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# Audit Handbook for EPA Managers

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*A guide to better audit management  
and effective audit resolution*



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## Introduction

The audit process is viewed as a valuable management tool in EPA. Audits are fully supported by EPA management and should receive your cooperation and attention. To obtain the maximum benefit that you and the Agency can receive from the audit, you should have some knowledge of the audit process.

This handbook has been designed to help introduce you to the audit process. It has been written with the assumption that you will have had little, if any, previous experience with an audit. However, even if you have had previous experience with audits, this handbook should help you to "refresh" your audit management skills.

This handbook approaches the audit "process" as a generic set of steps that are followed

regardless of the organization that is performing the audit. The terms and concepts presented in the handbook are meant to be general; therefore, not every approach will be applicable to every audit you may encounter. The appendix to this handbook contains a list of definitions of terms that may be new to you. It may be useful to refer to the appendix from time to time to clarify the terms that are used in the handbook.

This presentation is intended to be non-technical and will not contain all the information that you would need to become an "expert" in audit management. Your audit follow-up coordinator will have received the training necessary to coordinate the audit process and should be able to provide you with additional guidance.

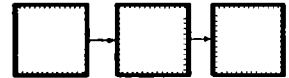
## Inspector General Act Amendments of 1988

The Inspector General Act Amendments of 1988 made significant changes to the audit resolution, followup and reporting process.

For the first time, management is required to report directly to the Congress, semiannually, on audit resolution and followup activities. The report must contain a table showing the dollar value of "disallowed costs," and a table showing the value of "recommendations that funds be put to better use," agreed to in a "management decision." Management must also explain why "final action" remains incomplete on any audit report one year following a management decision.

The Amendments contain new definitions of terms, which are included in Appendix D of this handbook. An executive summary of the Amendments appears in Appendix E.

At the time of this writing, the Resource Management Division of the Office of the Comptroller is coordinating the development of a new audit followup tracking system to meet the requirements imposed by the Amendments to the Inspector General Act.



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## Audits and the Audit Process

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### Types of Audits

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EPA managers will most likely face audits performed by the EPA Office of Inspector General (OIG) or the U.S. General Accounting Office (GAO).

The GAO primarily conducts *expanded scope audits*. These audits can cover the financial operations of your organization, the economy and efficiency with which your organization is managed, and the program results achieved by your organization.

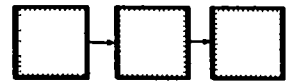
The OIG conducts audits that may cover any of the areas of the expanded scope audit. There are two general categories of OIG audits:

- **Internal audits** are performance audits which test program effectiveness, compliance with program laws and regulations, and program results. They may include economy and efficiency tests — in some cases the reviews will be extended to state or other agencies that have been delegated operational responsibility for the program being reviewed.
- **External audits** are financial audits, usually of EPA assistance recipients' financial statements or financial related systems, controls and funds. They include tests of specific financial compliance with established rules, regulations and agreements. They also may include economy and efficiency tests — these could be reviews before, during or after completion of the assistance agreement.

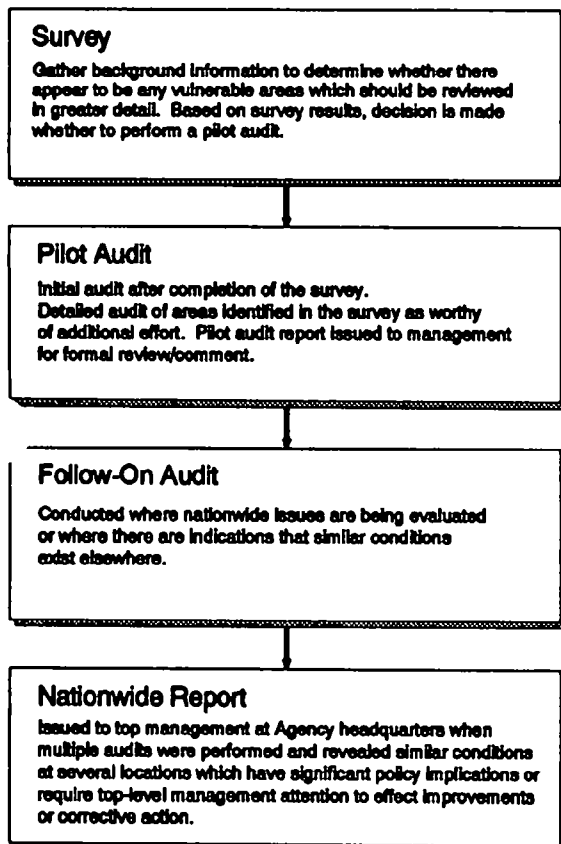
While the majority of audits conducted are external audits of grant recipients, they affect only a few managers. On the other hand, the relatively few GAO and OIG internal audits affect and will involve nearly every manager at one time or another.

Audits can be further classified by audit phase:

- **Survey**—Data gathering to gain background information on a program, activity, or function. The purpose is to assess whether there appear to be any vulnerable areas which should be reviewed in greater detail.
- **Audit**—An evaluation of a program, activity, or function in accordance with GAO standards.
- **Pilot Audit** — The pilot audit is normally a detailed audit of the areas identified in the survey as worthy of additional effort. The term "pilot" is used when it is expected that a follow-on audit will occur.
- **Follow-on Audit** — Audits conducted in cases where issues are being evaluated in which there are indications that similar conditions exist within a function or activity at more than one location.
- **Nationwide Report**—Consolidation of the results of work at several locations around the country into a national report.



## OIG Audit Phases



## The audit process

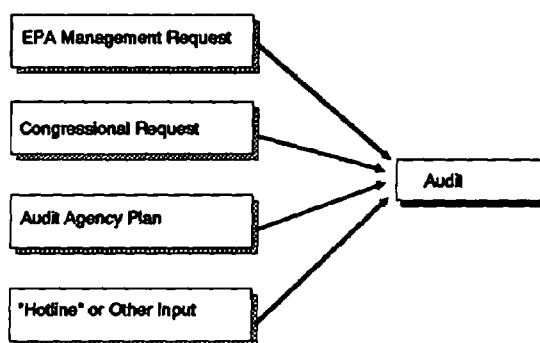
The OIG and GAO have established procedures for conducting audits of EPA programs. No one regulation or manual discusses the process for conducting an audit; however, audit procedures exist in both the OIG and GAO. This section discusses the audit process that is typically followed.

■ *Selecting the audit.* Audit areas are selected according to several factors. The OIG determines the areas to audit based on input from EPA AAs and RAs, other Agency officials, and OIG management and staff. In addition, the OIG may audit areas identified through its "Hotline" or based upon input from other sources. The areas selected for audit are then incorporated into an annual audit plan. The annual audit plan is updated quarterly. Your audit follow-up coordinator should have a copy of the audit plan and inform you if your area is identified for an audit.

Both the OIG and GAO may perform audits that are mandated by statute or regulation, or that are requested by Congress. The GAO identifies audit areas based on input from Congress, EPA officials and GAO management and staff. However, most of the audits performed by GAO are either legislatively mandated or requested by a member of Congress or a Congressional committee.



### What Starts the Audit Process?



■ **Entrance conference.** Both the OIG and GAO conduct entrance conferences. At the entrance conference, the auditors explain the purpose and scope of the audit and receive comments from Agency personnel regarding areas that could be included in the audit. Logistical issues are addressed, such as access to records, working space requirements, and interview lists.

The personnel attending the entrance conference should include the senior managers responsible for the areas being audited, those with technical expertise or extensive knowledge of the area being audited, and those who have experience with the audit process.

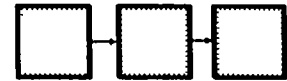
■ **Advisement of findings.** As the audit is conducted, the auditors should provide Agency management with feedback about preliminary findings and developing audit issues. This can best be done through written "position papers."

The advisement of findings allows the Agency managers to address misunderstandings and factual inaccuracies. If, during the audit process, you feel that the auditors are misinterpreting information or are developing findings that you feel — based on the facts — are incorrect, you should immediately discuss your concerns with the lead auditor and explain your interpretation of the situation. In addition, for those preliminary findings that you feel are accurate, you should immediately begin to take corrective actions to address weaknesses that are identified.

■ **Draft report.** A draft report is usually issued shortly after the audit is completed. The report contains the auditors' findings and supporting evidence for those findings.

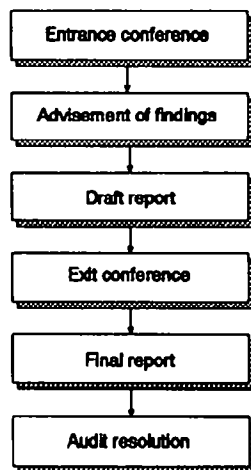
Agency management is expected to provide a written response to the audit findings contained in the draft report, either concurring with the findings or providing explanations for any disagreements with the findings. In addition, any corrective actions that have been planned or implemented should be described in the response. The written response should be provided within 30 days of receipt of the draft report.

Your goal should be to *resolve* the findings identified during the audit and within the audit report. You should not concentrate solely on *writing* a response to the report findings. *As soon as a problem is identified, it is important to start corrective actions.* By starting corrective actions immediately, you will place yourself in a better position to resolve the audit findings before the final audit report is issued.



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## The Audit Process



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■ **Exit Conference.** An exit conference is held to discuss the audit findings and clarify questions the auditors or Agency management may have regarding the audit. Information should be exchanged between the auditors and Agency management in order to reach agreement on the audit results.

■ **Final report.** The final audit report contains the auditors' findings and recommendations. It should reflect the pertinent information obtained from the audit and from the discussions with Agency management throughout the audit process.

The response should address the audit recommendations, either concurring with the auditors' opinions or providing alternative corrective actions to address the problems that were identified.

■ **Audit resolution.** Audit resolution occurs when a "final determination" is made for the findings in an external audit, or when a "final response" to the audit findings is issued for an internal audit. Audit resolution requires the timely and appropriate response to an audit report by the Action Official (the Action Official for internal audits is usually the Regional Administrator or Assistant Administrator; for external audits, the Action Official is usually a designee of the RA or AA).

For OIG audits containing significant findings, the Action Official must obtain the concurrence of the OIG on proposed corrective actions. The audit will be considered resolved when the OIG and Action Official agree upon the proposed corrective actions.

■ **Resolving disagreements.** If the Action Official and OIG do not reach agreement on an audit, the OIG may refer the case to the Audit Review Group (ARG) and Audit Resolution Board (ARB). In addition, the Agency Follow-Up Official may select for review an audit for which resolution is overdue. The Agency Follow-Up Official will attempt to facilitate a resolution to the audit. If unsuccessful, the ARG will review the case and issue a recommendation. The ARB will consider this recommendation and issue a final decision that will be binding upon the Action Official and the OIG.



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# How to Prepare for the Arrival of an Auditor

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## Introduction

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A few hours spent preparing for an audit before the audit starts can save the expenditure of many staff hours during the audit—responding to auditors' requests for information—and after the audit—resolving audit findings. The following items are provided as suggestions to assist you in preparing for an audit. Proper planning and preparation should result in an audit that progresses smoothly and minimizes the impact on your staff and your ability to complete day-to-day work during the audit.

The GAO or OIG normally will contact your audit follow-up coordinator at least two weeks prior to the start of an audit or review to arrange for an entrance conference with appropriate officials. At this time the auditors will also usually identify any special needs they have or information they will require. The audit follow-up coordinator will be responsible for much of the logistical arrangements prior to the audit.

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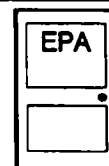
## Preparing for the audit

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■ *Designate an audit contact point.* After you are notified by your audit follow-up coordinator that an audit will be performed, you should designate an audit contact point within your immediate organization. This contact point should be responsible for managing logistical issues, responding to auditor inquiries, and tracking the progress of the audit. In addition, Agency staff, state program officials, and private individuals that will be affected by the audit should be informed. These individuals should, in turn, prepare their respective organizations for the audit process.

■ *Prepare for the entrance conference.* Ensure that appropriate personnel who are to attend the entrance conference are briefed on any information that is available regarding the audit. Appoint someone to take notes at the entrance conference. Make copies of those notes for your records and send to members of your organization who participated in the entrance conference and were involved with the audit. The audit follow-up coordinator will take notes and will copy you. The coordinator will also be responsible for following up on additional administrative needs of the auditors.





■ *Identify individuals who will be participating in the audit.* The audit follow-up coordinator may ask for a listing of Agency personnel the auditors should contact. Ask for a list of the audit personnel and the auditor-in-charge. Exchange these lists with the auditors and those involved with the audit. Contacts the auditors have within your organization should be coordinated through the audit contact point.

■ *Determine the scope of the audit.* The audit follow-up coordinator will brief you and will provide any available information and materials concerning the planned audit's scope of review. There will be an entrance conference during which you should ensure that you fully understand the scope of the audit. Determine if your audit follow-up coordinator or the Agency Audit Follow-up Coordinator knows of similar audits that have been performed in the past on other similar organizations (e.g. in other regions or in other agencies). Review the results of the audits with these organizations if possible.

■ *Plan the logistics of the audit.* During the initial contacts with the audit organization, the audit follow-up coordinator will ask the auditor-in-charge about the number of personnel that will participate in the audit and space and furniture requirements. The audit follow-up coordinator will ask for your assistance to locate appropriate space in or near your organization. Determine how long the auditors plan to remain on-site so that the space can be reserved for them. Also, determine if the auditors will need space to conduct private interviews.

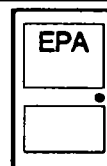
■ *Determine what documents or materials are needed.* Provide the individuals who will be involved with the audit with the documents they will need to prepare for the audit. Manuals, regulations, orders, and other documents pertinent to the audit should be collected. Those involved with the audit should be informed of what documents they may need to provide to the auditors. Each should familiarize themselves with the content of these documents before the audit begins. It is often useful to keep a central list of copies of documents provided to the auditors since these may be needed to respond to the audit report.

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## During the audit

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During the audit most of the burden for coordination and communication is your responsibility or as you delegate to your contact person. You must assure that your staff and delegated state staff are available to the auditors and are fully cooperative. The audit follow-up coordinator will be available to assist you with logistical or administrative problems and in clearing the auditors into other organizations, as the need arises.



■ ***Establish a centralized audit information file.*** To the extent possible, the audit contact point should maintain a listing of documents provided to the auditors both voluntarily or at their request. The file should also include all relevant and substantive correspondence and notes from meetings with the auditors. This information can be used to prepare for the exit conference and help you formulate responses to the draft and final reports.

■ ***Meet periodically with the auditors.*** You or your audit contact point should meet periodically with the auditors to track the progress of the audit and ensure that information requested by the auditors is provided to them in a timely manner. The audit follow-up coordinator should attend all progress meetings. In cases where multiple organizations are involved, the audit follow-up coordinator will arrange joint meetings. You should also ask the auditors to brief you on any preliminary findings they may have. Any problems that arise with regard to the audit process should be addressed in these meetings as expeditiously as possible.

■ ***Look for weaknesses and start corrective actions.*** When problems are identified — either by you, your staff, or the auditors — start corrective actions as soon as possible. It is important to begin corrective actions quickly since the goal of an audit is to identify and *correct* weaknesses. By taking corrective action early, you can place yourself and the Agency in a positive position and demonstrate that audit findings are being resolved before the final audit report is issued. When the problem is identified by the auditors, provide the background information on the problem, explain why the problem exists, and describe the corrective actions that are being taken, as appropriate.

■ ***Prepare for the exit conference.*** The audit follow-up coordinator is responsible for arranging the exit conference and ensuring each affected organization is represented. You should ensure that the appropriate personnel—for instance, those who can respond to the audit findings—attend the exit conference. Use the information obtained from your meetings with the auditors to prepare responses to preliminary findings. Clarify questions you or the auditors may have concerning the facts in the case. As with the entrance conference, appoint someone to take notes. The audit follow-up coordinator will send a follow up memo to the attendees of the exit conference on any agreements reached in the meeting.



## **Do's and Don'ts when Interacting with Auditors**

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### **Introduction**

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EPA management emphasizes the importance of timeliness and quality in audit resolution. The goal of management in EPA and the Office of the Inspector General is to reach an appropriate and agreeable resolution to audits in a timely manner. One of the keys to resolving audits in a timely manner is the establishment of a constructive working relationship with the auditors.

To help you as an EPA manager in working with auditors from either the EPA Office of the Inspector General auditors or the General Accounting Office, a list of "do's and don'ts" is presented in this section. The following listing should be used as a guide to help you when working with auditors.

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### **What to DO when interacting with auditors**

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- ✓ **Be cooperative**—provide all documents or information requested by the auditors in a timely manner.
- ✓ **Be responsive**—if you cannot provide the information by the time the auditor requests, indicate when the information can be made available.
- ✓ **Prepare for an audit**—review the audit directives to determine what the auditors will be looking for and the information you will be expected to provide.
- ✓ **Organize your records so pertinent documents will be available upon request**—keep all pertinent regulations, manuals, orders, operating procedures, and desk procedures current.
- ✓ **File all documents relevant to the audit**—everything in the official file is subject to review including memos for record, notes, telephone messages, and other form of documentation.
- ✓ **Communicate to the auditors the actions you have undertaken to improve problem areas and resolve outstanding issues.**



- ✓ **Schedule times to meet with the auditors on a periodic basis throughout the audit process.**
- ✓ **Volunteer to have follow-up meetings with the auditors if there are any questions.**

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## **What NOT to do when interacting with auditors**

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- ⊗ **Do not withhold information from an auditor—**They can examine almost anything they want within your organization. Attempting to withhold information will only complicate the audit.
- ⊗ **Do not take an audit personally—**it is a tool to help you identify where weakness exist, if any, and help you resolve them.
- ⊗ **Do not lie or be evasive—**do not try to hide problems or cloud the issues. Provide the auditors with data that they request or data that they need to understand the issues, but do not overwhelm them with information they do not need.
- ⊗ **Do not delay or hold up the audit—**schedule your time to complete your own work but leave adequate time for the auditors.
- ⊗ **Do not let potential audit findings get between you and the auditors—**cooperate and demonstrate steps already taken to resolve the issues or agree to begin to take corrective action if warranted.
- ⊗ **Do not get upset with the prospect of being audited—**you know more about your program than anyone else; demonstrate your knowledge.
- ⊗ **Do not treat an audit as a “one time” problem to get over with as soon as possible—**audits are ongoing management tools that should be understood and used to the Agency’s advantage.
- ⊗ **Do not get defensive with an auditor—**your goal should be to make all interactions with the auditors constructive.
- ⊗ **Do not look at an audit with a “them vs. us” mentality—**work together as a team and communicate with people in other regions or states to obtain information.



## Questions to Ask Before, During, and After an Audit

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### Introduction

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This section deals with questions you should address before the audit starts and issues that may arise during the course of the audit. Many problems associated with audits can be mitigated by effective planning before and during the course of the audit. The following list of questions and answers should help you prepare for an audit and identify the procedures you should understand and follow during the audit.

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### Before the audit

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■ *What is the best way to prepare for an audit?*

When you are notified of an audit, you should designate individuals within your organization that will be responsible to gather information and respond to the auditors' requests for information. These individuals should consist of key personnel who have technical or programmatic knowledge that would be valuable within the audit, senior managers that can respond to policy questions raised by the auditors, and state program officials, if appropriate.

■ *What is the best way to compile information to prepare for an audit?*

The key individuals involved with the audit should collect the necessary documentation required for the audit. Other organizations similar to yours—both within the region and in other regions—who have been audited in the past should be contacted, if possible, to gather information about their audit experiences. Within the organization being audited, a contact point should be designated through which the auditors can request information and set up appointments to interview personnel. The contact point should keep a record of all requests for information and the date the response was provided.

■ *Once the momentum is started how should it be maintained?*

Frequent meetings should be held with the individuals involved with the audit to exchange information. Relevant information that is collected from other organizations should be communicated to personnel who will be directly affected by the audit. Additional requirements for data can be assigned and discussed in subsequent meetings. At this early stage procedures should be established to manage the audit—i.e., progress meetings, points of contact, who attends the entrance conference, etc.

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## During the audit

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■ *What should I do if a significant problem is brought to my attention by an auditor?*

Senior EPA management should be advised immediately of any significant or sensitive audit finding that is brought to your attention during the course of the audit. The Agency has established an “early warning system” in which you have the responsibility to notify senior management about all significant or sensitive audit findings and any corrective actions that are planned or have been taken to address the findings.

The early warning system is intended to keep management apprised of developing audit issues and to ensure that corrective actions are begun early in the audit process. Any audit issues raised by the auditors that cannot be addressed by you or your staff should be referred immediately to senior EPA management for resolution.

■ *Will I know there are findings in my area before the audit report is published?*

You should work out arrangements with the auditors to receive position papers to insure that you are kept informed of findings as they are developed. At the entrance conference, you may want to discuss with the auditors what arrangements they have to present position papers. At a minimum the position papers should help you to confirm the information obtained by the auditors and allow you to begin corrective actions before the draft report is issued.

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## After the audit

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■ *What information is required for the audit follow-up process?*

Responses to draft audit reports should be developed and presented in written form and at the exit conference (if the exit conference is held after the draft report is issued). Each finding contained in the draft report should be addressed in your response. Supporting evidence for disagreements with the report should be provided in your response.



Responses to final audit reports should address the recommendations contained in those reports. Alternative solutions should be presented, if appropriate. OIG concurrence should be obtained on any sensitive or significant issues.

■ *How soon can corrective actions be implemented?*

Corrective actions should be implemented as soon as a weakness is identified. In addition, any corrective actions begun during the audit should be brought to the attention of the auditors and included in responses to the draft and final reports. Once the audit is resolved, the progress of corrective actions will be tracked by your audit follow-up coordinator and reported to the Agency Audit Follow-Up Coordinator.



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# How to Respond to Audit Findings

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## Introduction

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This section discusses how you should respond to findings in various types of audits and what you need to be aware of when writing a response to the draft and final audit report. The responses to audit findings will differ with every audit; however, there are common issues that should be addressed in order to satisfactorily respond to audit findings.

■ *You should have as a goal the early resolution of audit findings. To accomplish this goal, you should respond to audit findings as soon as they are communicated to you, preferably while the audit is being performed.*

The position papers presented to you during the course of the audit are intended to allow you to start to resolve findings *before* the issuance of the draft report. By responding to the position papers positively and quickly, you will give yourself and the Agency the opportunity to resolve the audit findings before the audit report is issued in final form.

■ *The Action Official is the person responsible for ensuring that responses to audit findings are completed in a timely and appropriate manner. In addition, the Action Official must ensure that necessary corrective actions are implemented in response to audit findings.*

The Action Official is either your Regional Administrator or Assistant Administrator, or individuals designated by them. Frequently, the action official who must provide the Agency response to the audit report is identified in the OIG cover letter transmitted with the draft audit report. You may be asked to help develop the response to the audit report. The audit follow-up coordinator will help coordinate this process and ensure that the deadlines for constructing responses are met.

■ *Time and attention should be devoted to responding to the draft report, even though less time is allowed to review and respond to draft reports than to final reports. The primary purpose of responding to the draft is to clarify facts and to respond to the auditors' findings.*

The comments provided on the draft report may be appended to or incorporated in the final report and addressed by the auditors in the final report. Thus, the manager should take the time to make an articulate presentation on the findings contained within the draft report and propose alternative approaches to the report's content and presentation, where appropriate.

■ *Responses to the final audit report should focus on the recommendations (for an internal audit) or provide a final decision on each cost questioned or set aside (for an external audit).*





References to the *findings* in a final report should only be made where necessary to explain the reason for a particular decision or action.

As a manager responsible for an audit, your response to findings and recommendations can differ significantly depending on the type of audit with which you are dealing. The following discussion deals with two types of audits and the requirements to respond to findings and recommendations contained within the audit reports.

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## Internal audits

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Beginning corrective action as soon as a problem is identified is a very important step in responding to findings in the draft internal audit report. The earlier you begin corrective actions, the more quickly the audit issues can be resolved.

You and everyone involved with the audit should communicate with each other before and during the audit to identify potential audit findings and begin action to correct existing weaknesses. Periodic meetings between you (or the audit contact point) and the auditors can help you to identify potential findings—if the auditors provide position papers—and help you to begin corrective actions immediately.

As soon as the draft report is published the audit follow-up coordinator should help you establish deadlines that must be observed to resolve the audit in a timely manner. You should distribute the report to the staff who were involved with the audit and enlist their support to develop responses to audit findings and recommendations. Where the audit included an evaluation of program results of delegated states, ensure that your response includes their input.

The audit report should be read carefully and checked for its accuracy. Any factual inaccuracies should be noted and clarified in your response.

■ *Any findings contained within the draft report must be addressed in your response.* If you disagree with any findings, you should explain why you disagree and provide support for your argument. If you have begun to take corrective actions and these are not described in the report, you should include a description of these actions in your response. Taking corrective actions—and providing details about these actions—is one of the best methods available to minimize the negative impacts that an audit could otherwise produce.

■ *When the final audit report is received, any recommendations contained in the report must be addressed.* You should state whether or not you concur with the recommendations. If you disagree with a recommendation, you must explain why and, if possible, provide an alternative solution. If you have an alternative recommendation to propose to fix the cause of a problem, you should include this information in your response.

All responses to draft (and final) audit reports must be for the signature of the action official. The audit follow-up coordinator is available to assist in developing responses; in many organizations the coordinator is responsible for reviewing all responses for completeness and responsiveness to all findings and recommendations.



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## External audits

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Audits of this nature may involve cooperative agreements, grants or contracts. As such, they may involve personnel such as state officials, contractors, municipalities, and organizations outside the direct control of the EPA.

■ *External audits may require the recovery of funds from grant recipients. As such, recoveries increase the potential for the expression of outrage from the grant recipient, inquiries from Congress, and the filing of a dispute for resolution by the Regional Administrator.*

Large disallowances of cost or recoveries of funds will also likely be reported in the OIG's semiannual report to Congress. For these reasons, program managers as well as ARAs and RAs need to pay attention to what is happening in external audits. Managers need to be aware of sensitive and significant audit findings or cases where large recoveries may be involved.

The Action Official is responsible for making final dispute decisions on audit findings and recommendations for all audits of cooperative agreements or grants, or of contractors under such agreements. In some regional offices, the audit follow-up coordinator may serve in this role. The appropriate contracting officer is the action official responsible for making final decisions on audit findings and recommendations of direct EPA contractors. In all cases, the Action Official or audit follow-up coordinator will keep you apprised of the status of the audit report response and will often seek your technical or programmatic input to resolve audit findings.

Any disagreements with the findings and recommendations should be noted in a response to the auditors and supporting evidence for an alternative position should be supplied to the auditors.

■ *External audits which contain \$100,000 or more of Federal questioned costs require the concurrence of the OIG before the audit is closed. If there are any sensitive or significant issues involved in the audit, you need to be aware of and agree with the conclusions and recommendations that are associated with the sensitive or significant findings before the determination is sent to the OIG.*

An inability to reach agreement with the OIG on an external audit may result in a referral of the audit issue to the Agency Follow-up Official for possible review by the Audit Review Group or Audit Resolution Board.

■ *The grant recipient has the right to formally dispute an audit determination to the Regional Administrator and, ultimately, to the program Assistant Administrator. Disputes can be very resource intensive and will bring the audit decision-making process under scrutiny within the region. Managers and audit follow-up coordinators should look for trends in disputes as an indicator of how well the audit resolution process is working.*



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## Elements of a response

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There is no easy definition of what constitutes an effective response to an audit finding. You must respond to each finding, whether or not you concur with the finding. If there are disagreements, discuss the issues fact by fact. Section 2, Chapter 109 of the OIG Manual discusses the elements of an audit finding. These elements are discussed here to assist you in preparing an effective response.

Audit findings, regardless of the subject matter, have four common elements. These include a comparison of “what should be” (criteria) with “what is” (statement of condition) and an answer to the question “what does this mean?” (effect). Further, if an audit report is to be constructive, the reasons “why” (cause) there is a difference between “what is” and “what should be” must be identified and explained. Once the cause is identified, the next logical step is to make a recommendation that will help prevent a reoccurrence of the problem. These terms are discussed below in more detail.

■ **Criteria.** Criteria are the standards against which an auditee is measured for a questionable condition or performance. Published criteria may be directly quoted, summarized, or paraphrased. Some examples of criteria are:

- Written requirements (laws, regulations, directives, etc.)
- Common sense.
- Independent opinion of experts outside the Agency.
- Prudent business practice.

- Oral instructions.
- Managerial expertise.
- Unwritten overall objectives as explained by management officials.

■ **Condition.** An overall statement of the situation that exists in the program or activity under review. It relates to the extent that goals or objectives of a program are being achieved. Some examples of condition are:

- The procedures that are being followed or not being followed.
- The controls that are in place or not in place.
- A description of how the program or activity was implemented or not implemented.
- A description of how the program or activity works or does not work.

■ **Cause.** Cause is the underlying reason why the questionable performance or condition occurred—the reasons for the questionable action, lack of action, weakness, deficiency, or inadequacy. Why did it happen? Why was there noncompliance? Some examples of cause:

- Lack of training.
- Lack of communication.
- Unfamiliarity with requirements.
- Negligence or carelessness.
- Guidelines or standards are inadequate or not provided.
- Lack of resources (funds or staff).
- Failure to use good judgment or common sense.
- Unwillingness to change.



- Lack of adequate control mechanisms or devices.

■ *Effect.* Effect is the actual or potential result of the condition being questioned, in dollar or other terms which may not be as readily measurable. Some examples of effect are:

- Uneconomical or inefficient use of resources (time, money, manpower).
- Violation of law.
- Funds improperly spent.

- Information or records which are not useful or meaningful or which are inaccurate.
- Inadequate control or loss of control over resources or actions.
- Lowered morale.

By understanding the common elements of an audit finding you should be able to respond to findings more effectively. Your responses to audit findings will differ depending upon the nature of the finding; however, by ensuring that the common elements of every finding are addressed, your responses will be more complete.

## **Appendix A**



# **Benchmark Questionnaire —Audit Preparedness**

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## **Introduction**

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The following questions are provided as a benchmark for EPA managers to use to check the capability of their organizations to deal with an audit. The managers can use this questionnaire to assess their own knowledge of the audit management process. The questionnaire is not intended as a substitute for managers to familiarize themselves with the agency's audit regulations and procedures. The questionnaire is intended to be used as a tool to allow managers to quickly assess their organizations' readiness to deal with an audit. As managers gain more experience with the audit process, they may want to add to this list the unique aspects of the audits they encounter.

The "Audit Handbook for EPA Managers" is designed to answer these and other questions EPA managers may have concerning the audit process. Additionally, each headquarters office and regional office has a designated audit follow-up coordinator who serves as a focal point for communication with the GAO and EPA's Office of Inspector General. As such, the audit follow-up coordinators are responsible for overall audit management for their organizations. You should determine who is your audit follow-up coordinator and use that person as a resource as you become involved in audits of your program.

Determine the extent to which you can answer each of the following questions. If you do not know the answer, you should seek additional guidance from your audit follow-up coordinator.



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## Prior to the audit

---

	I know the answer	I need addi- tional infor- mation
Are the procedures and controls within my organization logical and documented?	_____	_____
— Are they being followed?	_____	_____
Is my organization operating economically and efficiently?	_____	_____
— What can be done to improve our economy and efficiency?	_____	_____
Are procedures established to inform me of potential problems in my programs?	_____	_____
— When were the areas of potential weaknesses last addressed?	_____	_____
What are the outstanding policy issues in the programs and organizations, and what additional information is required to properly respond to an audit?	_____	_____
— What actions have to be taken to resolve the policy issues, and the timing of such resolution?	_____	_____
How does the agency notify managers of pending audits? Are the audit plans communicated to the managers regularly, are they available?	_____	_____
— How much time will I have to brief my personnel or other organizations with which we work?	_____	_____



	I know the answer	I need addi- tional infor- mation
Has my program been audited before?	_____	_____
— Where are the reports of previous audits maintained?	_____	_____
What are the results of previous audits?	_____	_____
— Have the corrective actions been implemented properly?	_____	_____
Have audits been performed in other EPA organizations similar to mine?	_____	_____
— Could the findings, conclusions, and recommended actions also apply to my program?	_____	_____
Who is the audit follow-up coordinator in my organization?	_____	_____
— What information might the audit follow-up coordinator have that may apply to my program?	_____	_____





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## After the audit is announced

---

	I know the answer	I need additional information
Who is conducting the audit (OIG, GAO)?	_____	_____
— Do I understand the audit process?	_____	_____
When will the entrance conference be held?	_____	_____
— Who should attend the entrance conference?	_____	_____
Who should be involved with the audit—collecting and providing information and maintaining a copy of all documents provided to the auditors?	_____	_____
— Who should be the contact point in my program area to work with the auditors, to manage logistics, and to set up interviews?	_____	_____

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## At the entrance conference

---

What type of audit will it be (Survey, Pilot Audit, Follow-on Audit)?

    — What prompted this audit?

Is this a region-specific audit?

    — Will there be a region-specific draft report?



I know the  
answer

I need addi-  
tional infor-  
mation

What are the audit scope and objectives?

\_\_\_\_\_

\_\_\_\_\_

— What unique preparation is required for the audit?

\_\_\_\_\_

\_\_\_\_\_

Who is the auditor-in-charge?

\_\_\_\_\_

\_\_\_\_\_

— Who will be working on the audit?

\_\_\_\_\_

\_\_\_\_\_

Will the auditors want to interview personnel in state or local agencies or other EPA organizations?

\_\_\_\_\_

\_\_\_\_\_

— Who will be involved at the state or local level and who will make the arrangements? Will an exit conference be conducted at the state or local agency before the draft report is issued?

\_\_\_\_\_

\_\_\_\_\_

Will the auditors provide position papers before the draft report is published?

\_\_\_\_\_

\_\_\_\_\_

— If not, how can information on potential findings be provided to me so I can start corrective actions at the earliest possible date?

\_\_\_\_\_

\_\_\_\_\_

Will I be provided with flash reports?

\_\_\_\_\_

\_\_\_\_\_

— How do I communicate significant and sensitive audit findings to upper management?

\_\_\_\_\_

\_\_\_\_\_

To what extent are the auditors familiar with the area they are auditing?

\_\_\_\_\_

\_\_\_\_\_

— What information could prove helpful to the auditors to prepare them for their assignment?

\_\_\_\_\_

\_\_\_\_\_

## **Appendix B**



## Audit Engagement Checklist

- This "Audit Engagement Checklist" was developed by an EPA regional office to identify the information that should be obtained from the auditors before the audit is started. You can use this as it is presented or modify it to help you gather the information that will help you better manage the audit process.

### 1. Notification

Date: \_\_\_\_\_

Name/Organization: \_\_\_\_\_

Telephone Number: \_\_\_\_\_

Who is conducting the audit:

OIG    \_\_\_    Office: \_\_\_\_\_

GAO    \_\_\_    Office: \_\_\_\_\_

Other   \_\_\_    Identify: \_\_\_\_\_

### 2. Description of the audit

Title: \_\_\_\_\_  
\_\_\_\_\_

Audit scope and objectives:

\_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_



Audit period: \_\_\_\_\_

Financial and Compliance: \_\_\_\_\_ Survey: \_\_\_\_\_

Economy and Efficiency: \_\_\_\_\_ Pilot: \_\_\_\_\_

Program Results: \_\_\_\_\_ Follow-on: \_\_\_\_\_

Previous audits: \_\_\_\_\_

Audit report number: \_\_\_\_\_

### **3. Audit management group**

Audit Focal Point: \_\_\_\_\_

Area Contact Point: \_\_\_\_\_

Others: \_\_\_\_\_

\_\_\_\_\_

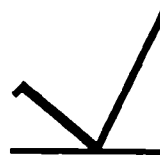
\_\_\_\_\_

### **4. Entrance conference**

Date: \_\_\_\_\_

Time: \_\_\_\_\_

Location: \_\_\_\_\_



## 5. Logistics

Field work (start/stop): \_\_\_\_\_  
Number of auditors on site: \_\_\_\_\_  
Space: \_\_\_\_\_  
Phone: \_\_\_\_\_  
File storage: \_\_\_\_\_  
Other: \_\_\_\_\_

## 6. Briefings (status reports)

Weekly: \_\_\_\_\_  
Bi-weekly: \_\_\_\_\_  
As requested: \_\_\_\_\_

## 7. Reporting procedures

Preliminary findings: \_\_\_\_\_  
Draft report: \_\_\_\_\_  
Final report: \_\_\_\_\_

## 8. Information requested prior to the entrance conference

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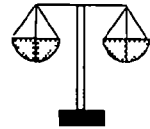
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## **Appendix C**



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# Standards for Audit

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## Introduction

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The "Standards for Audit of Governmental Organizations, Programs, Activities, and Functions" are issued by the Comptroller General of the United States. The standards are published in what is commonly referred to as the GAO "Yellow Book." The Yellow Book was revised in 1988; therefore, this summary is based on the 1988 edition.

The standards are to be followed by all Federal auditors and all non-Federal auditors who perform audits of Federal organizations. The standards include those established by the American Institute of Certified Public Accountants (AICPA) for financial audits and establish additional guidance for non-financial audits.

■ *In your position as an EPA manager, you should be aware of the audit standards in order to help you understand how auditors perform their work, what they look for during an audit, and how audit information will be conveyed to you and the public.*

In rare circumstances, an understanding of the audit standards may also help you identify situations in which an auditor may be acting in a manner that does not meet the standards. If such a situation occurs, you should raise your concern with the auditor and, if necessary, discuss the issue with the auditor-in-charge and your audit follow-up coordinator.

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## Types of audits

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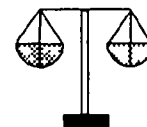
Government and nongovernment auditors conduct audits of government organizations, programs, activities, functions, and funds. This description is not intended to limit or require the types of audits that may be conducted but give an understanding of the types of audits that may be conducted. In conducting these types of audits, the Yellow Book sets applicable standards that auditors should follow.

All audits begin with objectives and those objectives determine the type of audit to be conducted and the audit standards to be followed. The types of government audits are classified as financial audits or performance audits. The Yellow Book lists detailed descriptions of the two types of audits:

Financial audits - include financial statement and financial related audits.

1. Financial statement audits determine (a) whether the financial statements of an audited entity present fairly the financial position, results of operations, and cash flows or changes in financial position in accordance with generally accepted accounting principles, and (b) whether the entity has complied with laws and regulations for those transactions and events that may have a material effect on the financial statements.





## Objectives of Financial Audits

### Financial Audits

Determine whether

- 1 The financial statements present fairly the financial position and the results of financial operations, and cash flows or changes in financial position
- 2 The entity is complying with laws and regulations for those transactions and events that may have a material effect on the financial statements

### Financial Related Audits

May include the following

- 1 Segments of financial statements
- 2 Financial information
- 3 Reports and schedules on financial matters
- 4 Contracts
- 5 Grants
- 6 Internal control systems and structure
- 7 Computer-based systems
- 8 Financial systems (e.g., payroll systems)
- 9 Fraud

2. Financial related audits include determining (a) whether financial reports and related items, such as elements, accounts, or funds are fairly presented, (b) whether financial information is presented in accordance with established or stated criteria, and (c) whether the entity has adhered to specific financial compliance requirements.

Performance audits include economy and efficiency and program audits.

## Objectives of Performance Audits

### Economy and Efficiency

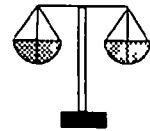
Determine whether the entity

- 1 Is following sound procurement practices.
- 2 Is acquiring the appropriate type, quality, and amount of resources when needed at the lowest cost.
- 3 Is properly protecting and maintaining its resources
- 4 Is avoiding duplication of effort by employees and work that serves little or no purpose
- 5 Is avoiding idleness and overstaffing
- 6 Uses efficient operating procedures
- 7 Is using the minimum amount of resources in producing or delivering the appropriate quantity or quality of goods or services in a timely manner
- 8 Is complying with requirements of laws and regulations that could significantly affect the acquisition, protection, and use of the entity's resources
- 9 Has an adequate system for measuring and reporting performance on economy and efficiency

### Program Audits

Determine whether the entity

- 1 Assess whether the objectives of a proposed, new, or ongoing program are proper, suitable, or relevant
- 2 Determine the extent to which a program achieves a desired level of program results
- 3 Assess the effectiveness of the program and/or individual program components
- 4 Identify factors inhibiting satisfactory performance
- 5 Determine whether management has considered alternatives for carrying out the program that might yield desired results more effectively or at a lower cost
- 6 Determine whether the program complements, duplicates, overlaps or conflicts with other related programs
- 7 Identify ways to make the program work better
- 8 Assess compliance with laws and regulations
- 9 Assess the adequacy of management's system for measuring and reporting effectiveness



1. Economy and efficiency audits include determining (a) whether the entity is acquiring, protecting, and using its resources (such as personnel, property, and space) economically and efficiently, (b) the causes of inefficiencies or uneconomical practices, and (c) whether the entity has complied with laws and regulations concerning matters of economy and efficiency.
2. Program audits include determining (1) the extent to which the desired results or benefits established by the legislature or other authorizing body are being achieved, (2) the effectiveness of organizations, programs, activities, or functions, and (3) whether the entity has complied with laws and regulations applicable to the program.

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## Goals of the audit

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Knowing that auditors may examine most any aspect of operations, finances, or management within your organization can help you understand the power of the audit. However, this knowledge does not provide you with a clear picture of the types of information for which the auditors will be searching.

■ *In most instances, the audit is being conducted because the auditors (or Congress, or EPA senior officials) either suspect that some weaknesses may exist within your organization or they are simply auditing selected areas to ensure that there are no weaknesses or problems.*

Weaknesses could, for instance, stem from inconsistent policy guidance, inadequate internal control systems, or, in rare situations, inefficient or fraudulent behavior by Agency employees, grant recipients, or contractors. The audit is intended as a tool to help you, the EPA manager, understand where such weaknesses may exist and help you resolve them.

Depending upon the elements covered in the audit (financial and compliance, economy and efficiency, or program results), several different objectives may exist. Some of these general objectives are listed in the Yellow Book.

If you know the scope of the audit that you will be facing, you should be able to identify the general objectives of the audit. With an understanding of these objectives, you can begin to assess your organization and try to identify where weaknesses may exist. If you can identify weaknesses, you should begin to formulate plans to address those weaknesses and, where possible, begin to take corrective actions, as soon as feasible.



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## Standards for audit

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The Yellow Book lists a number of standards for audit that must be followed by all Federal auditors and any auditors who perform audits of Federal organizations. Some of these standards cover internal audit management issues that should be of little concern for you since you will not be directly affected by them. However, other standards serve to guide the way auditors interact with you during the audit and to outline the format in which audit findings and recommendations are presented to you.

■ *You should be aware of key standards that are discussed here and understand the ways in which the audit in which you are involved meets these standards. The purpose of this is to ensure that the audit will be beneficial to you and your organization.*

The audit will be most beneficial if it is conducted according to the audit standards: the audit should describe the facts accurately, identify both strengths and weaknesses in your organization, present clearly the supporting evidence and arguments for findings and recommendations, and allow you an opportunity to review and comment on the audit report.

The following is a general list of audit standards that all auditors should follow:

■ *The organization should be examined to determine whether it complies with laws and regulations. Whenever a problem or issue is discussed during an audit or within an audit report, the auditors should cite the applicable laws and regulations—and any other criteria—they are using for their evaluation.*

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## Test of Compliance With Applicable Laws and Regulations

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### Legal and Regulatory Requirements

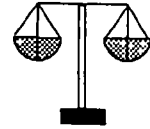
1. Identify the pertinent laws and regulations which could have a direct and material effect on the financial statements or the results of a financial related audit
2. Assess the risks that material noncompliance could occur
3. Design steps and procedures to test compliance with laws and regulations to provide reasonable assurance of detecting noncompliance

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The Yellow Book lists the potential sources of legal and regulatory requirements that auditors may use. These sources include laws, legislation, administrative orders, and contracts.

■ *In financial audits and performance audits, the auditors should provide "sufficient, competent, and relevant" evidence to support their judgments and conclusions.*

The Yellow Book provides definitions of what constitutes "sufficient, competent, and relevant" evidence. If your judgment of the evidence differs from the auditors' you should raise your concern with the auditors as early as possible in the audit process.



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## Standards for Reporting Audit Information

According to the Yellow Book, all reports should

- 1 Present factual data accurately and fairly
- 2 Present findings and conclusions in a convincing manner
- 3 Be objective
- 4 Be written in language as clear and simple as the subject matter permits
- 5 Be concise but, at the same time, clear enough to be understood by users
- 6 Present factual data completely to fully inform the users
- 7 Place primary emphasis on improvement rather than on criticism of the past

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■ *Written audit reports should be provided by the audit organization.*

With economy and efficiency audits and program results audits, audit reports are also to be issued in a timely manner. Specific items that should be included in economy and efficiency audits and program results audits are listed in the Yellow Book.

■ *The standards for reporting audit information are specific and clearly presented in the Yellow Book. When you receive an audit report, you should observe not only what is said but also how it is said.*

Definitions of reporting standards are provided by the Yellow Book and described in the paragraphs that follow.

■ *"Accuracy" is stressed as an important characteristic of the audit report. To be considered accurate, the audit report should include "objective evidence" to support any findings and conclusions presented by the auditors.*

■ *To be "convincing," findings should be supported by sufficient information and "conclusions and recommendations must follow logically from the facts presented."*

■ *The audit report should be "objective." As described in the Yellow Book, this means: "The audit report should be fair and not misleading and should place primary emphasis on matters needing attention."*

■ *The tone of the audit report should be of concern to both you and the auditors. The auditors should write the audit report in a tone that will lead the reader to respond positively to the conclusions and recommendations. If you have concerns about the tone and balance used by the auditors you should raise your concerns as early as possible in the audit process.*

## **Appendix D**



## Definitions of Terms

■ The definitions presented in this section were compiled from the following sources: *Government Auditing Standards* (the GAO Yellow Book); *EPA Order 2750*; OIG representatives; and the *OIG Manual*.

**Adequate response** — A response that addresses each finding or recommendation in an audit report and sets forth all appropriate corrective actions. An adequate response includes references to supporting documentation, legal basis, or precedent where a final decision differs from the auditors's findings and recommendations.

**Audit** — An assignment that is conducted in accordance with GAO standards, or parts thereof. In addition, for EPA Order 2750 purposes, an audit includes all special assignments or their resulting special reports.

**Audit finding** — A written explanation of an area audited, arriving at a conclusion(s) on the basis of the sum of available information gathered together. Fully developed findings include a discussion of Condition, Criteria, Cause, Effect, and Recommendation.

**Audit follow-up** — For OIG audits, the activity that occurs between the issuance of an audit report and the closing of the report in ATCS.

**Audit report** — A written report that states the scope of the audit and includes all pertinent findings.

**Audit resolution** — For OIG audits, the point when the OIG closes the audit report in ATCS.

**Audit Tracking and Control System (ATCS)** — The OIG's management information system, which is being replaced by the Prime Audit Tracking System (PATs).

**Auditing computer-based systems** — Generally, audit work covers reviewing the adequacy of management policies — examining approvals, documentation, test results, cost studies, and other data to see whether management policies are followed and legal requirements met — and determining whether the systems/applications have the necessary controls and audit trails.

**Compliance** — A determination of whether (1) there is compliance with laws and regulations that could materially affect the entity's financial position and statements, (2) there is compliance with laws and regulations that could significantly affect the acquisition, management, and utilization of the entity's resources, and (3) programs are being carried out in conformity with laws and regulations.

**Comprehensive grant audit** — An audit of an individual grant made in accordance with an individual Federal grant audit guide.

**Disallowed Cost** — A questioned cost that management, in a management decision, has sustained or agreed should not be charged to the Government.



**External audits** – External audits are independent reviews of the records and performance of individual assistance recipients and contractors. External audits generally follow the GAO financial and compliance standards, however, if the scope of work is sufficiently limited, a special report—not an audit report—may be issued. The following are examples of external audits:

*Pre-award audits* – A review and evaluation conducted to determine whether prospective cost or pricing data submitted were current, accurate, and complete. The review may include an assessment of the assistance recipient's or contractor's accounting, procurement, and property management systems

*Interim and final cost audits* – A review and evaluation conducted to assess, at a minimum, the allowability of costs claimed or reported under the assistance agreement or contract and to ensure compliance with applicable statutes, regulations, and terms and conditions of the award. These audits may include a review of incurred direct costs and the assistance recipient's or contractor's policies, procedures, and practices that influence and control grant contract costs.

*Indirect cost audits* – A review and evaluation conducted to determine whether an assistance recipient's or contractor's prospective or incurred indirect cost rate properly allocates costs allowable under Federal cost principles.

*Single audit* – An audit performed in accordance with the Single Audit Act (Public Law 98-502) and OMB Circular A-128.

**Final Action** – (a) The completion of all actions that management has concluded, in its management decision, are necessary with respect to the findings and recommendations included in an audit report, and (b) in the event that management concludes no action is necessary, final action occurs when a management decision has been made.

**Final determination** – The Action Official or Contracting Officer's statement to the auditee detailing the final decision on the audit findings and recommendations.

**Findings/results** – The result of information development; a logical pulling together of information and arriving at conclusions on the basis of the sum of the information about an organization, program, activity, function, condition, or other matter which was analyzed or evaluated and considered to be of interest, concern, or use to the entity. It need not be critical or concerned only with deficiencies or weaknesses. Purely informational findings need not include conclusions. A finding could be the basis for recommendations for action by the entity, but a recommendation is not part of a finding.

**Flash report** – Early notification by the OIG and EPA top management of significant problems found during the course of an internal or external audit so that top management has maximum opportunity to address the problems.

**Grantee** – A recipient of grant funds.

**Incomplete response** – "Incomplete" implies the absence of necessary information in the response or the response contains errors.



**Internal (Internal and Management — I&M) audit** — An independent review of Agency programs and operations conducted by the OIG generally in accordance with at least one of the three elements (financial and compliance, economy and efficiency, or program results) of the GAO standards. The audit is designed to determine whether: (a) desired results and objectives are being achieved effectively, (b) resources are managed and used economically and efficiently, (c) operating procedures are effective and being carried out, (d) applicable laws and regulations have been complied with, (e) financial operations are conducted properly, and (f) financial reports are presented fairly.

**Management decision** — The evaluation by management of the findings and recommendations included in an audit report and the issuance of a final decision by management concerning its response to such findings and recommendations, including actions concluded to be necessary.

**Materiality** — The concept which refers to the significance of an item of information which could appear, does appear, or does not appear in a financial statement.

**Minor (immaterial) audit finding** — An audit finding involving a relatively small amount of money or the benefits to management seem exceedingly small compared to the time and effort which would be needed to develop all elements of the finding in detail. Such a finding may or may not require OIG and/or action official follow-up.

**Pilot audit** — An initial internal audit conducted in a limited area usually following a survey. This audit would provide the basis for a decision to conduct similar audit work in additional areas.

**Position paper** — A statement of fact representing an OIG area of concern which is circulated prior to a draft report to allow reviewee input before publication of a draft report.

**Questioned costs** — A cost that is questioned by the OIG because of: (a) an alleged violation of a provision of a law, regulation, contract, grant, cooperative agreement or other agreement or document governing the expenditure of funds; (b) a finding that, at the time of the audit, the cost is not supported by adequate documentation; or (c) a finding that the expenditure of funds for the intended purpose is unnecessary or unreasonable.

**Recommendation that funds be put to better use** — A recommendation by the OIG that funds could be used more efficiently if management took actions to implement and complete the recommendations, including:

- a. reductions in outlays,
- b. deobligation of funds from programs or operations,
- c. withdrawal of interest subsidy costs on loans or loan guarantees,
- d. costs not incurred by implementing recommended improvements related to the operations of the establishment, a contractor or grantee,
- e. avoidance of unnecessary expenditures noted in preaward reviews of contract or grant agreements, or
- f. any other savings which are specifically identified.





**Reinstated costs** — Costs questioned or set aside by the auditor and sustained by the Action Official or Contracting Officer but were subsequently determined acceptable or waived after an assistance project review decision, contract appeal decision, or compromise of debt.

**Set aside costs** — A proposed or claimed amount which the auditor has not questioned but which the auditor cannot accept without additional information or evaluations and approvals by responsible Agency program officials.

**Special reports** — Any assignment, other than an audit conducted in accordance with audit standards, that seeks to promote economy and efficiency or prevent or detect fraud and abuse results in a special report. The following are examples of special reports:

***Allegation review*** — Review of allegations received through the hotline, correspondence, personal visits, etc., concerning an activity or auditable function.

***Desk review/agreed upon procedures review*** — A review performed by the OIG with limited analysis of a claim (in contrast to an audit).

***Early warning system review*** — The analysis of information for projects with potential problems at an early stage to limit the potential severity of the problem.

***Special review*** — A review that responds to the OIG need for a quick turn-around analyses of significant issues facing the Agency. Special reviews are meant to be quick studies rather than detailed audits. Reports are generally provided to senior executives and identify issues and obtain corrective action in less time and with fewer resources than an audit would take.

Special Reports are conducted under the authority of sections 4(a)(3), 6(a)(2), and 7(a) of the IG Act. For purposes of follow-up, desk reviews and early warning system reviews are handled as if they were assistance project-type external audits under EPA Order 2750. Allegation reviews and special reviews may either be handled as assistance project-type external audits or as internal audits under EPA Order 2750.

**Sustained costs** — Proposed or incurred costs that were questioned or set aside by the auditor and that the Action Official or contracting officer disallowed in the final determination. These sustained costs represent the governments "cost benefits" achieved either through costs avoided or payments to be recovered through collection or offset.

**Unsupported cost** — A cost that is questioned by the OIG because the OIG found that, at the time of the audit, the cost was not supported by adequate documentation.

## **Appendix E**

## Executive Summary

### REQUIREMENTS OF INSPECTOR GENERAL ACT AMENDMENTS OF 1988 P.L. 100-504, October 18, 1988

- o Amendments to the Inspector General Act were enacted last October.
- o The amendments affect all Federal agencies by mandating new semiannual reporting requirements for **agency management** as well as the IG.
- o Starting in October, 1989, we will be tracking management's response to audits and reporting the results to the Congress semiannually. The report covering the first six-month period will be made in May, 1990.
- o The reports must include
  - A table showing the dollar value of **disallowed costs**;
  - A table showing the value of **recommendations that funds be put to better use, agreed to in a management decision**; and
  - **Explanations of why any final actions are not complete a year after a management decision was made.**

*A detailed executive summary of the reporting requirements and new definitions of terms begins on the next page*

- o We are working to develop the simplest possible system for meeting the requirements of the amendments. We will work with ARAs and SBOs in developing the system, and will provide policies, guidance and training material for implementing it.

## Executive Summary

### ANALYSIS OF REPORTING REQUIREMENTS

#### Inspector General Act Amendments of 1988 P.L. 100-504, October 18, 1988

### MANAGEMENT'S SEMIANNUAL REPORTING REQUIREMENTS

#### ADDITIONAL REQUIREMENTS

1. Any comments (on the Inspector General's report) determined appropriate
2. A table showing number of audit reports, and dollar value of *disallowed costs*, for audit reports---
  - o Where **final action was not taken by the start** of the reporting period,
  - o Where **management decisions** were made **during** the reporting period,
  - o Where **final action** was taken **during** the reporting period, including---
    - Dollar value of disallowed costs **recovered** by management;
    - Dollar value of disallowed costs **written off** by management, and
  - o Where **no final action** has been taken by the **end** of the reporting period.
3. A table showing number of audit reports and dollar value of *recommendations that funds be put to better use, agreed to in a management decision*, for audit reports---
  - o Where **final action was not taken by the start** of the reporting period,
  - o Where **management decisions** were made **during** the reporting period;

#### PREVIOUS REQUIREMENTS

1. Any comments (on the Inspector General's report) deemed appropriate

o Where **final action** was taken during the reporting period, including---

- Dollar value of **recommendations** that were **completed**,
- Dollar value of recommendations that management subsequently concluded **should not or could not be implemented** or completed, and

o Where **no final action** has been taken by the end of the reporting period

4 Statement on audit reports where management decisions were made but **final action not taken**,

other than audit reports where a management decision was made within the preceding year,

containing---

- List of such reports and the **dates** issued,
- Dollar value of **disallowed costs** for each report,
- Dollar value of **recommendations that funds be put to better use agreed to by management** for each report, and
- **Explanation** of why **final action was not taken** with respect to each such report, except---
  - where formal administrative or judicial appeal is under way or where management has agreed to pursue a legislative solution,but shall identify the number in each category excluded

## THE IG'S SEMIANNUAL REPORTING REQUIREMENTS

### ADDITIONAL REQUIREMENTS

1 A listing, subdivided by subject matter, of *each audit report issued during the reporting period* and for each audit report, *where applicable*, the---

### PREVIOUS REQUIREMENTS

1 Description of significant **problems, abuses, and deficiencies** disclosed by the activities of the OIG during the reporting period

- o Total dollar value of **questioned costs**--- including a **separate** category for the dollar value of **unsupported costs** and
  - o Dollar value of recommendations that **funds be put to better use**
- 2 Summary of each particularly significant report
- 3 Tables showing number of audit reports and total dollar value of *questioned costs*--- including a *separate* category for the value of *unsupported costs*, for audit reports---
- o Where **no management decision** was made by the **start** of the reporting period,
  - o Which were issued **during** the period,
  - o Where a **management decision** was made during the period, including---
    - Dollar value of **disallowed costs**, and
    - Dollar value of **costs not disallowed**, and
  - o Where **no management decision** has been made by the **end** of the period
- 4 Tables showing number of audit reports and the dollar value of *recommendations that funds be put to better use*, for audit reports---
- o Where **no management decision** was made by the **start** of the reporting period,
  - o Which were issued **during** the period,
  - o Where a **management decision** was made during the period, including---
    - Dollar value of **recommendations agreed to by management**, and
    - Dollar value of **recommendations not agreed to by management**, and
- 2 Recommendations for **corrective action** made by the OIG during the period with respect to item identified pursuant to paragraph 1
- 3 Identification of each significant recommendation in previous semiannual reports **where corrective action has not been completed**
- 4 Summary of actions referred to **prosecutive authorities** and the prosecutions and convictions which have resulted
- 5 Summary of each report made to the agency head during the reporting period about **information or assistance** requested from the agency or any Federal, State or local governmental agency, that is unreasonably **refused or not provided**

- o Where no **management decision** has been made by the **end** of the period
- 5 Summary of each audit report issued *before the start* of the period where---
- no management decision* was made by the *end* of the period---
- o Including the---  
**date and title**  
of each such report,
  - o An **explanation** of the reasons that such **management decision** has **not** been made, and
  - o A **statement** about the desired **timetable** for getting a management decision on each such report
- 6 A description and explanation of the reasons for any *revised management decision* made during the period
- 7 Information on any significant *management decision* with which the Inspector General is in *disagreement*

## TERMS DEFINED IN THE IG ACT AMENDMENTS

### NEW DEFINITIONS

- 1 *Questioned cost* A cost questioned by the OIG because of---
- o An alleged **violation** of law, regulation, contract, grant, agreement or document governing the expenditure of funds,
  - o A finding that such cost is **not** supported by **adequate documentation**;
  - o A finding that the expenditure for the intended purpose is **unnecessary or unreasonable**.

- 2 *Unsupported cost* A cost questioned by the OIG because it is **not** supported by **adequate justification**
  
- 3 *Disallowed cost* A questioned cost that **management**, in a management decision, has sustained or **agreed** should **not be charged** to the Government
  
- 4 *Recommendation that funds be put to better use* A recommendation by the OIG that funds could be used more efficiently if management implemented and completed the recommendation by---
  - o Reductions in **outlays**,
  - o **Deobligation** of funds,
  - o **Withdrawal of interest subsidy** costs on loans, guarantees, insurance, or bonds,
  - o Costs not incurred by implementing recommendations related to the **operation**, of the agency, contractor or grantee,
  - o Avoidance of unnecessary expenditures noted in **preaward reviews** of contract or grant agreements, or
  - o Any other savings specifically identified
  
- 5 *Management decision* The evaluation by management of the findings and recommendations in an audit report and the **issuance of a final decision by management** on its response, including actions concluded to be necessary
  
- 6 *Final action*
  - o Completion of all actions that **management concluded**, in its management decision, are necessary, and
  - o In the event that **management concludes no action is necessary**, final action occurs when a management decision has been made