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REPORT ON REVIEW
OF
CENTRAL OFFICE'S DIRECTION OF
INTERNAL AUDIT ACTIVITY

AUDIT DIVISION
GENERAL SERVICES ADMINISTRATION



UNITED STATES
GENERAL ACCOUNTING OFFICE

MARCH 1967

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

CIVIL DIVISION

MAR 10 1967

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Dear Mr. Knott:

The accompanying report summarizes the findings and proposals based on our review of the direction of the internal audit activity by the Audit Division, General Services Administration. This report is essentially the same as the draft submitted to you in December 1966, except for the inclusion of your comments on action being taken to implement our proposals. We are pleased to note that our proposals have been accepted and that they will be of assistance to the Administration in its current efforts to further strengthen, improve, and extend its internal audit activity.

We believe that the implementation of actions to strengthen the Audit Division's reporting practices will make internal audit reports more meaningful to management and more helpful to operating personnel. We believe also that providing guides where necessary and updating existing audit guides will help to assure management that internal audits are performed on a consistent basis nationwide in fulfillment of the Administration's broad audit objectives.

Copies of this report are being sent to the Government Activities Subcommittee of the Committee on Government Operations, House of Representatives, and to the Director, Bureau of the Budget.

Sincerely yours,

A. T. Samuelson

Director, Civil Division

The Honorable Lawson B. Knott, Jr.
Administrator, General Services Administration

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REPORT ON REVIEW
OF
CENTRAL OFFICE'S DIRECTION OF
INTERNAL AUDIT ACTIVITY
AUDIT DIVISION
GENERAL SERVICES ADMINISTRATION

GENERAL COMMENTS

The General Accounting Office has reviewed the activity of the Audit Division of the General Services Administration (GSA). Our review was directed primarily toward evaluating the effectiveness with which the Audit Division is directing the efforts of the area audit offices. Evaluations of the manner in which the area audit offices execute audit assignments are made from time to time in connection with our reviews of GSA's operations and financial transactions and become the subject of separate reporting. The scope of our review is shown on page 14.

GSA's basic policy requires that the internal audit program be an integral part of total agency management and assist all levels of management in achieving the most efficient administration. As of October 1, 1966, the Audit Division was staffed with 18 auditors at the central office in Washington, D.C., and 44 at the five area audit offices; 73 auditors were authorized by the approved budget for fiscal year 1967.

Although the Audit Division does not report directly to the Administrator of General Services, we found that its authority is broad enough to give the internal auditors a great degree of independence in the selection of areas for audit and in the scope of their work; we found indications that this independence was, in fact, exercised by the Audit Division. Also, our review showed that:

1. Audit coverage of operations and financial transactions is planned in advance.
2. Audit work, such as examination of inventories, payrolls, receipts, and disbursements, is scheduled in all regions on a cyclical basis.
3. Audit findings are discussed with cognizant operating personnel.
4. Reports are submitted to high-level management officials to ensure that authoritative consideration will be given to audit findings and recommendations.
5. Audit findings and recommendations are followed up in order to appraise the adequacy of corrective actions taken.

There are, however, a few areas of GSA's internal audit program which we believe can be improved. These areas are discussed in this report.

AREAS FOR IMPROVEMENT

INTERNAL AUDIT REPORTS TO MANAGEMENT

There are several techniques or forms of presentation which the Audit Division can use to make its reports more meaningful to management and its recommendations more helpful to the operating personnel. This conclusion is based on our evaluation of selected reports on various reviews, which issued from the central office and the area audit offices through fiscal year 1966. These reports included 27 issued in fiscal year 1964 covering reviews of lease rentals and space management activities and 30 issued in fiscal years 1964 and 1965 covering reviews of utility charges in leased and Government-owned buildings.

Deficiency reporting

An important function of an internal auditor is to review and report on the effectiveness of internal controls and the extent and nature of management's compliance with agency policies, plans, and procedures and with applicable legal and regulatory requirements. One technique used by the auditor is to look at the results of an operation and, if deficiencies are noted, to determine whether the causes of the deficiencies can be attributed to weaknesses in internal controls or to noncompliances with prescribed policies and procedures. The auditor's report comments, however, should not be confined only to those matters which are unsatisfactory; if the operation is generally well controlled or if there are no major findings of deficiencies, the internal auditor should so inform management. The fact that reasonable audit coverage disclosed no reportable deficiencies is of itself reportable as an assurance to management of the effectiveness of internal controls and the compliance with prescribed procedures.

To keep an audit assignment within manageable proportions, an auditor will frequently limit his work at any one time to a small segment of the operations. Thus, because an entire management function has not been reviewed, there may be a hesitancy on the part of the auditor to express an appraisal of management's efficiency and its compliance with prescribed policies and procedures. However, if the auditor is careful to describe the area covered and the scope of his review, management will be able to place his appraisals in proper perspective with the work done.

Although the Audit Division is required to evaluate the effectiveness of internal controls and the extent and nature of management's compliance with agency policies, plans, and procedures and with applicable legal and regulatory requirements, it has limited its reports, in general, to the deficient aspects. We recognize that areas found in need of improvement deserve special audit and reporting attention; however, we believe that there is need for report recognition of audit findings of compliance with policies, procedures, and other requirements.

Reports having evaluations as to compliance with, and adequacy of, internal controls and having descriptions of the areas audited and the scope of work done by the internal auditor would give management opportunities to place the audit findings in proper perspectives with the segments of operations reviewed. Also, digests of audit findings having appraisals of the effectiveness of management controls would give the Administrator another basis for evaluating the manner in which the Services fulfilled their responsibilities in those areas covered by the summary reports of the Audit Division.

Identification of basic causes
of deficiencies

The basic responsibility for compliance with prescribed policies and procedures rests with operating personnel in the GSA Services and regions. On the other hand, the role of internal audit is to review and appraise compliance with policies, plans, and procedures and to render independent and objective reports to management. In a large organization such as GSA, the number of areas which will benefit from these reviews is virtually unlimited; however, full audit coverage of all areas will usually be beyond the manpower resources of the internal audit organization. Accordingly, so that the audit mission may be properly fulfilled, it is necessary that the internal audit identify and report the basic causes of deficiencies noted and avoid expending manpower resources on activities which are the responsibility of program management.

Response to the interest
of management

In the event that operating personnel has not fulfilled its responsibilities, management is primarily interested in knowing the fundamental causes and the necessary corrective actions in order to prevent a recurrence. To help achieve this goal, GSA has prescribed operating policy which states that:

"Internal audits will include reviews of program and financial operations to test compliance with and the adequacy of established policies and to make appropriate recommendations to improve the effectiveness of controls ***."

To implement this policy, the internal auditor must identify the causes of deficiencies noted and aim his principal audit recommendations toward correcting the apparent weaknesses or failures of

internal controls which allowed the deficiencies to happen. Secondary recommendations, of course, would be for the operating personnel to review its operations to determine the full extent of the deficiencies and to recover possible overpayments or initiate such other corrective actions as may be appropriate.

We noted that, in reporting the results of its reviews, the Audit Division generally tended to highlight the effect of specific deficiencies rather than to identify the causes; many of the auditors' reports recommended that specific overpayments be recovered or that required documentation be obtained. Also, many reports did not identify the causes of the specific deficiencies or recommend appropriate action to strengthen the weak internal controls which permitted the deficiencies to occur.

For example, some of the audit reports covering reviews of lease rentals and space management activities stated that there were indications that rents paid exceeded the limitations set by the Economy Act (40 U.S.C. 278a). In summarizing these reports, the Audit Division stated that, subsequent to the issuance of the reports to regional administrators, regional officials had substantiated compliance with the Economy Act by reappraising the leased properties, revising estimates of lessor service costs, or making determinations that the original appraisals "may have been conservative in various estimates which were not too well supportable by market data."

We believe that the audit reports would have been more helpful to operating personnel if they had (1) identified the weaknesses in internal controls which had failed to prevent the execution of leases in apparent violation of Economy Act limitations and

(2) recommended appropriate action to strengthen the controls and thus minimize the danger of recurrence of the problem.

Also, the audit reports on reviews of charges for utilities stated principally that GSA was not being billed under the most favorable rate structures for which it qualified; that, because of multiple metering at some locations, GSA was being deprived of the benefit of lower rates usually available when total consumption can be consolidated through single metering; and that excessive charges were being made by lessors. The audit recommendations generally were concerned with the correction of specific findings and were not directed to the strengthening of internal controls. Therefore, the resulting corrective actions were not designed to prevent recurrences of the deficiencies. Ultimately, in summarizing findings included in about 40 reports issued to regional administrators, the Audit Division pointed out the need for providing the regional offices with technically qualified utility specialists.

Better utilization of
audit manpower resources

Another benefit of identifying the causes of deficiencies is that it promotes better utilization of internal audit manpower. The GSA organizational structure provides for review and appraisal functions at all management levels. Each level is subject to review and appraisal by the next higher level or by experts in specialized fields at staff levels. Therefore, the basic responsibility for determining whether prescribed policies and procedures are being followed rests with program management.

The internal audit reviews should be directed to the effectiveness of internal controls, including management's review and appraisal function. Reports should identify the causes of deficiencies noted and make appropriate recommendations to assist

management in meeting its responsibilities. Once it has brought to management's attention a condition warranting corrective action, the Audit Division should allow management a reasonable period to undertake the necessary corrective action before resuming audit work in a specific area.

We noted that, in connection with the review of leasing activities in GSA regions 3, 5, and 7 in fiscal year 1964, the Audit Division was aware in April 1964 of deficiencies relating to payments for electricity at 30 locations. Yet, the internal audit of utilities was subsequently extended to eight GSA regions, including the above three regions, and deficiencies were reported at 96 locations; in substance, the deficiencies were similar to those found in the earlier reviews. In our opinion, the extension of the reviews by the Audit Division served chiefly to identify additional examples of the deficiencies found in its earlier reviews which had already indicated that management's review and appraisal function was not being adequately performed. Although substantial overpayments and possible savings in electricity consumption had been disclosed in the Audit Division's extended reviews, we believe that, once the condition was disclosed, the reviews to determine the extent of the problem and the necessary corrective action were essentially an operating function rather than an internal audit function.

We believe that, in view of the indications of lapses in management's review and appraisal function found in the earlier reviews of leasing activities, the Audit Division needlessly committed manpower to further reviews in an area examined only a short time previously. The Audit Division workload stemming from the diversity of GSA's activities and the magnitude of the financial

transactions is such as to require that the closest attention be given to the conservation of audit manpower to ensure adequate examination into the effectiveness of the management controls governing the operating and staff organizations constituting GSA. To the extent that audit manpower beyond that required is committed in one area, there is less manpower available to apply in other areas.

Proposals

In the interests of improving the GSA Audit Division's reporting practices so that audit reports will be more meaningful to management and more helpful to operating personnel and promoting the better utilization of audit manpower, we proposed that, in their reports, auditors (1) include appraisals of the adequacy or inadequacy of internal controls and the compliance of operating personnel with prescribed policies and procedures and (2) state the basic causes of deficiencies noted, including possible weaknesses or failures in internal controls, and recommend corrective actions to cure the causes of the deficiencies as well as the specific deficiencies.

In commenting on our proposals, GSA stated that instructions were being revised to broaden the scope of audits of internal controls and the degree of compliance therewith and to ensure that audit reports include recommended actions to cure the causes of deficiencies noted in the audits. GSA stated also that this action should strengthen the internal audit reporting practices to overcome the reporting deficiencies which we noted in our review.

AUDIT GUIDES

Under GSA's internal audit program, the Audit Division is charged with responsibility for developing audit guidelines defining the objectives, nature, and scope of audit work to be performed by the auditors. The audit guide states the specific objectives, basic techniques, principles, and other information required to carry out an auditing assignment in a uniform manner in all GSA regions. Ideal guidelines help to provide assurances that the effectiveness of internal controls will be appraised in depth by all auditors and that all important aspects of the operations under audit will be reviewed, including the operating personnel's compliance with prescribed policies and procedures.

Audit guides obsolete

Many of the audit guides in use in the Audit Division are obsolete and of limited aid to internal auditors; 24 of the Division's 34 audit guides were issued before September 1959 and have not been kept current. Many changes in accounting and operating procedures and in GSA's organizational structure have been made since most of the audit guidelines were written, and the usefulness of the guidelines is impaired by references therein to obsolete procedures and nonexistent organizational units. It is desirable that internal audits be conducted to an adequate depth of coverage in all GSA regions. Auditors who are busy on day-to-day problems or who possibly are unfamiliar with the area being audited should be provided with up-to-date audit guidelines geared to assist them in appraising the effectiveness of current internal controls and determining the extent of compliance with current policies and procedures.

GSA is not a static organization. Program operating procedures are revised to take advantage of technical advancements, and short cuts are taken to reduce costs. Also, GSA, in a continuing effort to improve the financial management system, may add or eliminate account classifications in the chart of accounts; change the format of source documents so that certain types of information are no longer shown on the documents; transfer the responsibility for processing documents from one organizational unit to another; and eliminate certain intermediate steps in processing contract, procurement, fiscal, and other documents.

Internal controls frequently are affected by such changes, and auditors in the field should be alerted, preferably by means of updated audit guides, as to the effect that such revised internal controls will have on their audit plans and procedures. Otherwise, it will be necessary for auditors in the central office and in each area audit office to spend time in basic research to determine where internal controls may have been weakened or changed by reorganizations and revised operating procedures; even then, there are no assurances that every auditor will recognize or place the same degree of importance to the changes.

In our opinion, the updating of audit guidelines is almost mandatory in helping to ensure that effective audit procedures are followed by all auditors whenever prescribed audit instructions are no longer applicable because of changed operating techniques and documentation. Accounting transactions were being processed on electrical accounting machines when most of the audit guidelines were written and many of the audit instructions were related to source documents and "hard copy" ledgers then available; "hard copy" ledgers were discontinued, new source documents were adopted,

and existing source documents were revised or discontinued in July 1963 when the processing of accounting transactions was transferred to a card-oriented electronic data processing system. Further modifications to GSA's accounting system and organizational responsibilities were made in fiscal year 1965 when accounting operations were transferred from the 10 regions to the five accounting centers. These changes, many of which have a significant bearing on internal controls, have not yet been incorporated in the audit guides.

Audit guides not provided

Although the Audit Division's annual audit plans provide the broad objectives for each planned assignment, guides have not been issued on a number of assignments and the approach, scope, and depth of the audit required to meet the objectives is left to the discretion of the cognizant audit staffs. Of the 38 assignments included in the Audit Division's audit plans for fiscal year 1966, audit guides had not been issued on 7 recurring or multiregional review assignments. Some of the assignments involved determinations of compliances with the laws and regulations governing the activities being reviewed.

Individual guides designed for particular assignments would conserve the manpower of the audit staffs responsible for conducting the reviews by obviating time-consuming research into the applicable laws, regulations, and prescribed policies and procedures necessary to develop specific audit procedures. Audit guides would also provide a basis for uniformity of approach, completeness of coverage, and fulfillment of objectives, particularly on recurring reviews and multiregional reviews conducted by several area audit offices.

Proposals

We proposed that the Director of the Audit Division assign to specific members of his staff responsibility for (1) reviewing and analyzing all changes in GSA policy, organization, operating, and accounting handbooks on a current basis to evaluate their possible effects on existing internal controls and audit instructions, (2) revising audit guides whenever audit instructions are rendered obsolete by organizational and procedural changes in GSA operations, and (3) providing audit guides in those areas where they have not been provided.

In commenting on our proposals, GSA recognized that effective guides contribute to a successful audit program and stated that it had started action to provide additional resources to work on a project to improve and update the detailed audit guides.

We believe that the implementation of these proposals will (1) conserve manpower in the central office and in each area audit office where auditors have been independently reviewing changes in prescribed operating procedures to determine the impact on audit plans and procedures and to revise their audit instructions accordingly and (2) provide assurances that the scope and depth of the audits performed are on a consistent basis nationwide in fulfillment of the broad audit objectives in the annual audit plans.

SCOPE OF REVIEW

Our review was carried out in Washington, D.C. We reviewed (1) audit guides and instructions, (2) annual audit plans and schedules, (3) selected audit reports, (4) distribution of reports to cognizant management officials, and (5) follow-up of corrective action on reported deficiencies. We reviewed also the Audit Division's mission and functional statements, its place in the GSA organizational structure and its degree of independence from the offices directly responsible for GSA's program operations, the numerical relationship of the professional audit staff in area audit offices to selected workload factors, and the staff training program.

In addition to being responsible for the GSA internal audit program, the Audit Division is responsible for auditing contractors' records for use in contract negotiations or in the determination of rental payments to GSA. Our review did not cover these aspects of the Audit Division's activities.