing Army auditors to audit combat readiness and other tactical activities. The rationale for excluding these activities from audit is that they can be better evaluated by inspections made by Inspector General personnel. This restriction was based on the premise that Inspector General personnel, by virtue of their military backgrounds, are more qualified than auditors to evaluate activities of a tactical nature. We disagree. Inspections cannot be a substitute for audits because they lack the depth of audits and therefore do not satisfy our standards for audit coverage. Restricting audits

of activities can result in problems not being identified and reported to top management, our office, and the Congress.

THE CHIEF OF THE ARMY
AUDIT AGENCY SHOULD
BE A CIVILIAN

Contrary to the intent set forth in congressional appropriation language and DOD policy, which requires all nonmilitary positions to be filled by civilians, the Audit Agency is headed by a military officer. The position of Chief of the Army Audit Agency requires skills found in the civilian community and does not require the skill factors set forth in Department of Defense criteria for using military personnel. In addition, because military officers are subject to periodic rotation, the Audit Agency has had five different military chiefs since May 1970. Based on these considerations, we concluded that the position should be filled by a qualified civilian. This arrangement not only would be consistent with Department of Defense policy but also would provide a longer tenure for incumbents of the position thus providing greater continuity to carry out management policies and procedures.

NEED FOR MORE EFFECTIVE
USE OF AUDIT STAFF

The Audit Agency devotes a considerable amount of time to work that is either not consistent with its primary mission or is not sufficiently productive.

The Audit Agency incurs substantial costs in auditing non-appropriated fund activities. These audits, while undoubtedly

needed, involve a questionable use of staff resources because they represent a free service provided at the taxpayers' expense to activities intended to be self-supporting.

The Audit Agency also spends a considerable amount of staff time on audits specifically requested by Army commanders. These audits are usually evaluations of problems already identified by requesting commands, result in reports with limited distribution and low visibility, and do not result in the correction of major problems.

We also believe that the use of auditors for audits of the American National Red Cross, although required by law, is inconsistent with the Audit Agency's primary mission.

NEED FOR MORE EFFECTIVE
FOLLOWUP ON AUDIT FINDINGS

The Army's audit followup does not insure that all deficiencies identified by internal audits are promptly corrected. Reported deficiencies sometimes are not corrected until the next scheduled audit, which may not occur for several years. In the meantime, opportunities for savings are lost and inefficient and ineffective operations continue to exist.

Presently, the Army's audit followup system is operated by the Audit Compliance Branch of the Office of the Inspector General. We believe the followup function would be strengthened by placing this responsibility with the Army Audit Agency because it would permit auditors who are already located in the field and who are familiar with reported conditions to evaluate

the adequacy of corrective actions taken.

RECOMMENDATIONS TO THE CONGRESS
AND SECRETARY OF DEFENSE

Mr. Chairman, certain of our recommendations in the Army Audit report are addressed for Congressional consideration while others are addressed to the Secretary of Defense for his action.

Specifically, we recommended that the Congress amend the National Security Act to require that the internal audit functions of the three military departments be placed under the respective Secretaries or Under Secretaries. This organizational change would provide a direct reporting channel to these top officials. We also recommended that the American National Red Cross Act of 1905 be amended to relieve DCJ of its responsibility for auditing the Red Cross financial operations.

To strengthen the Army Audit Agency, we made several recommendations to the Secretary of Defense that he direct the Secretary of the Army to:

- 1) abolish the Priority Committee;
- 2) insure that internal auditors will not be restricted in selecting activities for audit and determining the scope of audit work;
- 3) more clearly define the nature and scope of audits and inspections;
- 4) fill the position of Chief of the Army Audit Agency with a professionally qualified civilian;

- 5) reduce commander-requested audits and audits of non-appropriated fund activities; and
- 6) transfer the audit followup function from the Office of the Inspector General to the Army Audit Agency and otherwise strengthen the Army's audit followup system.

AGENCY ACTION

Mr. Chairman, the Assistant Secretary of Defense (Comptroller) responded to the recommendations in our draft report and concurred with most of them. He agreed to raise the reporting level of the Audit Agency, appoint a civilian head, abolish the Priority Committee, clarify Army regulations governing audits and inspections, and seek ways to more effectively use the audit staff.

One area of disagreement dealt with our recommendation that the audit followup function be transferred to the Audit Agency. The Assistant Secretary's comments stated that followup is a management responsibility and should remain with the Office of the Inspector General. We agree that audit followup is a management responsibility, but as the system is today, deficiencies identified by the Audit Agency are not always promptly corrected. We believe the Secretary of Defense should follow our recommendations in seeking ways to improve the followup function.

RESULTS OF OUR REVIEW OF RESOURCES OF THE DEPUTY ASSISTANT SECRETARY

Mr. Chairman, I would now like to discuss briefly our

report which addressed your concerns about the authority and resources of the Deputy Assistant Secretary of Defense for audit to provide policy and procedural direction to the military service internal audit agencies. As you know, we performed this work in accordance with your request dated February 24, 1977.

The report points out that the Deputy Assistant Secretary has a dual responsibility. As Director of the Defense Audit Service, he is responsible for conducting internal audit operations and as Deputy Assistant Secretary of Defense for audit he is responsible for Defense-wide policy and reporting.

In this latter role, we noted that the Deputy Assistant Secretary has the responsibility to develop internal audit policy and review its implementation but does not have the authority to provide policy and procedural direction to the military service internal audit agencies. Instead, the authority to provide this type of direction to the military internal audit agencies rests with the Assistant Secretary of Defense (Comptroller).

We also point out in the report that while the Deputy Assistant Secretary has sufficient resources to develop internal audit policy, he may not have sufficient resources to review its implementation.

We recommended that the Secretary of Defense take at least three steps to improve the internal audit function in the Office of the Secretary of Defense.

First, the audit policy, audit operations, and reporting function should be combined into one functional organization under the Deputy Assistant Secretary of Defense for audit.

Second, the head of the combined organization should be required to periodically review the implementation of audit policy and procedural directives by the internal audit organizations in DOD. Also, formal, written reports on policy violations should be provided directly to the Secretary or Deputy Secretary of Defense.

Lastly, careful consideration should be given to bringing the required audit workload and staff capabilities of the Defense Audit Service into balance.

This concludes my statement, Mr. Chairman, I would be pleased to answer any questions you may have.