Honorable Donald E. Kirkendall
Inspector General
Department of the Treasury
Room 2412, Main Treasury Building
1500 Pennsylvania Avenue, NW.
Washington, DC 20220

Dear Don:

We are pleased to issue our final report on the President's Council on Integrity and Efficiency (PCIE) External Quality Control Review of the Department of the Treasury Office of Inspector General. Your response to the October 24, 1991, draft report indicates that you agree with all of the recommendations. That response is included in its entirety in the final report as Appendix A.

There is one item we would like to bring to your attention. In the "Evidence" section of the draft report, we recommended that referencers should be required to reference substantial changes from draft to final reports. Your response did not address this issue. Unless you notify us differently, we will assume this was acceptable and that you will address this issue in future instructions to your staff.

Your response shows that many actions have been implemented in response to our recommendations and the recommendations of your Quality Assurance Reviews. It also reports a number of planned actions that, once completed, will satisfy all of our concerns.

We appreciate your cooperation and support during the peer review process.

Sincerely,

Patrick E. McFarland
Inspector General
Office of Personnel Management

David C. Williams
Inspector General
U.S. Nuclear Regulatory Commission

Enclosure
PRESIDENT'S COUNCIL ON INTEGRITY AND EFFICIENCY

EXTERNAL QUALITY REVIEW OF

THE DEPARTMENT OF THE TREASURY
OFFICE OF INSPECTOR GENERAL

Report Number 2A-00-91-TR

Performed by:

Office of Personnel Management
Office of Inspector General

and

U.S. Nuclear Regulatory Commission
Office of Inspector General
Introduction

In accordance with the February 8, 1991, Memorandum of Understanding between the Department of the Treasury, the General Services Administration, the United States Nuclear Regulatory Commission (NRC), and the Office of Personnel Management (OPM), NRC and OPM have conducted an external quality control review of the Department of the Treasury Office of Inspector General (OIG) audit operations. The review was conducted in accordance with the President's Council on Integrity and Efficiency (PCIE) February 5, 1990, draft Guide for Conducting External Quality Control Reviews of the Audit Operations of Offices of Inspectors General.

A draft report was issued to the Department of the Treasury OIG on October 24, 1991. The Treasury OIG's response to the draft report, dated December 16, 1991, indicates agreement with all recommendations. The response is included in its entirety as Appendix A.

Background

Public Law 100-504, the Inspector General Act Amendments of 1988, established a statutory OIG in the Department of the Treasury effective April 16, 1989. The Amendments consolidated Treasury's existing OIG and those portions of the Offices of Internal Affairs in the Bureau of Alcohol, Tobacco, and Firearms (ATF) and the U.S. Customs Service and the Office of Inspection in the U.S. Secret Service that were engaged in audit activities. The Amendments provided that the OIG would initiate, conduct, and supervise internal audits and internal investigations within Treasury. They also provided that the OIG would oversee internal investigations made by the Offices of Internal Affairs and Inspection in the Bureaus of ATF, Customs, and Secret Service and internal audits and internal investigations of the Inspection Service of the Internal Revenue Service (IRS).

Objectives, Scope, and Methodology

The objectives of the peer review were to determine if the OIG has an internal quality control system that is adequate, in place, and operating effectively; follows the General Accounting Office's Government Auditing Standards (GAS) and its own established policies and procedures; and follows an annual planning process that meets the requirements of Office of Management and Budget (OMB) Circular A-73, Audit of Federal Operations and Programs.

The field work was conducted from August 12 to September 6, 1991, by a peer review team of five auditors from the United States Office of Personnel Management and the United States Nuclear Regulatory Commission Offices of Inspector General. Work was
conducted at the Treasury OIG office in Washington, D.C., the Western Regional Office in El Segundo, California, and the Northeastern Regional Office in Boston, Massachusetts.

The team did not review IRS policies and procedures or audits performed by the IRS audit staff and, therefore, reached no conclusion regarding IRS audit operations. In a memorandum to the IRS Commissioner dated August 14, 1991, the Inspector General recommended that IRS arrange for a peer review by an organization that is comparable to the IRS' internal audit function. To be in compliance with standards, this review should be conducted by January 1, 1992.

The team reviewed OIG policies and procedures and internal quality assurance functions, including recent Quality Assurance Reviews. The OIG's Semiannual Reports for the periods ended September 30, 1990, and March 31, 1991, listed 212 audits, 111 of which were IRS audits. We selected 20 audits from the remaining 101 non-IRS audits for review. Audits selected were from several bureaus and included a variety of types and sizes of audits performed. We reviewed two additional audit reports using only the reporting standards section of the PCIE audit guide. Finally, we offered to perform a limited review of current audit working papers, and reviewed the set provided to us.

In addition to reviewing the audit reports and supporting working paper files, the team members interviewed audit officials at each site and discussed observations with them during the review. Professional judgment was used in determining compliance with policies, procedures, and applicable standards.

This review was less in scope than an audit performed in accordance with generally accepted Government auditing standards. Because it was based on a judgmental sample of audits performed, our review would not necessarily disclose all weaknesses or lack of compliance with standards. Also, because we reviewed work reported as of March 31, 1991, our review may not have recognized all improvements in operations made since that time. We are confident, however, that our work was sufficient to offer an opinion on the OIG's compliance with standards.

RESULTS OF REVIEW

Based on our review, we concluded that the OIG had an internal quality control system that was adequate, in place, and operating effectively; materially complied with GAS and its own established policies and procedures for the individual audits reviewed; and substantially met the requirements of OMB Circular A-73.

In 1990, the Department of the Treasury OIG established an Office
of the Assistant Inspector General for Oversight and Quality Assurance to be responsible for assessing the quality of OIG work. Within this office, the Office of Oversight oversees internal investigations made by the Offices of Internal Affairs and Inspection in the Bureau of ATF, Customs Service, Secret Service and the internal audits and internal investigations of the IRS. The Office of Quality Assurance (OQA) evaluates audit and investigative performance within the OIG, including the regional and field offices.

To date, the OQA has conducted eight Quality Assurance Reviews (QAR) of OIG audit activity. The team reviewed the QAR reports and three sets of QAR working papers. We also performed an independent review of three sets of working papers reviewed by OQA as part of their evaluation. We concluded that an internal quality control system is in place and operating effectively to provide reasonable assurance that the OIG Office of Audit is following GAS and its own established policies and procedures.

The OIG has developed audit universe and planning policies and procedures which, although not fully implemented at the time of our review, provide guidance for the planning process. These directives require OIG officials to take a forward-looking approach to planning by identifying pending issues that have implications for future audit activity. We concluded that the OIG substantially met the annual planning requirements of OMB Circular A-73.

The OIG is in the process of substantially revising the OIG Manual. It is our opinion that the Manual, when completed, will provide comprehensive guidance to the staff on conducting audits that meet or exceed GAS requirements.

For the individual audits reviewed, the team concluded that the OIG materially complied with GAS and internal policies and procedures. Auditors' judgments and conclusions were generally supported by sufficient, competent, and relevant evidence. The audit reports were clear and objective and appeared to accurately present the facts. Audit progress was tracked, as evidenced by audit status reports produced by the OIG Management Information System.

During the course of our review, we found several matters that should be considered by the OIG to improve the system of quality control. In some instances, these matters are similar to recommendations made by the OQA in recent reviews. In order to present a complete record of the peer review, however, we are reporting all areas for potential improvement identified by the team.
OPPORTUNITIES FOR IMPROVEMENT

This section discusses areas where the OIG could further develop existing policies, procedures, and controls in order to improve its system of quality control, but which do not materially affect the statement of positive assurance about the organization's auditing operations.

Quality Control Reviews

The OQA has performed QAR's of OIG compliance with most areas covered by GAS and has made several recommendations for improvement. However, we determined that OQA has not yet reviewed OIG compliance with GAS reporting standards. We suggest this area be included in future QAR's.

Continuing Education and Training

GAS requires audit organizations to establish a program to ensure audit staff meet specific continuing education and training requirements. It further requires the organizations to keep documentation of education and training completed. Our interviews and reviews of OIG policies and procedures disclosed that OIG management is fully aware of this requirement. We relied on the work performed by OQA to verify that OIG met the standard for continuing education and training.

At the time of our review, the OIG was implementing a new Employee Training Inventory system to centrally track and monitor continuing education and training. This system will replace the Training Information Management System used by some supervisors to document continuing professional education credits completed.

We found that information in the new Employee Training Inventory system was not complete. Specific information for a significant number of OIG employees had not been entered into the system, and information in the system had not been reviewed for accuracy. When the OIG completes and verifies information in the system and establishes effective procedures to ensure information is maintained on a current basis, we believe that the system will adequately monitor compliance with the continuing education and training requirements.

Independence

GAS requires the audit organization to be organizationally independent in all matters pertaining to audit work. It also requires all auditors to be free from personal and external
impairments to independence and to maintain an independent attitude and appearance. Our examination of the OIG's implementation of this standard revealed two issues for concern. The first issue pertains to the organizational independence of the OIG legal counsel; the second involves financial disclosure for OIG employees.

**Organizational Independence of OIG Legal Counsel**

Legal counsel is provided to the OIG under an informal arrangement with the Department of the Treasury's Office of the General Counsel (OGC). An OGC attorney is specifically designated to provide such counsel and has been providing this service for the past 5 years.

Although the attorney's salary and position are charged to the OIG, she is formally assigned to OGC and has not been officially detailed to the OIG. Furthermore, OGC prepares her performance appraisal with input from the OIG. There is no Memorandum of Understanding between OIG and OGC to define the responsibilities of the legal counsel or procedures for handling conflicting opinions between the legal counsel and OGC. We believe the absence of a fully defined relationship between OIG and OGC regarding the status and responsibilities of the attorney results in an impairment to organizational independence.

Optimally, legal counsel should be a member of the OIG staff to avoid even the appearance of a conflict of interest or an impairment to organizational independence. If this is not possible, the OIG and OGC should formalize the arrangement with a Memorandum of Understanding.

**Individual Auditors**

GAS requires individual auditors to maintain an independent attitude and appearance. OIG officials fully recognize the need for auditors to be independent in appearance and in fact. OIG policy requires employees at grade 13 and above to complete financial disclosure statements. At the time of our review, we noted the OIG was in the process of collecting current statements. Therefore, we were unable to confirm that all required statements had been submitted. Because it is reasonable to assume that employees in grade 12 and under could have a financial-related impairment to independence, we believe OIG policy should require financial disclosure statements from all staff who are directly involved in audits, regardless of their grade level.
Individual Audit Planning

GAS standards for financial and performance audits require that audits be well-planned. Our review of the audit planning process revealed that audits were sufficiently planned and audit programs were generally followed. Several sets of working papers contained evidence of detailed planning for each audit objective. However, audit programs did not always incorporate current GAS and OIG requirements. OIG needs to consistently document:

- Steps to review Federal Managers Financial Integrity Act reports, GAO reports, and prior audit reports;
- steps that reference current laws and regulations;
- steps to assess internal control systems in financial audits or to determine if an internal control assessment is necessary to meet audit objectives in performance audits; and
- background, objectives, scope, methodology, definition of unique terms, and special instructions in performance audit programs.

The OIG should strengthen individual audit planning processes to ensure these areas are considered in future audit programs.

Supervision

GAS requires that staff be properly supervised throughout the audit. Because supervision was not consistently documented in the working papers, we could not always confirm that supervisory activity occurred. We found that OIG needs to routinely document:

- Supervisory approval of audit programs and adherence to and deviations from the programs; and
- timely supervisory reviews of working papers and responses to supervisory comments.

At the time of our review, OIG was revising policies and procedures on supervision. The OIG should place a high priority on completing and implementing this guidance and ensure it includes specific guidelines for documenting supervisory reviews.
Evidence

GAS requires sufficient, competent, and relevant evidence to support audit findings. Our review of working papers disclosed that the evidence used as a basis for the audit reports met this standard. Evidence in interrelated working papers, summaries, and schedules was properly cross-referenced.

Independent referencing is an important quality control step to ensure audit evidence is presented clearly and accurately in the audit report. OIG policy requires audit reports be referenced. It also requires that referencing be performed by an independent referencer with an appropriate level of experience.

In our review of working papers, we found instances where draft reports had not been completely referenced. In most cases, we could not determine if referencers had sufficient experience and were independent from the audit work they were referencing. However, we did find indications that some referencing had been performed by a grade 7 auditor. In addition, we found that final audit reports were not routinely referenced.

To strengthen quality control, OIG should ensure that the policy of having independent, experienced referencers reference reports be strictly enforced. The OIG should also require the referencers to reference substantive changes from draft to final reports. Finally, the OIG should include specific requirements on the level of experience required to reference reports in its policy.

Reporting

The reports in our sample were well-written and generally in compliance with GAS. Objectives were clearly stated, and findings appeared to be complete and presented fairly.

GAS requires the scope and methodology section of the report to describe the depth and coverage of audit work conducted to accomplish the audit's objectives. The standards also require disclosure of any constraints or scope impairments. We found that the scope sections of many reports omitted at least one of the following: the time period covered by the audit, the place where the audit was conducted, types of audit procedures performed, or references to other reports or the work of other auditors. The OIG should ensure audit report scope sections fully describe the audit work performed.

For financial audits, GAS requires a written report on the auditor's tests of compliance with applicable laws and regulations. It also requires a written report on the auditor's understanding of the entity's control structure and the
assessment of control risk. If these standards are not followed, GAS requires a disclosure in the scope section stating that the applicable standard was not followed, the reason it was not followed, and the effects not following the standard had on the audit. We found that audit reports for several financial related audits did not contain either the reports or the required disclosure. The OIG should strengthen the process for reviewing audit reports to ensure all applicable standards were followed or an appropriate disclosure is made.

Policies and Procedures

Overall, we found that Treasury's OIG policies and procedures were clear and consistent with the requirements in GAS. A major initiative was underway at the time of our review to update and expand the OIG Manual. We identified several areas where existing or proposed policies and procedures did not fully address GAS requirements. As part of the Manual revision process, we suggest the OIG:

- Develop additional procedures for OIG auditors to use in determining whether to rely upon the work of other auditors when the report will not make reference to that auditor's work;

- develop policies and procedures to address the requirements to assess and report on internal control systems and compliance with applicable laws and regulations;

- develop specific policies and procedures to address the requirements and standards for financial audits and financial reporting;

- include additional procedures for reporting on personal, external, or organizational impairments in the scope section of the audit report;

- identify procedures to report all significant instances of noncompliance and abuse found in connection with an audit; and

- clarify the situations in which privileged and confidential information (such as Freedom of Information Act data or classified data) is prohibited from disclosure.
Audit Planning and Universe

OMB Circular A-73 requires each audit organization to develop annual audit plans. It also requires organizations to maintain records of their audit universe that identify the organizations, programs, activities, and functions subject to audit and to periodically review the audit universe to determine coverage, frequency, and priority of audits required.

The OIG has developed policies and procedures covering the audit universe and audit planning processes, but they had not been fully implemented at the time of our review. As noted earlier, we determined the annual audit plan was in compliance with OMB Circular A-73. The annual planning process also substantially complied with the requirements of OMB Circular A-73 for setting audit priorities. The process included obtaining input from Treasury management and developing ideas based on the OIG staff's audit experiences. The OIG updated the annual plan on a quarterly basis to adjust for differences between planned and actual usage of resources and to include special audit requests.

However, the OIG did not have a complete, up-to-date audit universe as required by OMB Circular A-73. Some old universe data relating to individual Bureaus were available, as were descriptions of regional Treasury functions. We determined that an effort was underway to identify all Treasury contracts and ADP systems. This information will become a part of the OIG universe. Even with the additional information, however, the universe will still not meet the requirements of OMB Circular A-73. The OIG should take steps to satisfy the requirements of the Circular and the newly developed policy by completing and evaluating the audit universe.
The Honorable Patrick E. McFarland  
Inspector General  
Office of Personnel Management  
1900 E Street, N.W., Room 6400  
Washington, D.C. 20415

Dear Mr. McFarland:

I appreciate the opportunity to comment on the draft peer review report on our audit operations. I also appreciate receiving this positive and helpful report and the professional manner with which the joint team conducted the review.

In accordance with the peer review agreement, your team examined reports included in our September 30, 1990, and March 31, 1991, semi-annual reports. However, due to the recent creation and rapid growth of this OIG, our organization, policies and procedures have significantly changed during and since the period covered by the peer review. We have also taken actions in response to matters identified by quality assurance reviews and self-assessments that will address many of the issues raised in your report. This is evidenced by the number of references in this response to manual chapters issued near the end or following the period of your review.

Quality Control Reviews

Recommendation

"The OQA has performed QAR's of OIG compliance with most areas covered by GAS and has made several recommendations for improvement. However, we determined that OQA has not yet reviewed OIG compliance with GAS reporting standards. We suggest this area be included in future QAR's."

Response

We agree. Our Office of Quality Assurance has reviewed each region's compliance with the audit standards, except reporting standards. We have included in our FY 1992 Quality Assurance Review Plan an initiative for implementing this recommendation. We will be selecting several reports for review throughout the year and matching them against the Comptroller General reporting standards. From the beginning of our Quality Assurance process in 1989, we had planned to begin this initiative after reviewing the Office of Audit's compliance with the other standards. In addition, we plan to review the Office of Audit report quality control process.
Continuing Education and Training

Recommendation

"At the time of our review, the OIG was implementing a new Employee Training Inventory system to centrally track and monitor continuing education and training. This system will replace the Training Information Management System used by some supervisors to document continuing professional education credits completed."

"We found that information in the new Employee Training Inventory system was not complete. Specific information for a significant number of OIG employees had not been entered into the system, and information in the system had not been reviewed for accuracy. When the OIG completes and verifies information in the system and establishes effective procedures to ensure information is maintained on a current basis, we believe that the system will adequately monitor compliance with the continuing education and training requirements."

Response

We agree. At the time of the peer review, our Human Resources Division (HRD) was just beginning to collect information to build an automated training system data base. The new system will cover all employees, and, as your report indicates, will fulfill our continuing education and training monitoring requirements. The system will track education, training completed, CPE credits earned, professional organization membership and various other training-related information. The target date for having all information entered into the new automated system, the accuracy of the data verified, and reports issued to management is December 31, 1991. Until then, our various offices will continue to maintain the required data manually or with the PC-based system mentioned in your report.

Organizational Independence of OIG Legal Counsel

Recommendation

"Optimally, legal counsel should be a member of the OIG staff to avoid even the appearance of a conflict of interest or an impairment to organizational independence. If this is not possible, the OIG and OGC should formalize the arrangement with a Memorandum of Understanding."

Response

We agree that the OIG legal counsel should optimally be a member of the OIG staff and independent of the Office of General
Counsel. We are currently working with Treasury officials on this matter.

**Independence of Individual Auditors**

**Recommendation**

"Because it is reasonable to assume that employees in grade 12 and under could have a financial-related impairment to independence, we believe OIG policy should require financial disclosure statements from all staff who are directly involved in audits, regardless of their grade level."

**Response**

We agree that assurance of independence should extend to all staff on an audit assignment, but prefer a different approach to accomplish this assurance. Instead of a financial disclosure statement once a year from each auditor, we are considering requiring each auditor on each audit assignment to complete a "Certification of Auditor's Independence." These certifications will be filed with the assignment workpapers. This statement will address not only financial independence, but all other forms of independence as well.

OIG Manual Chapters 1210 - *Standards of Conduct*, 1220 - *Outside Employment*, and 1230 - *Conflict of Interest*, provide policy and guidelines concerning independence and employee standards of conduct, outside employment, and conflicts of interest. Further, we are revising Chapter 1210 to further define and restrict activities that constitute a conflict or give the appearance of a conflict of interest by OIG employees. The draft of the rewritten version has been approved and should be issued in final form in early 1992.

**Individual Audit Planning**

**Recommendation**

"Audit programs did not always incorporate current GAS and OIG requirements. OIG needs to consistently document:

1. Steps to review Federal Managers Financial Integrity Act reports, GAO reports, and prior audit reports;
2. steps that reference current laws and regulations;
3. steps to assess internal control systems in financial audits or to determine if an internal control assessment is necessary to meet audit objectives in performance audits; and

4. background, objectives, scope, methodology, definition of unique terms, and special instructions in performance audit programs.

The OIG should strengthen individual audit planning processes to ensure these areas are considered in future audit programs.

Response

Although our current policies and procedures concerning audit programs and workpaper documentation represent considerable change and improvement since the period reviewed by the Peer Review Team, we recognize there is still room for improvement.

1. Agree -- Corrective Action Planned. Our current policy process is to review FMFIA, GAO and other reports during the survey phase of the audit. OIGM Chapter 4350, Developing and Using Audit Programs (issued June 20, 1991), requires that auditors review findings and recommendations from GAO and OIG audit reports that relate to the audited area. OIGM Chapter 4340, Audit Surveys (issued March 4, 1991), requires that auditors review FMFIA reports during the survey phase of each audit. The audit team then develops the audit program from the survey results. We, therefore, believe it would be redundant to include this requirement again in the audit program. However, the AIGA will issue by January 31, 1992, an OIG Staff Memorandum requiring the use of a standard survey guide. This guide will require inclusion of a step to review these other reports as required in the above-cited OIG Manual chapters. We will later incorporate the new policy in the OIG Manual.

2. Agree -- Corrective Actions Taken. OIGM Chapter 4350, Developing and Using Audit Programs (issued June 20, 1991), requires compiling and researching pertinent regulations, legislation and directives on the subject audit area. OIGM Chapter 4340, Audit Surveys (issued March 4, 1991), requires reviewing authorizing legislation and applicable program regulations.

3. Agree -- Corrective Action Planned. The AIGA will issue an OIG Staff Memorandum by January 31, 1992, requiring that audit programs include steps to assess internal control
systems in financial audits or to determine if an internal control assessment is necessary to meet audit objectives in performance audits. The staff memorandum will reference OIGM Chapter 4310, Assessing Internal Controls and Compliance with Laws and Regulations (issued June 20, 1991), which provides detailed guidance to auditors for assessing internal control systems in financial audits and determining if an internal control assessment is necessary to meet audit objectives in performance audits. In addition, the staff memorandum will reference OIGM Chapter 4330, Planning Individual Audits, which requires adherence to GAS when assessing internal control systems in financial and performance audits. We will later incorporate the requirements in the staff memorandum into OIGM Chapter 4350, Developing and Using Audit Programs, which has already been issued.

4. Agree -- Corrective Action Implemented. OIGM Chapter 4350, Developing and Using Audit Programs, (issued June 21, 1991) incorporates GAS requirements for preparing audit programs. Specifically, OIGM Chapter 4350 states that audit programs should include sections for background, objectives, scope, methodology, definition of unique terms, and special instructions in performance audit programs.

**Supervision**

**Recommendation**

"GAS requires that staff be properly supervised throughout the audit. Because supervision was not consistently documented in the working papers, we could not always confirm that supervisory activity occurred. We found that OIG needs to routinely document:

- Supervisory approval of audit programs and adherence to and deviations from the program; and

- timely supervisory reviews of working papers and responses to supervisory comments.

At the time of our review, OIG was revising policies and procedures on supervision. The OIG should place a high priority on completing and implementing this guidance and ensure it includes specific guidelines for documenting supervisory reviews."
Response

We have already taken corrective actions in response to internal quality assurance reviews that identified the same weaknesses. The specific actions taken have addressed the two recommendations by the peer review team:

OIGM Chapter 4350, Developing and Using Audit Programs (issued June 20, 1991), requires that each Regional Inspector General for Audit (RIGA) approve audit programs and be advised of any changes to the program. Further, the RIGA must obtain the approval of the DAIGA for Audit Operations for any changes to the program that change the audit objectives or scope. The RIGA must also coordinate such changes with the appropriate Audit Program Director. The RIGA is responsible for documenting the basis for and approval of any deviation from the approved audit program.

In addition, OIGM Chapter 4380, Supervising Audits (scheduled for issuance by January 31, 1992), will also require the responsible RIGA to review and approve audit programs. However, the DAIGA (Audit Operations) will approve those audit programs for highly visible and/or sensitive matters. Moreover, the RIGA and the Audit Manager are responsible for documenting any changes to the scope and/or objectives of the audit and for getting the written approval of both DAIGAs for the changes.

OIGM Chapter 4380, Supervising Audits, will require several different levels of supervisory review. For example, the Auditor-in-Charge must provide the first level of supervisory review of workpapers within 10 days after preparation. The Audit Manager is also responsible for providing a second level of supervisory review at least monthly.

In addition, a draft OIG Staff Memorandum, Workpaper Guidelines, requires the use of a "Supervisory Review Record" to document responses to supervisory comments.

Also, OIG Staff Memorandum 91-OA-05, Documentation of Supervisory Review, dated May 3, 1991, reinforced the requirement to document supervisory reviews of working papers. In addition, the memorandum required the RIGA to review subordinates' workpapers at least every three months related to at least 25 percent of the region's audits. We use OIG staff memoranda to issue timely policy and/or procedure changes. We later incorporate the new or revised policies and/or procedures into the OIG Manual when the pertinent chapter is revised.
Evidence

Recommendation

"To strengthen quality control, OIG should ensure that the policy of having independent, experienced referencers reference reports be strictly enforced. The OIG should also require the referencers to reference substantive changes from draft to final reports. Finally, the OIG should include specific requirements on the level of experience required to reference reports in its policy."

Response

We agree that we need better enforcement of our policy of having independent, experienced referencers. We have taken steps to ensure that this will be done. Recently issued OIG Manual Chapter 4350, Audit Report Referencing (issued March 22, 1991) and a memorandum from the AIGA issued on August 28, 1991, (which was issued in response to an internal Quality Assurance Review finding) should help assure that the OIG policy of having independent, experienced referencers reference reports is enforced. The AIGA will also emphasize this point in meetings with his managers.

Furthermore, we intend to further revise our policy statement and require that all referencers be GS-12 or higher. In extreme circumstances, exceptions to this requirement may be made only with written approval of the cognizant RIGA. This policy will be stated in an OIG Staff Memorandum which will be issued by December 31, 1991. The Memorandum will also assign responsibility to the Audit Manager and Auditor-in-Charge for ensuring that referencers are independent and possess sufficient skills and experience necessary to perform a proper review.

Reporting

Recommendation

1. "The OIG should ensure audit report scope sections fully describe the audit work performed."

2. For financial and financial-related audits "the OIG should strengthen the process for reviewing audit reports to ensure all applicable standards were followed or an appropriate disclosure is made."
Response

The AIGA will ensure that OIGM Chapters 4510, Audit Reporting Guidelines, and 4520, Reviewing and Issuing Audit Reports, now being drafted, will provide procedures and establish controls to ensure that the reporting weaknesses identified by the peer review team are corrected. The draft OIGM Chapters will be finalized in early 1992. Specifically, in response to each of the two peer review team recommendations:

1. **Agree -- Corrective Actions Planned.** Draft OIGM Chapter 4510 will require audit report scope sections to disclose the period covered by the audit, the place where the audit was conducted, types of audit procedures performed, and references to other reports or the work of other auditors. In addition, OIGM Chapter 4520 will contain a report review checklist which will have a step to ensure that scope sections contain the information and disclosures required by GAS.

2. **Agree -- Corrective Action Planned.** Draft OIGM Chapter 4510 will require reports to contain a statement on the auditor's tests of compliance with applicable laws and regulations and on the auditor's understanding of the entity's control structure and the auditor's assessment of control risk. OIGM Chapter 4510 will reference OIGM Chapter 4310, Assessing Internal Controls and Compliance with Laws and Regulations, which provides procedures for assessing and reporting on the auditor's test of compliance with applicable laws and regulations and on the auditor's understanding of the entity's control structure and the assessment of control risk.

Draft OIGM Chapter 4510 will require scope sections to contain a disclosure statement when audit standards were not followed which will explain the exceptions to the standards, the reason(s) for not following the standards, and the known effect on audit results from not following audit standards.

Moreover, draft OIGM Chapter 4520 contains a checklist for reviewing audit reports that strengthens the process for ensuring that all applicable standards were followed or an appropriate disclosure was made.

Policies and Procedures

Recommendations

"As part of the Manual revision process, we suggest the OIG:

1. Develop additional procedures for OIG auditors to use in determining whether to rely upon the work of other
auditors when the report will not make reference to that auditor's work;

2. Develop policies and procedures to address the requirements to assess and report on internal control systems and compliance with applicable laws and regulations;

3. Develop specific policies and procedures to address the requirements and standards for financial audits and financial reporting;

4. Include additional procedures for reporting on personal, external, or organizational impairments in the scope section of the audit report;

5. Identify procedures to report all significant instances of noncompliance and abuse found in connection with an audit; and

6. Clarify the situations in which privileged and confidential information (such as Freedom of Information Act data or classified data) is prohibited from disclosure.

Response

1. Agree -- Corrective Actions Implemented and Planned.
OIGM Chapter 4330, Planning Individual Audits (issued June 20, 1991), Section 6-2, provides procedures to auditors for following-up and relying on the work of others. In addition, draft OIGM Chapters 4510, Audit Reporting Guidelines, and 4520, Reviewing and Issuing Audit Reports, will strengthen the OIG's reporting controls to ensure compliance with GAS 3.40. Specifically, these OIGM chapters will require that when auditors decide to rely on the work of others, but not take responsibility for that work, the audit report scope section must disclose the division of responsibility between that portion of the work the auditors conducted and that conducted by others, and the magnitude of the audit work completed by others. These draft OIGM chapters will be completed in early 1992.

2. Agree -- Corrective Action Implemented. OIGM Chapter 4310, Assessing Internal Controls and Compliance with Laws and Regulations, was issued on June 20, 1991. Sections 2.0 and 3.0 address assessing internal controls and compliance with applicable laws and regulations respectively. Further, Sections 2.7 and 3.7 address the GAS requirement to report on internal control systems and compliance with laws and regulations respectively.
3. **Agree.** Although our OIG Manual Chapters 4110, *General Requirements and Standards for Audit* and 4120, *Requirements for Specific Audits and Technical Assistance* address financial audit requirements and standards, we agree that our policy and guidance, especially concerning financial-related audits, should be more complete. The AIGA will evaluate our current policy statements and develop a Staff Memorandum to restate our policy and guidance in accordance with current standards. This Staff Memorandum will be issued by March 31, 1992, and will be later incorporated into the appropriate revised manual chapters.

4. **Agree -- Corrective Actions Planned.** Draft OIGM Chapter 4510, *Audit Reporting Guidelines*, will require audit report scope sections to explicitly report personal, external, or organizational impairments. In addition, draft OIGM Chapter 4520, *Reviewing and Issuing Audit Reports*, contains a checklist for reviewing audit reports. The checklist will include a step to ensure that audit report scope sections disclose any personal, external, or organizational impairments. OIGM Chapters 4510 and 4520 will be completed during early 1992. Meanwhile, OIGM Chapter 4500, Section 4510 (dated January 11, 1988), requires that audit report scope sections disclose any constraints imposed on the audit approach by data limitations or scope impairments (which would imply an personal, external, or organizational impairments).

5. **Agree -- Corrective Actions Implemented.** OIGM Chapter 4310, *Assessing Internal Controls and Compliance with Laws and Regulations* (issued June 20, 1991), Section 3.7, requires the OIG to report all significant instances of noncompliance and abuse and all indications or instances of illegal acts that could result in criminal prosecution that were found during or in connection with the audit (both performance and financial audits).

6. **Agree -- Corrective Actions Implemented and Planned.** As noted in our written response to the exit conference, OIGM 4320, *Detecting and Reporting Fraud and Illegal Acts* (issued June 20, 1991), provides guidance for instances when information should not be disclosed because of legal considerations, ongoing investigations, grand jury process, security and/or privacy material, court seal, or protective order. In addition, by March 31, 1992, the AIGA will review issued and draft OIG Manual chapters and ensure that the appropriate manual chapters contain clear guidance for situations in which privileged and confidential information (such as Freedom of Information Act data or classified data) is prohibited from disclosure. The policy statement will also provide guidance on scope statements necessary when such information is withheld from the report.
Audit Planning and Universe

Recommendation

"The OIG should take steps to satisfy the requirements of the Circular and the newly developed policy by completing and evaluating the audit universe."

Response

As required by OMB Circular A-73, the Treasury OIG originally issued policies and procedures covering the audit universe and audit planning processes on February 22, 1989, and a revision on July 8, 1991. As required in the original policy, each Audit Program Group (APG), and before them each Director of Audit, obtained the assessable units that each Treasury bureau and the Department identified in the FMFIA process. The APGs or Audit Directors analyzed additional programs, functions and activities that should be considered for the audit universe. This information was reviewed annually by the appropriate APG or Audit Director during the FMFIA process. The universe information is maintained by each APG and before that by each bureau audit site.

The Deputy Assistant Inspector General for Audit Program Services (DAIGA-APS) is responsible for ensuring that each APG effectively carries out his/her responsibilities as outlined in the OIG Manual Chapter 4210, Audit Universe and Profiles, and is responsible for preparing an OIG audit universe, including changes to the universe, at least annually. APGs have been instructed by the DAIGA-APS to update the bureau audit universes by January 1992.

While we are making a concerted effort to update the audit universes, we believe that the audit universe is not the sole instrument for identifying all audit priorities or maintaining effective audit coverage. Because of limited resources, we are concentrating our efforts on those issues we believe represent the Department's most serious management control problems and identifying areas that could result in adverse publicity to the Department.

Sincerely,

Donald E. Kirkendall
Inspector General