

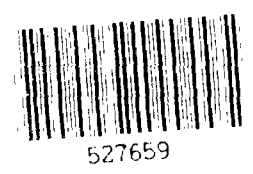
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STUDY BY THE STAFF OF THE U.S.

# General Accounting Office

## Audit Guides To Review Implementation Of The Federal Managers' Financial Integrity Act: The First Year

The Federal Managers' Financial Integrity Act imposes an important responsibility on all Government officials to strengthen internal controls. GAO's audit guides provide for (1) a comprehensive assessment of agencies' first year efforts to implement the act and (2) working in a cooperative manner with the agencies to make implementation of the act as successful and meaningful as possible.



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## PREFACE

In passing the Federal Managers' Financial Integrity Act of 1982, Congress focused attention on the need to strengthen internal controls. The 1982 act requires agencies to periodically evaluate internal control systems and the heads of executive agencies to report annually on their systems' status. The act presents an opportunity for a cooperative effort among OMB, GAO, and the agencies to improve internal controls throughout the Government.

GAO's audit guidelines are prepared for its internal use and, as a general practice, are not made available for external distribution. In this instance, limited distribution of appropriate sections of the guidelines is being made to OMB and the Inspector General, to apprise them of the key areas on which GAO will initially focus and which it believes need to be stressed in this first effort to achieve compliance with the Federal Managers' Financial Integrity Act. Any wider distribution of the guides should be made only upon approval by GAO (Director, Accounting and Financial Management Division).

We would appreciate any comments or suggestions OMB or the Inspector General may have concerning the audit guides. Any inquiries concerning the audit guides should be directed to Mr. John F. Simonette, Associate Director (telephone 275-1581).



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## INTRODUCTION

Over the years, internal controls have not been an area of management emphasis throughout the Government. Although some managers have stressed effective internal controls, the development of effective Government systems of internal control has generally been marked as a slow, painstaking process with inadequate resources allocated to the task.

The Accounting and Auditing Act of 1950 required management in each executive agency to implement and maintain effective systems of internal and accounting control. These systems were expected to help prevent fraud, waste, abuse, and mismanagement in Federal Government operations.

The 1950 act notwithstanding, the Government experienced situation after situation where illegal, unauthorized and questionable acts were characterized as fraud, waste, and abuse. Often these problems resulted from weaknesses in internal controls or from breakdowns in compliance with internal controls. Recently within the Government, attention focusing on internal controls has increased dramatically because of a number of events including budget cuts; continued disclosure of fraud, waste, and abuse; and findings of poor internal controls in Federal agencies.

In October 1981, the Office of Management and Budget (OMB) issued Circular A-123, "Internal Control Systems," to reiterate requirements that adequate systems of internal control be developed and maintained. Unlike the 1950 act, the

Circular defined requirements and responsibilities to transform expectations into reality. Included in the requirements were:

- The assignment of internal control responsibilities to specific officials throughout each agency.
- The completion of vulnerability assessments covering all agency components by December 31, 1982.
- The performance of internal control reviews on an ongoing basis.
- The establishment of administrative procedures to enforce the intended functioning of internal controls, and procedures to take necessary actions to correct internal control weaknesses on a timely basis.

Congress has supported good internal controls in the Federal Government and in September 1982 passed the Federal Managers' Financial Integrity Act of 1982, amending the 1950 act. The integrity act requires executive agency heads to report annually, beginning December 31, 1983, on their agency's compliance with internal control standards prescribed by the Comptroller General <sup>1/</sup> and the guidelines for evaluation of internal controls issued by OMB. <sup>2/</sup>

THE FEDERAL MANAGERS' FINANCIAL  
INTEGRITY ACT OF 1982

The Federal Managers' Financial Integrity Act of 1982 (the act) established a Government-wide framework for

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<sup>1</sup> Standards for Internal Controls in the Federal Government, GAO.

<sup>2</sup> Guidelines for the Evaluation of Improvement of and Reporting on Internal Control Systems in the Federal Government, OMB.



improving and monitoring the effectiveness of programmed financial management in Federal agencies. This act amends the Accounting and Auditing Act of 1950, requiring each Federal agency to establish systems of internal accounting and administrative controls that can provide reasonable assurance that (1) obligations and costs comply with applicable law; (2) funds, property, and other assets are safeguarded from waste, loss, unauthorized use, or thefts; and (3) revenues and expenditures are properly recorded, accounted for, and reported. The act also requires each agency to assess its accounting systems for compliance with principles and standards prescribed by the Comptroller General.

Systems of Internal Accounting  
and Administrative Control

The act charges the Comptroller General with prescribing internal accounting and administrative control standards to be followed by Federal agencies in establishing required control systems. The Director, Office of Management and Budget, in consultation with the Comptroller General, is to set guidelines for agencies to use in performing annual self-assessments of their systems of internal accounting and administrative controls. Finally, the act requires each Federal agency head to report to the President and the Congress annually beginning on December 31, 1983, on the status of agency systems of internal accounting and administrative control.

In their reports under the act, Federal agencies are required to (1) state whether their control systems conform to the guidelines set out by the Comptroller General, and (2) identify any control systems that do not comply with these guidelines and the plans and schedule for bringing these systems into conformance with the standards promulgated by the Comptroller General.

The concept of internal controls is defined by the GAO Standards for Internal Control in the Federal Government as:

"The plan of organization and methods and procedures adopted by management to ensure that resource use is consistent with laws, regulations, and policies; that resources are safeguarded against misuse, waste, and loss, and that reliable data are obtained, maintained, and accurately disclosed in reports."

Internal controls are an integral part of each system management uses to regulate and guide its operations.

To satisfy the act's requirements, agencies will have to continuously evaluate their systems of internal accounting and administrative controls. These systems are necessary not only for financial and administrative activities, but for program and operational activities as well. Each agency will have to develop a plan to evaluate, improve, and report on its internal control systems in the most efficient and effective manner.

The OMB guidelines provide a basic approach to evaluating, improving, and reporting on internal controls. The

guidelines recommend the following steps as one efficient, effective way to perform the required evaluations. (See Chart A on page 6.)

1. Organizing the process

Each agency must carefully organize and assign responsibilities to make sure the process is done efficiently and effectively. Primary considerations for organizing include specific assignment of responsibilities; IG's role; quality assurance over the process; internal reporting; documentation requirements; personnel and supervision; and scheduling the evaluation processes.

2. Segmenting the agency

Each agency must systematically divide the agency into units to be assessed for internal controls. (These are called "assessable units.") This is critical in making a comprehensive evaluation of an agency's internal control system.

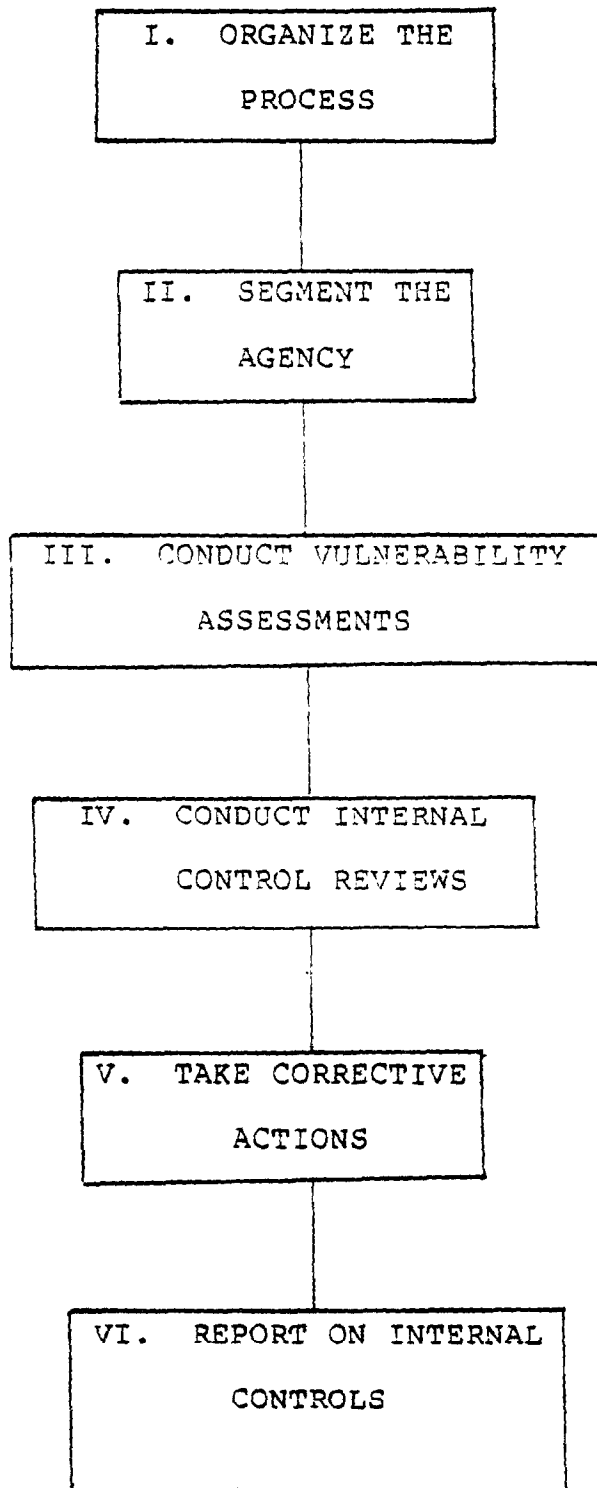
3. Conducting vulnerability assessments

Next, reviews of the susceptibility of each "assessable unit" to the occurrence of waste, loss, unauthorized use, or misappropriation will be accomplished. These reviews (called "vulnerability assessments") should enable agencies to identify either corrective actions to be taken or the areas requiring further evaluation.

4. Reviewing the internal controls

The vulnerability assessments should identify those areas with the most serious internal control problems. Resources should be focused on these areas to perform detailed examinations to determine if adequate control measures exist and what

CHART A



procedures can be implemented in a cost effective manner to provide the necessary controls.

#### 5. Taking corrective actions

After controls have been identified for implementation, procedures should exist not only to make sure corrective action is taken but also to make sure the action is effective in providing the control needed.

#### 6. Reporting

Annually, agencies must submit a report to Congress and the President by December 31 on the adequacy of internal controls and the plans to correct problems in those areas identified as "high or medium risk."

#### Accounting Systems' Compliance with the Comptroller General's Accounting Principles and Standards

In addition to the statement on the adequacy of their internal control systems, the act requires the agencies to forward to the President and the Congress a statement as to whether their accounting system conforms to the accounting principles and standards prescribed by the Comptroller General.

Although OMB has not published any guidelines to be used by the agencies in response to this requirement, it is now in the process of doing so. In the meantime, we believe the following steps should have been used by the agencies in conducting their evaluations.

#### 1. Organizing the process

Each agency must carefully organize and assign responsibilities to make sure the process is done efficiently and

effectively. Primary considerations for organizing include specific assignment of responsibilities; IG's role; quality assurance over the process; internal reporting; documentation requirements; personnel and supervision; and scheduling the compliance process.

## 2. Identification of accounting operations

Each agency must identify and systematically divide its accounting operations into systems/subsystems to be assessed for compliance with the Comptroller General's accounting principles and standards. This is a critical step in evaluating whether its system is in compliance with the prescribed accounting principles and standards.

## 3. Conducting compliance evaluations

Next, compliance evaluations of the identified systems/subsystems should be performed. These evaluations should enable the agencies to identify deviations from the principles and standards and corrective action to be taken to conform the agency's accounting system to the prescribed accounting principles and standards.

## 4. Taking corrective action

After the deviations and corrective action have been identified, procedures should be prescribed to not only make sure that action is taken to conform the system to the prescribed principles and standards, but also whether the action was effective in conforming the system to the principles and standards.

## 5. Reporting

Annually, agencies must submit a report to the Congress and the President by December 31, on the compliance of their accounting system with the Comptroller General's prescribed accounting principles and standards.

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More specific criteria, definitions, descriptions, and guidelines are enclosed as part of the work program package.

Included are:

1. Federal Managers' Financial Integrity Act of 1982.
2. OMB Circular A-123, "Internal Control Systems."
3. GAO's Standards for Internal Controls in the Federal Government.
4. OMB's Guidelines for the Evaluation and Improvement of and Reporting on Internal Control Systems in the Federal Government, December 1982.
5. Comptroller General's memo on "Statement of Accounting Principles and Standards for Federal Agencies," April 18, 1983.
6. Comptroller General's memo on "Modification of General Accounting Office Procedures with Respect to Approval of Executive Agency Accounting Systems," April 18, 1983. (Includes the definition of "Accounting Systems Subject to GAO Approval" as an enclosure.)

## WORK OBJECTIVES

The overall objectives of the assignment are to:

- Assess agencies' processes for evaluating and improving systems of internal accounting and administrative control for reporting under the act.
- Evaluate agency reports to assure that all identified material internal control weaknesses and accounting systems deviations are reported and evaluate the adequacy of plans for implementing corrective actions.
- Provide an assessment on the overall adequacy of internal accounting and administrative controls throughout the Government.

More specific work objectives are identified in the appropriate sections of the work program.



## I. PRELIMINARY AGENCY SURVEY

Our preliminary efforts in the agency will be to accumulate available general information on the agency and their initial efforts to implement the act. The core group will provide as much of this information as possible.

The audit team should meet with the core group to obtain the data the group acquired from OMB prior to contacting the agency. All additional data will have to be obtained from the agency.

### A. Obtain preliminary data and information:

#### TASKS

1. Obtain the following:
  - a. Agency mission statement.
  - b. Organization charts.
  - c. Approved Budget (fiscal year 1982 and 1983).
  - d. Functional descriptions of agency organization.
  - e. Prior GAO reports (lists for the past 2 years should be obtained from the Office of Information Systems and Services) and any other prior year significant open recommendations.
  - f. Prior IG/Internal Audit reports (lists for past 2 years) and any other prior year significant open recommendations.
  - g. Relevant documents on the agency organization for implementing the act. (Among the information obtained include the names of the senior internal control official and each component's internal control official and any internal documents supporting this effort.)

- h. Vulnerability assessment guidance, directives, procedures manual, training material, and plan.
  - i. Internal control directives, guidance, procedures manual, and training materials.
  - j. Plan and schedule for staffing to perform the internal control reviews.
  - k. Assignments of internal control responsibility.
  - l. Inventory of segments and assessable units.
  - m. Summary and analysis of completed vulnerability assessments.
  - n. Summary and analysis of completed internal control reviews.
  - o. Plan and schedule for implementation of corrective actions.
  - p. Followup system documentation.
  - q. Reporting procedures (for agency head reports).
  - r. ADP systems inventory.
  - s. Accounting systems inventory.
  - t. Consultant/Contractor studies and reports for the past 2 years.
  - u. Congressional staff reports for the past 2 years.
  - v. Congressional hearings for the past 2 years.
  - w. Guidelines for accounting systems compliance evaluations.
2. Meet with key GAO personnel with knowledge of the agency to identify known internal control weaknesses and accounting systems deficiencies.

3. Meet with key Congressional staff members to discuss their interests and concerns relating to internal controls and accounting systems in the agency.
- B. Each audit team should initiate their contacts within the agency at the highest levels responsible for the act and periodically brief those officials on progress of the assignment.

TASK

1. Determine the highest level official responsible for the agency's integrity act work and arrange for periodic briefings on the progress of the assignment.
- C. Develop an inventory of agency internal control weaknesses based on past GAO and IG work, consultant/contractor studies, Congressional staff reports, and other available information.

TASKS

1. Using the information accumulated in II A, develop an inventory of the agency's known internal control weaknesses. Primarily use the following information
  - GAO Reports
  - Inspector General/Internal Audit Reports
  - Congressional staff reports
  - Congressional hearings
  - Consultant/Contractor studies
2. Maintain contact with current GAO and IG/Internal Audit staffs doing work in the agencies to supplement the inventory of known weaknesses.

II. ORGANIZATION TO COMPLY WITH THE ACT  
BACKGROUND AND OBJECTIVES

It is critically important that Federal agencies organize in a way that will ensure that the internal control evaluation, improvement, and reporting process required by the act is conducted efficiently and effectively, and in a way that provides for quality control over the process. The overall objective for the divisional audit team's review of agency efforts to organize themselves to comply with the act is to determine if agencies have adequately organized and provided overall direction necessary to meet the internal control evaluation, improvement, and reporting requirements of the act.

In reviewing an agency's efforts to organize to comply with the act, divisional audit teams should at a minimum, determine the extent to which the following objectives have been achieved:

- A. Overall responsibility assigned to high level agency official.
- B. IG role defined to assist agency management without usurping management responsibility or IG independence.
- C. Internal reporting system provided for.
- D. Adequate documentation provided for.
- E. Quality and consistency assured on an agency-wide basis.

The following sections provide a listing of tasks for divisional audit teams to accomplish these objectives.

- A. Determine if overall responsibility for organizing and directing the process has been assigned to a high level official, i.e., Assistant Secretary level.

TASKS:

1. Determine if the internal control directive assigns overall responsibility for the agency's process to a senior level official (i.e., Assistant Secretary level).
2. Determine if the directive has been disseminated throughout the organization.
3. Determine if there is evidence of agency head commitment to internal control evaluation, improvement, and reporting.
  - a. Determine if the agency head has been involved in establishing policies and procedures to guide the agency's compliance with the act.
  - b. Determine if the agency head has been involved in establishing schedules for internal control evaluation and improvement, and in establishing schedules for information and assurances needed to support annual report.
4. Determine if the central agency official assigned overall responsibility has sufficient

authority and resources to direct and coordinate the agency process. (Refer to the GAO Standards for Internal Control in the Federal Government for criteria to apply in performing the following tasks.)

- a. Identify who was assigned overall responsibility for the internal control process and their position in the agency. Obtain a description of their Financial Integrity Act responsibilities and comment on whether the responsibility was assigned at an appropriate level (i.e., to an individual with adequate authority and appropriate management skills.)
- b. Determine if the central agency official assigned overall responsibility for the process has authority to resolve intra-agency conflicts, and to ensure cross-agency quality and consistency. If not, how will these issues be resolved?
- c. Determine if the central agency official assigned overall responsibility for the process has staff support to monitor and provide guidance, technical assistance, and training and to evaluate, summarize, and process results on an agency-wide basis.

- d. Determine if the central agency official has provided guidance, technical assistance and training to responsible internal control managers commensurate with their internal control responsibilities.
- B. Determine if agency policies and procedures define the Inspector General (IG), or equivalents' role, in a way that will facilitate management's implementation of the act.

TASKS:

1. Determine if agency policies and procedures define a role for the IG, or equivalent, to provide technical assistance to agency management's internal control process.
  - a. Determine if agency policies and procedures define a role for the IG, or equivalent, to provide
    - training,
    - vulnerability assessment methodology development, and
    - internal control review methodology deveopment.
  - b. Determine if agency policies and procedures define the IG technical assistance role in a way that recognizes management's primary responsibility.

2. Determine if agency policies and procedures define the IG, or equivalent's, role in providing comments as to whether management's internal control evaluation process has been conducted in accordance with OMB guidelines.
  - a. Describe the review process the IG plans to use to provide a basis for IG comments on management's compliance with OMB guidelines.
  - b. Determine whether the IG has summarized and updated past audit work to identify current material weaknesses in agency internal control systems that should be included in the agency's annual report.
3. Determine if plans exist to coordinate the IG, or equivalent's, separate reviews of internal controls with agency management's internal control evaluation, improvement and reporting process.
  - a. Determine if the IG's audit plans consider management's plans and schedules for conducting vulnerability assessments and internal control reviews.
  - b. In instances where both management and the IG plan to review certain agency activities, describe how the IG plans to carryout its reviews in a way that will help accomplish



the evaluation required by OMB guidelines and avoid duplication of work.

- C. Determine if internal reporting and followup systems have been provided for to monitor the vulnerability assessments, internal control reviews, and internal control improvement processes.

TASKS:

1. Determine if policies and procedures exist to:
  - a. Schedule and monitor completion of corrective actions resulting from vulnerability assessments and internal control reviews.
  - b. Summarize evaluative information to support annual statement.
  - c. Gather other data necessary to improve internal controls (e.g., status of training, impact on performance appraisals, other personnel actions).

D. Determine if adequate documentation has been provided for in agency's policy for its internal control evaluation, improvement, and reporting process. (See vulnerability assessment and internal control review sections for detailed documentation requirements in these areas.)

TASKS:

1. Determine if policies and procedures provide for documentation of the methods used, personnel in-

volved and their roles, and conclusions reached in the internal control evaluation process. If not, determine how the agency plans to assure itself that OMB guidelines were complied with on a consistent basis.

2. Determine if policies and procedures provide that documentation supporting internal control evaluation and improvement process be maintained and made available upon the request of the IG or GAO. If not, determine how the agency plans to assure itself that OMB guidelines were complied with on a consistent basis.

- E. Determine what agency policies and procedures exist to assure quality and consistency in the agency's internal control evaluation, improvement and reporting process.

TASKS:

1. Determine if agency policies and procedures define a role for the IG in the agency quality assurance process. (If not, identify and define how the agency plans to assure a quality process.)
2. Identify the criteria the agency plans to use to measure quality and consistency in its internal control evaluation, improvement, and reporting process on an agency-wide basis.

### III. SEGMENTING THE AGENCY

OMB guidelines suggest that the most effective way to systematically perform an evaluation of agency systems is to segment the agency first into organizational or other components and then into the programs and administrative functions within each component. The guidelines also state that there is no single method to divide an agency into components, programs, and administrative functions for purposes of evaluating the system of internal control; particularly since agencies vary so widely in organizational structure and the nature of activities conducted. The basic goal of the division is to develop an agency-wide inventory of "assessable units,"<sup>3/</sup> each of which could be the subject of a vulnerability assessment. This inventory should provide complete coverage of all program and administrative functions. The individual assessable units should be of an appropriate nature and size to facilitate the conduct of meaningful vulnerability assessments.

OMB suggests that, in developing the inventory of assessable units, reference should be made to such sources of information as the agency's budget and related materials, organization charts, agency manuals, and program and financial management information systems. The following specific factors should be considered:

--Existing organizational structure.

<sup>3/</sup>OMB's definition of "assessable unit" is a program or administration function or subdivision thereof which is to be the subject of a vulnerability assessment.

- Nature and size of the agency's programs and administrative functions.
- Numbers of sub-programs or sub-functions in a program or function.
- Number of separate organizations operating the program.
- Degree of independence of the program or function.
- Differences in operating systems.
- Degree of centralization or decentralization.
- Budget levels.
- Numbers of personnel.

The degrees of independence and centralization/decentralization are very significant. A program or administrative function could operate in several locations. Since the program or administrative function and internal control system may vary among locations--in design and/or operation--it may be necessary to perform separate vulnerability assessments and/or internal control reviews for each location.

Also, it should be remembered that the purpose of the review is to evaluate and improve the internal controls for operating programs and administrative functions. Policymaking activities are not subject to the guidelines and should not be included in the inventory, according to OMB.

Once the agency inventory of assessable units has been developed, the information should be documented. The documentation provides the means for organizing and managing the evaluation process.

The definitions of segments and assessable units are not specific and agencies have a lot of flexibility in interpreting and implementing the OMB guidelines in this respect. We need to document how agencies implemented OMB's guidelines and determine whether the agencies segmented comprehensively to cover all organizations' components, programs, operations, and functions.

- A. Determine whether the agency has identified its segments and assessable units in a comprehensive manner and give an overall evaluation as to whether the agency covered all organizational components, operations, functions, and programs as required by GAO's internal control standards.

TASKS:

1. Determine the agency's definition for segments.
2. Obtain a copy of the agency's inventory of segments.
3. Determine whether segments were entities that had a specific responsible manager. If so, determine whether these managers were held responsible for internal controls in SES contracts, performance evaluations, ratings, or other methods.
4. Describe how the agency divided into segments and obtain the agency's documentation of its process for dividing into segments. If the

process is not documented, interview responsible agency officials to determine how the segments were formulated.

5. Determine whether the agency's inventory of segments covers all organizations, programs, operations, and functions.
  - a. Using the organization chart for the agency, determine if all activities on the chart have been included within the inventory of segments.
  - b. Using the agency's budget, determine whether the agency's inventory of segments included all activities and functions for which it was provided funds.
  - c. Note major omissions, particularly in agency management and program management.
6. Determine the agency's definition for assessable units.
7. Obtain a copy of the agency's inventory of assessable units and determine how many assessable units are in the agency's inventory.
8. Determine whether the agency has organized its inventory of assessable units in a way that enables senior managers to perform vulnerability assessments for all their areas of responsibility.
9. Determine whether assessable units were entities that had a specific responsible manager. If so,

determine whether the managers were held responsible for internal controls in SES contracts, performance evaluations, ratings, or other methods.

10. Describe how the agency divided into assessable units and obtain the agency's documentation of its process for identifying assessable units. If the process is not documented, interview responsible agency officials to determine how the assessable units were formulated.
11. Determine whether the agency's inventory of assessable units covers all organizations, programs, operations, and functions.
  - a. Using the agency's organization chart, determine if all activities have been covered by the inventory of assessable units.
  - b. Using the agency's budget, determine whether the agency's inventory of assessable units included all activities and functions for which it was provided funds.
12. Determine whether the agency has established procedures to update its inventory of assessable units for such events as reorganization and changes in mission.
13. Using the inventory of internal control weaknesses developed in the preliminary agency survey, categorize the weaknesses for which the

agency has not taken corrective action. The categories used should be the agency's major segments for which the results of their vulnerability assessments will be "rolled up" and summarized.

14. Give an overall evaluation as to whether the agency's segmenting process covered all of its programs, functions, components, and operations.

B. Prepare a referenced summary.

TASK:

Prepare a referenced summary covering the steps in the organization and segmenting sections of the work program. This summary should evaluate the agency's efforts to organize and segment themselves to meet the requirements of the act in accordance with GAO methodology and procedures. This summary should be submitted to the core group no later than August 31, 1983.



#### IV. AGENCY PERFORMANCE OF VULNERABILITY ASSESSMENTS

The OMB defines a vulnerability assessment as a review of the susceptibility of a program or function to the occurrence of waste, loss, unauthorized use, or misappropriation. More specifically, a vulnerability assessment is intended to determine the likelihood that situations exist in which:

- Obligations and cost comply with applicable law,
- All assets are safeguarded against waste, loss, unauthorized use, and misappropriation; and
- Revenues and expenditures applicable to agency operations are recorded and accounted for properly so that accounts and reliable financial and statistical reports may be prepared and accountability of the assets may be maintained.

GAO's standards point out that agencies, in assessing their internal controls, should

- Identify (1) risks inherent in agency operations, (2) criteria for determining low, medium, and high risks, and (3) acceptable levels of risks under varying circumstances.
- Assess risks both quantitatively and qualitatively.

As indicated, however, the internal control evaluation process does not stop with vulnerability assessments since, by themselves, vulnerability assessments do not necessarily identify weaknesses or result in improvements. Rather, vulnerability assessments are the mechanism with which an agency can determine the relative potential for loss in these programs

and functions. Then, after giving consideration to such relevant factors as management priorities, resource constraints, etc., the agency can schedule internal control reviews or corrective actions. The internal control reviews provide a more indepth analysis to identify, plan, and implement corrective actions. Internal control reviews and corrective actions are covered in other parts of this work program.

Chapter IV of OMB's "Guidelines for the Evaluation and Improvement of and Reporting On Internal Control systems in the Federal Government," December, 1982, contains the specific criteria to perform vulnerability assessments. These criteria should be used by the auditor performing the tasks in this section. Also, the auditor should be familiar with the agency organization and segmenting for its internal control evaluation. Most importantly, the auditor should determine whether GAO's internal control standards are being followed by the agency.

In reviewing the vulnerability assessments performed by the agency, several steps require the auditor to reach conclusions based on limited review. These steps should be performed concurrently to the extent feasible. Our overall objective is to evaluate agencies' reviews of their susceptibility to waste, loss, unauthorized use, or misappropriation.

- A. Determine the adequacy of documentation required for vulnerability assessments.

TASKS:

1. Determine whether the agency's prescribed procedures require sufficient documentation of vulnerability assessments to provide an audit trail showing the criteria used in performing the assessments and the agency's rationale for the vulnerability assessment rating. Determine if the guidance:
  - a. Is clear and adequate as to how the results of the assessments are to be documented.
  - b. Requires a description of the assessable unit, the program and administrative function involved, and the organization involved.
  - c. Requires identification of the personnel performing and reviewing the assessments, approving the results and the responsible manager of the controls assessed.
  - d. Requires a narrative description of the methodology used in performing the vulnerability assessments and in arriving at the overall ratings for the assessable units. This description should include: how the agency analyzed the general control environment, analyzed inherent risk, and made a preliminary assessment of safeguards.

- e. Requires a description of the organizational segments involved and their relation to the assessable unit being rated.
  - f. Provides standardized criteria for determining the vulnerability of assessable units.
  - g. Provides for standardized reporting of vulnerability assessments' results.
  - h. Describes the process for summarizing results.
  - i. Identifies the organizational unit/person to which the vulnerability assessment results will be reported.
  - j. Describes the Inspector General's or equivalent's role in the vulnerability assessment process.
  - k. Describes the quality assurance procedures for assuring the adequacy and consistency of documentation for vulnerability assessments.
  - l. Includes provisions for the documentation of conclusions reached in performing vulnerability assessments.
2. Based on a limited review of vulnerability assessments, determine whether the agency's documentation efforts were implemented in accordance with the OMB and agency's written guidelines.

3. Based on a limited review of the vulnerability assessments, reach and document conclusions on your overall evaluation of whether the vulnerability assessments were documented adequately, consistently, and timely. This step is critical to the overall evaluation of vulnerability assessments. The work necessary to accomplish this step will vary by agency.
- B. Determine whether the training provide to personnel performing the assessments was appropriate and at what level the vulnerability assessments were performed.

TASKS:

1. Determine whether any formal training was provided to personnel who were to perform the vulnerability assessments.
  - a. Determine the number of the hours of training provided each person.
  - b. Determine who provided the training.
  - c. Describe the training, tell who was provided training, and give an overall evaluation as to whether the training was:
    - timely;
    - covered the material in OMB's guidelines;
    - explained the agency's organization, segmenting, and vulnerability assessment performance procedures;

--explained the agency's vulnerability assessment documentation and reporting procedures; and  
--covered GAO's internal control standards.

2. Determine who performed the vulnerability assessments. The personnel performing the assessments should be knowledgeable in the areas which they assess.
  - a. Prepare a schedule showing approximately what percent of the assessments were performed by (a) Comptroller, Accounting, or Financial Management personnel; (b) internal audit and Inspector General<sup>4/</sup> staffs; (c) management analysts and quality assurance personnel; (d) outside consulting firms or CPA firms; (e) managers of the function being reviewed; (f) managers from functions other than that being reviewed; (g) others--describe and list each separately with percentages.
  - b. Comment on whether personnel who performed the assessments were knowledgeable in the areas they were assessing and had some knowledge of internal controls and control techniques.

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<sup>4/</sup>Does not include military service Inspectors General.

- c. After determining to what extent Inspector General 5/ or internal audit staffs were involved in the vulnerability assessment process, comment on whether they have provided guidance and assistance. Describe the assistance and guidance provided. If they actually performed any of the assessments, document this fact and discuss with agency officials to obtain and document their rationale for this approach.
3. Describe at what level (the lowest level) vulnerability assessments were performed (e.g., headquarters level, division level, office level, etc.).
  - a. Explain whether the level described is first tier, second tier, third tier, etc. (e.g. headquarters, the highest level, would be first tier).
  - b. Arrive at an overall evaluation as to whether the level seems appropriate using (1) results of the work performed in the section on segmenting the agency and (2) discussions with agency officials. Document your overall conclusion as to whether the level at which the assessments were performed was appropriate. The senior advisors should be consulted before the auditor takes

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5/Does not include military service Inspectors General.

exception to the agency's approach. This will help assure a consistent GAO position at all agencies being reviewed.

- C. Determine whether the methodology used to conduct the assessments was appropriate and in accordance with OMB's guidelines.

TASKS:

1. Obtain the guidance issued by the agency to personnel who performed vulnerability assessments and determine whether the guidance conformed within OMB's guidelines.
  - a. Determine whether the guidance requires an assessment of the general control environment which considers:
    - management attitude,
    - organizational structure,
    - personnel,
    - delegation & communication of authority and responsibility,
    - policies and procedures,
    - budgeting and reporting practices,
    - organizational checks & balances, and
    - ADP considerations.
  - b. Determine whether the guidance requires an assessment of the "inherent risk" to waste, loss, unauthorized use, or misappropriation which considers the assessable unit's
    - purpose and characteristics,



- budget level,
- impact outside the agency,
- age and life expectancy,
- degree of centralization,
- special concerns,
- prior reviews (GAO, IG and others),
- and
- management responsiveness.

c. Determine whether the guidance requires a preliminary evaluation of safeguards within the assessable unit and determine if this evaluation

- represents a preliminary judgment of whether appropriate controls are in place to prevent, or at least minimize, waste, loss, unauthorized use, or misappropriation;
- is based on a working knowledge of "assessable unit's" operation; and
- is not an in-depth review of existing controls at this stage.

d. Determine whether the guidance requires that the vulnerability assessment results be

- summarized into an overall vulnerability rating for each segment in an agency,

--adequately documented, and  
--done consistently throughout the  
entire organization.

e. Determine whether the guidance provides quality assurance procedures for performing and reporting results of vulnerability assessments. These procedures should include provisions for:

--reviews to assure consistency, timeliness, adequacy and accuracy;  
--selective validation of the results of vulnerability assessments; and  
--redoing vulnerability assessments that were found to be inadequate.

2. Document the following information.

- a. The cutoff date established for completing the first series of vulnerability assessments.
- b. Number of vulnerability assessments performed. This should be the same as the number of assessable units identified in the work program section on segmenting. Document any differences in the number of assessable units and the number of vulnerability assessments performed. Discuss the differences with agency officials to obtain and

document their reasons for not performing vulnerability assessments for all assessable units.

c. Number of units assessed as

--high risk (list areas),

--medium risk (list areas), and

--low risk (list areas).

d. Total staff days and dollar resources expended performing vulnerability assessments (if available).

3. Determine if the agency placed any constraints (dollar amount, staff day limitations, etc.) on the level of effort to be consumed on vulnerability assessments.

4. Determine what level of effort was involved in a limited number of vulnerability assessments.

Determine

--dollars,

--staff days,

--timeframe (from/to).

5. Based on a limited review of vulnerability assessments and discussions with a limited number of personnel who performed the assessments, perform the following:

a. Give an overall assessment as to whether the agency's guidance (1) was a reiteration of the OMB guidelines, (2) was an expansion on

OMB guidelines to provide adequate guidance specifically tailored to the agency's needs and was in accordance with GAO's internal control standards, or (3) omitted significant points addressed in OMB's guidelines or GAO's internal control standards (if so, list and explain).

- b. Determine when the agency published its guidelines and whether personnel who performed the vulnerability assessments felt that the guidance was adequate and timely.
- c. Describe the agency's vulnerability assessment process as it was actually implemented and comment on whether the process was accomplished in accordance with OMB and agency guidelines.
- d. Determine whether personnel who performed the assessments felt that they were given adequate time and resources to perform good assessments. Discuss results with agency officials and document your overall conclusion as to the adequacy of time and resources.
- e. Describe the process for quality assurance over the assessments and comment on whether

it seemed adequate to assure consistent performance and reporting for vulnerability assessments .

f. Arrive at, and document your overall evaluation of whether vulnerability assessments were performed

- adequately,
- consistently,
- timely,
- in accordance with GAO's internal control standards,
- in accordance with agency guidance, and
- in accordance with OMB guidance.

If the agency's written procedures vary from the actual methodology used, discuss with agency officials, address these variances in your assessment, and to the extent feasible explain why they occurred.

D. Determine how vulnerability assessment results were reported and determine what actions resulted from the assessments. This information will be used in the work program sections dealing with internal control reviews and first year reporting.

TASKS:

1. Describe the process used to report results of the vulnerability assessments (along functional

lines, organizational lines, etc.)

Note: Reporting may occur through normal channels even though assessments are done by programs or functional areas.

2. Determine how and to whom the vulnerability assessment results were reported.
3. Determine whether the vulnerability assessment results were reported systematically and consistently (i.e., did they address the same factors, were they reported to the same group or individual, and were they presented in the same amount and level of detail).
4. Determine and list the actions taken as a result of vulnerability assessments (e.g., how many internal control reviews were planned and were any corrective actions taken or other actions planned or taken). This information will be used in the work program sections on internal control reviews, followup actions, and reporting.
5. Determine plans for future vulnerability assessments.
  - a. Determine if additional guidance is to be developed.
  - b. Determine when future vulnerability assessments are planned.

- c. Determine how often vulnerability assessments will be performed.
  - d. Describe the agency's future plans, including approach and organization for performing vulnerability assessments.
  - e. If the agency has not developed these plans, this step should be performed later. For this reason, it is repeated in the section on agency follow-up systems.
6. Compare the segments rated as having "high or medium vulnerability" by the agency to the listings of GAO and IG reports, Congressional hearings, and contractor studies. Give a preliminary assessment of which areas were not identified as high or medium risk which possibly should have been. Notify the senior advisors of these areas to discuss our plans for future work.
- E. Prepare a referenced summary.

**TASK:**

Prepare a referenced summary covering the steps in this section of the work program in accordance with GAO methodology and procedures and give an overall evaluation of the adequacy of the vulnerability assessments and submit it to the core group not later than September 30, 1983.

V. AGENCY PERFORMANCE OF INTERNAL CONTROL REVIEWS

After agencies perform vulnerability assessments, they are to develop a plan and schedule for performing detailed internal control reviews. The plan and schedule should take into consideration the agencies' highest risks and most critical areas as indicated by the vulnerability assessment results. The auditor performing this segment must become familiar with OMB's Internal Control Guidelines (December 1982), GAO's Internal Control Standards, and the work performed in prior sections of this work program, especially that dealing with vulnerability assessments.

GAO defines internal controls as the plan of organization and methods and procedures adopted by management to ensure that resource use is consistent with laws, regulations, and policies; that resources are safeguarded against misuse, waste, and loss; and that reliable data are obtained, maintained, and accurately disclosed in reports.

The ultimate responsibility for good internal controls rests with management. Internal controls should not be looked upon as separate, specialized systems within an agency. Rather, they should be recognized as an integral part of each system that management uses to regulate and guide its operations. In this sense, internal controls are management controls.

GAO's standards require, among other things, that internal control objectives are to be identified or developed for each agency activity and are to be logical, applicable, and reasonably complete.



One GAO standard requires that objectives be tailored to an agency's operations. All operations of an agency can generally be grouped into one or more categories called cycles. Cycles comprise all specific activities (such as identifying, classifying, recording, and reporting information) required to process a particular transaction or event. Cycles should be compatible with an agency's organization and division or responsibilities.

Cycles can be categorized as one of four types: (1) agency management, (2) financial, (3) program (operational), and (4) administrative.

Agency management cycles cover the overall policy and planning, organization, data processing, and audit functions. Financial cycles cover the traditional control areas concerned with the flow of funds (income and disbursements), related assets, and financial information. Program (operational) cycles are those agency activities that relate to the mission(s) of the agency and which are peculiar to a specific agency. Administrative cycles are those agency activities providing support to the agency's primary mission, such as library services, mail processing and delivery, and printing. The four types of cycles obviously interact, and controls over this interaction must be established. For example, a typical grant cycle would be concerned with eligibility and, if awarded, administration of the grant. At the time of award, the grant (program) and disbursement (financial) cycles would interface to control and record the payment authorization.

Complying with this standard calls for identifying the cycles of agency operations and analyzing each in detail to develop the cycle control objectives. These are the internal control goals or targets to be achieved in each cycle. The objectives should be tailored to fit the specific operations in each agency and be consistent with the overall objectives of internal controls as set forth in the Federal Managers' Financial Integrity Act.

In appendix B of its "Guidelines for the Evaluation and Improvement of and Reporting on Internal Controls Systems in the Federal Government," OMB has provided a suggested list of agency cycles and cycle control objectives. Agencies should consider this and other sources when identifying their cycles and cycle control objectives.

Internal control techniques are the mechanisms by which control objectives are achieved. Techniques include, but are not limited to, such things as specific policies, procedures, plans of organization (including separation of duties), and physical arrangements (such as locks and fire alarms). This standard requires that internal control techniques continually provide a high degree of assurance that the internal control objectives are being achieved.

Agencies should generally follow OMB's guidelines for performing internal control reviews and comply with GAO's internal control standards.

OMB defines an internal control review as a detailed examination of a system of internal control to determine whether adequate control measures exist and are implemented to prevent or detect the occurrence of potential risks in a cost effective manner. OMB recommends six steps for performing internal control reviews:

- identification of event cycles,
- analysis of the general control environment,
- documentation of the event cycle,
- evaluation of the internal controls within the event cycle,
- testing of the internal controls, and
- reporting the results.

OMB's guidelines describe how to perform these steps. Internal control reviews and reports, like vulnerability assessments, are not an end in themselves. The recommendations derived from these reviews should be considered by management on a timely basis and corrective actions should be planned and taken as soon as possible. A formal followup system should be established to monitor these actions. This will be covered in another part of this work program.

Our overall objective in this section is to evaluate the adequacy of agencies' processes and plans for performing detailed reviews to identify actions needed to correct weaknesses in systems of internal accounting and administrative control.

- A. Determine the adequacy of the documentation required for internal control reviews.

TASKS:

1. Determine what written guidelines were issued concerning the preparation of and maintenance of adequate documentation on the internal control review results. Determine if the guidance
  - a. is clear and adequate as to how the results of the reviews are to be documented;
  - b. requires a description of the assessable unit or other entity being reviewed, the program or administrative function and organization involved;
  - c. requires a description of the objectives, scope, and methodology used in the internal control reviews;
  - d. requires a description of the organizational segments involved and their roles in the performance of internal control reviews;
  - e. requires a description of what criteria, including internal control standards and objectives, were used in performing the internal control reviews;
  - f. requires a description of which internal control standards were not complied with and which objectives were not met;

- g. includes provisions for the documentation of conclusions reached and additional actions planned as a result of performing internal control reviews;
  - h. describes the organizational unit/person to which the internal control review results will be reported;
  - i. describes the summarization and reporting process and provides standard reporting requirements;
  - j. describes the role of the Inspector General or equivalent in the internal control review process;
  - k. describes the person responsible for taking corrective action;
  - l. describes the quality assurance procedures for assuring the adequacy and consistency of documentation for internal control reviews;
  - m. requires identification of the personnel performing the reviews, approving the results, and the responsible manager for the controls reviewed; and
  - n. requires a description of the event cycles identified for review.
2. Review a limited number of internal control reviews to determine whether the agency's documentation efforts were implemented in accordance with OMB's and the agency's written guidelines.

3. Reach and document conclusions on your overall evaluation of whether internal control reviews performed to date were documented adequately, consistently and timely.
- B. Determine what training and guidance will be provided to personnel performing reviews and who will perform the reviews.

TASKS:

1. Determine whether any formal training was or will be provided to personnel who are to perform the reviews.
  - a. Determine the number of hours of training provided to each person.
  - b. Determine who provided the training.
  - c. Describe the training content, tell who was provided training, and give an overall evaluation as to whether the training was:
    - timely,
    - covered the material in OMB's guidelines,
    - explained the agency's internal control review procedures,
    - explained the agency's internal control review documentation and reporting procedures, and
    - covered GAO's internal control standards.
2. Determine who will perform the internal control reviews. The personnel performing the reviews should be knowledgeable in the areas which they

review. They should also have knowledge of the application of internal controls and control techniques.

- a. Prepare a schedule showing approximately what percent of the reviews will be performed by (a) Comptroller, Accounting, or Financial Management personnel (b) internal audit and Inspector General<sup>6/</sup> staffs, (c) management analysts and quality assurance personnel, (d) outside consulting firms, CPA firms, (e) managers of the function being reviewed, (f) managers from functions other than that being reviewed, or (g) others-- describe and list each separately with percentages.
- b. Comment on whether personnel performing the internal control reviews were knowledgeable in the areas they were reviewing and had knowledge of internal controls and control techniques.
- c. After determining to what extent Inspector General or internal audit staffs will be involved in the internal control review process, comment on whether they have provided guidance and assistance. Describe

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<sup>6/</sup>Does not include military service Inspectors General.

the assistance and guidance provided. If they actually performed any of the reviews, document this fact and discuss with agency officials to obtain and document their rationale for this approach.

- C. Determine how the agency scheduled and planned internal control reviews based on the results of vulnerability assessments and whether they followed OMB's guidelines when performing the reviews. Agencies should develop specific plans with timeframes for completing internal control reviews. These plans should establish priorities for reviewing high risk or critical areas first, if feasible.

TASKS:

1. Determine how the agency planned and scheduled internal control reviews.
  - a. Determine whether the planned reviews are based on the results of adequate vulnerability assessments which were performed in accordance with OMB guidelines. This step will require the auditor to become familiar with the results of our analysis of the agency's vulnerability assessments.
  - b. If we concluded that the vulnerability assessments were incomplete, determine whether the agency had some other



adequate basis for planning internal control reviews and describe their basis.

- c. If we considered the agency's vulnerability assessments to be comprehensive, comment on whether the agencies internal control review plans and schedule seem logical based on results of the vulnerability assessments. Determine whether

--areas within each category (high, medium, or low vulnerability) were ranked so that areas with the highest vulnerability within each category could be identified;

--areas with a high vulnerability rating were scheduled for review first, to the extent feasible;

--personnel resources available for performing the reviews were identified; and

--reporting timeframes and milestones were established.

- d. Given the agency's resource constraints, comment on whether their plans and schedule for completing internal control reviews seem reasonable. This will be a very subjective evaluation but should be based on as much factual information as is available.

2. Compare the agencies internal control review procedures manual to OMB's Guidelines for performing internal control reviews and to GAO's internal control standards.
  - a. Determine if all key elements in OMB's guidelines are included in the agency's manual. List any items excluded from the agency's manual and determine whether the internal control procedures manual requires:
    - Internal control reviews to be performed with the objectives of providing reasonable assurance that: obligations and costs comply with applicable law; funds, property, and other assets are safeguarded against waste, loss, unauthorized use, or misappropriation; and revenues and expenditures are properly recorded and accounted for.
    - Identification of the event cycles for the internal control review process.
    - Analysis of the general control environment which can draw upon knowledge obtained when performing vulnerability assessments.

- Documentation of the event cycles and all the procedures, forms, personnel, and processing which make up the cycles.
- Identification of control objectives for the event cycles with an explanation of typical control objectives for the agency's major types of activity.
- Examination of documentation to determine whether specific internal control techniques are supposed to be in place.
- Identification of key control techniques that must work to effectively meet control objectives.
- Testing of internal controls where control techniques are either critical or seem to be inadequate for achieving the internal control objectives.
- Identification of potential ways that internal control weaknesses can be corrected.
- An assessment of whether internal controls comply with internal control standards established by GAO.

- b. Determine whether the agency adequately complied with GAO's internal control standards in performing its internal control reviews.
3. Document the following information:
  - a. The number of internal control reviews completed (as of September 30, 1983).
  - b. The number of internal control reviews scheduled to be completed by December 31, 1983.
  - c. The number of areas identified as high risk (refer to results of work program section on vulnerability assessments) for which (1) internal control reviews were completed as of September 30, 1983, (2) internal control reviews are scheduled to be completed by December 31, 1983, and (3) internal control reviews in process October 31, 1983.
  - d. Prepare a schedule showing when the agency will perform detailed internal control reviews for its high risk areas and when the agency plans to complete its reviews of all high risk areas.
  - e. Total staff days and resources to be expended performing internal control reviews during (1) fiscal 1983, and (2) fiscal 1984.
4. Determine if the agency placed any constraints (dollar amount, staff day limitations, etc.) on the level of effort to be consumed on internal control reviews.

5. Determine what level of effort was involved in a limited number of internal control reviews.

Determine

- dollars,
- staff days, and
- timeframe (from/to).

6. Based on a limited review of internal control reviews and discussions with a limited number of personnel who performed the reviews, perform the following:

- a. Give an overall assessment as to whether the agency's guidance (1) was a reiteration of the OMB guidelines, (2) was an expansion on OMB guidelines to provide adequate guidance specifically tailored to the agency's needs, and included GAO's internal control standards, or (3) omitted significant points addressed in OMB's guidelines or GAO's internal control standards (if so, list and explain).
- b. Determine when the agency published its guidelines and comment on whether personnel who performed the internal control reviews felt that the guidance was adequate and timely.
- c. Determine whether personnel who performed the internal control reviews felt that they were given adequate time and resources to perform good reviews. Discuss results with

agency officials and document your overall conclusion as to the adequacy of time and resources.

- d. Describe the agency's internal control review process and arrive at, and document your overall evaluation of whether internal control reviews were performed

--adequately,

--consistently,

--timely,

--in accordance with agency guidance,

and

--in accordance with OMB guidance.

If the agency's written procedures vary from the actual methodology used, discuss with agency officials, and address these variances in your assessment, explaining why they occurred to the extent feasible.

- e. Compare the areas for which the agency performed internal control reviews to our inventory of known internal control weaknesses previously developed from past GAO reports, IG reports, etc. Determine if the agency's reviews of those areas covered the weaknesses in our inventory. Document any significant omissions and notify the core group.

- D. Determine how the internal control review results will be consolidated and reported and determine what

actions are planned as a result of the reviews. This information will be used in the work program section dealing with agency followup on corrective actions.

TASKS:

1. Describe the process used to report results of internal control reviews and any plans to consolidate results of reviews.
2. Determine how and to whom internal control review results will be reported and comment on whether results will be reported to an individual that has responsibility and authority for assuring that results are followed up on and appropriate action is taken to correct deficiencies.
  - a. Indicate any sub-levels where the reports are reviewed and revised prior to being finalized.
  - b. Determine the extent to which review results are or can be revised prior to finalization. Make an overall assessment as to whether these revisions can or have resulted in "watered down" reports.
3. Determine whether the internal control review results were reported systematically and consistently.
  - a. Determine whether a standard format and method was established for reporting.

- b. Determine whether reports addressed the deficiencies as they related to GAO's internal control standards and OMB's guidelines.
  - c. Determine whether reports were presented in the same amount and level of detail.
- 4. Determine whether review results were reported in accordance with:
    - a. Agency guidelines, and
    - b. OMB guidelines.
  - 5. Based upon the internal control reviews performed, give an overall assessment of whether the agency's internal control review plans and procedures (1) will provide the agency with useful, timely reports and information for improving or establishing essential internal controls for its highly vulnerable or critical programs and functions; and (2) are conducive to establishing a good followup and tracking system.
  - 6. Determine and list actions taken as a result of internal control reviews (eg. corrective actions).
- E. Prepare a referenced summary.

TASK:

Prepare a referenced summary covering the steps in this section of the work program and give an overall evaluation of the adequacy of the internal control reviews in accordance with GAO methodology and procedures and submit it to the core group not later than October 31, 1983.



VI. EVALUATING AGENCIES' REPORTING ON INTERNAL CONTROL UNDER THE FEDERAL MANAGERS' FINANCIAL INTEGRITY ACT.

The act's reporting requirements bring strong focus on agency head's responsibility and accountability for establishing and operating effective systems of internal control.

First, the act requires a statement from each agency head to the President and to the Congress as to whether the agency has established a system of internal accounting and administrative control in accordance with standards prescribed by the Comptroller General and whether this system provides reasonable assurance that:

- Obligations and costs are in accordance with applicable law;
- Funds, property and other assets are safeguarded against waste, loss, unauthorized use, or misappropriation; and
- Revenues and expenditures are properly recorded and permit the preparation of reliable financial and statistical reports.

Second, the act requires each agency to submit to the President and the Congress a report listing identified material weaknesses in internal accounting and administrative control as well as a plan and schedule for their correction.

Our primary goal under this work segment is to evaluate whether agencies' reports identify all known material internal control weaknesses and provide for adequate plans for implementing corrective actions. Our specific objectives in evaluating the reports are to:

1. Determine whether the statement identifies all known material weaknesses in internal control.
2. Ascertain whether agency head has an adequate basis for making the required statement.
3. Assess the adequacy of the plans and schedule for correcting identified material internal control weaknesses.
4. Determine whether statement's wording provides the information and assurance required by the act.

To accomplish these objectives, we will need to determine the agency's reporting plans as early as possible before the required report is issued. Using data and information obtained during the preliminary survey and our performance of previous work steps, we will identify potential omissions of significant internal control weaknesses from the report and discuss these with appropriate agency officials to clarify the discrepancies as early as possible.

Identification of these omissions will be done by relying on prior audit reports, Congressional hearings, etc.; and the knowledge GAO has of the agency and its operations. Discrepancies that we plan to discuss with the agency should be discussed with the senior advisors prior to meeting with agency officials.

Our objectives are to either convince the agency to include significant internal control weakness in their report or clarify why the weaknesses will not be included. This initial effort is obviously contingent upon agency cooperation.

We need to document the issues not to be included and the agency justifications. Also, we plan to review plans for corrective actions for selected significant internal control issues which will be included in the agency's report. These should be coordinated with the senior advisors.

Timely completion of this work is essential for two reasons. First, GAO must be in a position to provide meaningful advice to the agency before the yearend report is issued. Secondly, the bulk of this work must be finalized in early January to meet the assignment's milestones.

Determining the scope of work under this section is critical and coordination with the senior advisors in making the scoping decisions is imperative for consistency and appropriateness.

- A. Determine whether the agency reported all identified material internal control weaknesses. Accomplishment of this objective will require (1) using data from our inventory of known internal control weaknesses previously developed from past GAO reports, IG reports, etc.; (2) evaluating the data to determine the weaknesses' significance, materiality, and the degree of corrective action taken; (3) determining whether the agency head intends to include such weaknesses in his report; and (4) reaching a conclusion on whether all material weaknesses are reported as required by the act.

**TASKS:**

1. Develop an inventory of known internal control weaknesses.
  - a. Using data accumulated in the Preliminary Agency Survey, identify and categorize internal control weaknesses that we believe should be included in the agency's report. Specifically, use the following:
    - Prior GAO reports,
    - Prior IG/Internal audit reports,
    - Consultant/Contractor studies and reports,
    - Congressional staff reports, and
    - Congressional hearings.
  - b. Supplement the inventory through discussions with knowledgeable GAO staff on known internal control weaknesses for programs and accounting systems.
  - c. Supplement the inventory through discussions with knowledgeable agency officials, particularly IG or equivalent.
2. Using the inventory developed, evaluate current status of the internal control weaknesses identified that the agency may need to report on.
  - a. Determine the status of actions taken on these internal control weaknesses by following up with:

--GAO's report followup system,  
--IG/Internal audit recommendations  
tracking system, and  
--Discussions with cognizant GAO and  
agency personnel.

- b. Determine if the agency's vulnerability assessments covered the weaknesses and how the agency assessed and rated its vulnerability in the areas with internal control weaknesses identified in our inventory. Some of this work may have been completed under the work program section on vulnerability assessments. If feasible, discuss the vulnerability assessment with the individual who performed it and document the rationale for the rating given.
- c. Determine if the agency plans any internal control reviews relating to the weaknesses. If so, what is the basis for the reviews? Use information obtained in the work program sections on vulnerability assessments, internal control reviews, and followup systems to assist you in performing this step.

- d. Determine IG/Internal audit plans to perform work related to the weaknesses. Use information obtained in work program sections on vulnerability assessments, internal control reviews, and followup actions to assist you in making this determination.
3. Using the results of step 2, identify the internal control weaknesses the agency may need to report on.
  - a. Determine the agency plans for reporting.
  - b. Compare the planned report with our inventory of weaknesses.
  - c. Coordinate with the senior advisors on any discrepancies between the agency's planned report and our inventory.
  - d. Discuss any discrepancies or omissions in the agency's report and attempt to convince the agency to include the weaknesses in the report or obtain their rationale for not including significant internal control weaknesses in their report. Document, in detail, your discussions with agency officials on these discrepancies and give your overall conclusion on which significant internal control weaknesses should have been reported but were omitted from the agency's report and their reasons for not reporting them.

4. Evaluate the agency's report on internal control weaknesses.
  - a. Obtain the agency report.
  - b. Summarize, by program or functional area, the internal control weaknesses which were included in the agency's final report and submit this summary to the core group as part of your referenced summary.
  - c. Considering the results of step 3, evaluate the completeness and accuracy of the report. If additional followup is considered necessary, consult the core group immediately for the specific work planned by GAO.
  - d. Develop a list of areas which have been identified as having significant internal control weaknesses using our inventory of past GAO reports, IG reports, etc. which are not included in the agency's final report. Submit this list to the core group as part of your referenced summary.
- B. Ascertain whether agency head has an adequate basis for making the required statement. Neither the act nor the OMB Guidelines for implementing it provide detailed requirements on specifically what information the agency head should have to make the required statement. OMB suggests only that (1) if all its guidelines for complying with the act are followed and (2) the agency head receives written assurances

from appropriate officials, then the agency head will be in a position to make the report. Our work under this objective is designed to assess whether the agency head has been provided sufficient factual information upon which to conclude whether the organization's internal control systems comply with the act's requirements. Accordingly, much of this data will be developed through other phases of this work program.

TASKS:

1. Consider conclusions reached in GAO's evaluation of the agency's vulnerability assessments and internal control reviews; specifically, where they are successful in meeting the objective of identifying all material weaknesses in internal controls.
2. Determine whether results of the reviews and assessments were accurately communicated to the agency head. Refer to GAO's work on the agency's followup and reporting systems. Obtain and evaluate reports, memorandums etc., on internal control status provided to the agency head.
3. Determine whether all existing significant information pertaining to internal controls, such as GAO, IG, and consultants reports, were communicated to agency head. (See work steps under next objective.)
4. Based on GAO's work on segmenting the agency



(section IV of this audit program), consider specifically (1) which officials should provide assurances to the agency on the effectiveness of internal controls in their areas of responsibility and (2) determine whether these officials have provided such assurances.

5. Obtain all written statements on internal control provided to the agency head and ascertain whether they support the agency head's statement.
6. Reach and document a conclusion on whether the agency head has an adequate basis for making the required statement.

C. Assess the adequacy of the agencies' plans and schedule for correcting reported material internal control weaknesses. Neither the act nor OMB's guidelines provide specific instruction to the agencies regarding the plans and schedule for correcting internal control weaknesses which must be included in the agency head's reports. Accordingly, GAO will have to develop its own criteria for measuring the adequacy of the agencies reported plans for corrective actions. For the first year of our work under the act, GAO will evaluate the plans for corrective actions in light of the following:

--Do the plans address the weaknesses identified?

--Are the plans realistic and achievable?

--Are the plans backed with agency  
managements' high priority?

The agency heads' reports will likely describe the plans for corrective action only in brief and general terms. However, the plan in the report should be backed-up with detailed action plans within the agency and our work will focus primarily on these plans. Reference to GAO's work on vulnerability assessments, internal control reviews, and the followup reporting system may provide a good insight for this work.

TASKS:

1. Evaluate whether plans address reported weaknesses, and are realistic and achievable by:
  - a. Discussions with the group which identified weaknesses.
  - b. Discussions with operating officials.
  - c. Consultation with GAO personnel with appropriate expertise (programming division, systems group, etc.).
2. Determine priority placed on plans by agency management by considering whether:
  - a. responsibilities and accountability are appropriately assigned,
  - b. timetables and milestones are established, and
  - c. progress is periodically monitored.

3. Prepare a schedule of actions planned by the agency to correct internal control deficiencies they reported. These actions should be identified in the agency's report. Submit this schedule to the core group with your referenced summary.
- D. Determine whether statement's wording provides the assurances and information required by the act. The act requires the statement to specifically say whether the agency's internal control systems "fully" comply with GAO standards and provide reasonable assurance that:

- Obligations and costs are in compliance with applicable law;
- Funds, property, and other assets are safeguarded against waste, loss, unauthorized use, or misappropriation; and
- Revenues and expenditures applicable to agency operations are properly recorded and accounted for to permit the preparation of accounts and reliable financial and statistical reports and to maintain accountability over assets."

**TASKS:**

1. Obtain and examine agency's draft statement prior to signature. If it does not conform to act's requirements, point out any shortcomings to appropriate officials, and attempt to resolve any problems before signature.

2. Obtain and examine final, signed statement.

Document whether its wording conforms to act's requirements.

E. Prepare a referenced summary

TASK:

Prepare a referenced summary covering the steps in this section of the work program and give an overall evaluation of the adequacy of the agency's report in accordance with GAO methodology and procedures and submit it to the core group not later than February 29, 1984.

VII. TRACKING AND REPORTING FOLLOWUP SYSTEMS FOR VULNERABILITY ASSESSMENTS, INTERNAL CONTROL REVIEWS, AND CORRECTIVE ACTIONS

To meet the act's objectives, the vulnerability assessments and internal control reviews should not be an end in themselves. Rather, the results of the assessments and reviews in the form of corrective actions must be considered and acted upon by management to ensure that real improvements are achieved. To accomplish this, the agencies need to have effective systems and procedures to track, control, monitor and report on work performed under the act. The need for such systems and procedures to be formalized, and most likely automated, is especially evident at the larger agencies. To illustrate, the Department of Health and Human Services performed thousands of vulnerability assessments. Clearly, that Department would need an effective, systematic approach to track and monitor this work and summarize its results.

To properly control and evaluate their Financial Integrity Act work the agencies should have systems and procedures capable of:

- Scheduling performance of vulnerability assessments and internal control reviews,
- Recording and reporting the results of vulnerability assessments and internal control reviews,
- Scheduling and tracking corrective actions on weaknesses identified in the vulnerability assessment and internal control review process,
- Informing appropriate officials of progress and delays in accomplishing planned corrective actions, and

--Summarizing and reporting the overall results of vulnerability assessments, internal control reviews, and corrective actions.

These factors are implicitly recognized in OMB's guidelines (chapter II, Internal Reporting).

Because of the short time the act has been in effect, it is likely that many agencies will not yet have fully developed and implemented formal systems having the capabilities discussed above. Some agencies are using contractors to develop such systems while others are developing them in-house. Where systems are in the development stage, our work should evaluate their design and specifications as indicated in the work steps discussed below. However, in such cases consideration will also have to be given to the agency's temporary, first year arrangements and procedures to schedule vulnerability assessments and internal control reviews and to report on their results.

As noted in Section VIII of this work program, the act also requires agency heads to report on whether their organization's accounting systems comply with Comptroller General principles and standards. Accordingly, our efforts under this section of the work program will also consider the procedures or systems the agency has established to identify any deviations from Comptroller General principles and standards and to track the progress of related corrective actions. In event the agency uses the system for tracking its internal control work under the act to also track its accounting system work, the tasks listed below will apply to

both. If a separate tracking system is used, it will have to be evaluated separately. The tasks detailed below should be modified as necessary and used to accomplish this evaluation.

The overall objective is to evaluate agencies' systems and procedures to schedule, track, monitor and summarize vulnerability assessments, internal control reviews, and accounting system compliance evaluations, as well as planned corrective actions. More specifically we will (1) determine and document the agencies system for tracking, monitoring, and summarizing its Financial Integrity Act work, (2) evaluate the system's capabilities and performance, and (3) prepare a work summary describing the system and any improvements needed.

- A. Determine and document agency's system for tracking, monitoring and summarizing Financial Integrity Act work.

#### TASKS

1. Identify officials responsible for the agency's Financial Integrity Act compliance (internal control aspects and accounting system aspects). Obtain and document an overview of system's procedures and assigned responsibilities for:
  - a. Scheduling vulnerability assessments, internal control reviews, and accounting system compliance evaluations.
  - b. Identifying weaknesses noted.
  - c. Scheduling and tracking corrective actions.
  - d. Monitoring progress on corrective actions.
  - e. Summarizing and reporting results to key officials.

2. Obtain and evaluate available documentation covering the issues noted in Task 1 above. Such documentation could include:
    - a. Directives, recommendations, or instructions.
    - b. Official agency procedures or orders.
    - c. Formal agency plans for compliance with the act.
    - d. Contractor/consultant proposals or reports.
    - e. Systems documentation.
    - f. Other appropriate reports on vulnerability assessments, internal control reviews, and accounting system compliance evaluations.
  3. Ascertain whether the system/procedures are coordinated with or integrated into the agency's audit followup information system. If not, determine why.
  4. Evaluate followup systems under development. If a formal followup system is in the development or implementation stage, contact cognizant agency officials or contractor personnel and determine whether the pending system's design and specifications provide for the functions noted in Task 1 under this objective.
- B. Evaluate the adequacy of the agency's followup program to (1) log actions to correct internal control weaknesses and deviations from our accounting system



principles and standards as well as projected target dates for correction and (2) monitor whether the corrective actions are actually taken and are in accordance with the projected correction dates.

TASKS:

1. Confirm whether the system/procedures actually operate as described by the agency.
  - a. Obtain several completed vulnerability assessments, internal control reviews, and accounting system compliance evaluations and trace them through all phases of the follow-up/reporting system. Determine whether systems tracking included:
    - beginning and ending dates,
    - weaknesses identified,
    - corrective actions planned and target dates for completion, and
    - current status of corrective actions.
  - b. Obtain copies of any reports or summaries used for monitoring the results and progress of the agency's vulnerability assessments, internal control reviews and accounting system compliance evaluations. Determine whether the reports
    - contain the required information, (see task 1 above),

--are distributed timely and to  
appropriate personnel, and  
--are summarized and brought to the  
attention of top agency officials.

2. Ascertain if appropriate priority has been given to tracking the corrective action plans by considering whether
  - a. the responsibility and accountability for corrective actions has been assigned at a high enough level,
  - b. timetables and milestones for the corrective actions have been established, and
  - c. provisions have been included in the system for periodical progress and measurement reporting.
3. Determine plans for future vulnerability assessments. (If this task was not performed when we did the vulnerability assessment section, it must be done now.)
  - a. Determine if additional guidance is to be developed.
  - b. Determine when future vulnerability assessments are planned.
  - c. Determine how often vulnerability assessments will be performed.
  - d. Describe the agency's future plans, including approach and organization for performing vulnerability assessments.

C. Prepare a referenced summary.

TASK

Prepare a referenced summary covering the steps in this section of the work program and give an overall evaluation of the adequacy of the agency's followup system in accordance with GAO methodology and procedures and submit it to the core group not later than November 30, 1983.

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