

**DOCUMENT RESUME**

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**Actions Needed to Strengthen the New Defense Internal Audit Service. FGMSD-77-11; B-160759. January 27, 1977. 3 pp. + appendix (4 pp.).**

**Report to Secretary, Department of Defense; by D. L. Scantlebury, Director, Financial and General Management Studies Div.**

**Issue Area: Internal auditing Systems: Sufficiency of Federal Auditors and Coverage (201).**

**Contact: Financial and General Management Studies Div.**

**Budget Function: Miscellaneous: Financial Management and Information Systems (1002); National Defense: Atomic Energy Defense Activities (013).**

**Organization Concerned: Department of Defense: Defense Audit Service.**

A survey was conducted of internal audit operations of the Office of the Secretary of Defense to determine whether internal audit operations were efficiently and effectively carried out and whether practices and procedures conformed to standards prescribed by the Comptroller General. During the survey, the Defense Audit Service was established to carry out functions and responsibilities previously carried out by three other offices. Findings/Conclusions: Before the reorganization, internal audit policies, plans, and operations generally complied with requirements for an effective internal audit system. Recommendations: The effectiveness of the new internal audit organization could be enhanced by: performing more reviews in significant areas of high level defense organizations; using a more systematic method for following up on audit recommendations to insure appropriate corrective action; and reviewing contemplated staffing levels of the Defense Audit Service to determine if they are adequate to meet required audit cycles. (RRS)

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*UNITED STATES  
GENERAL ACCOUNTING OFFICE*

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# Actions Needed To Strengthen The New Defense Internal Audit Service

## Department of Defense

The Defense Audit Service is a new Defense agency created by combining existing internal audit operations of two organizations and absorbing existing spaces from audit agencies in the military departments.

GAO believes that the Defense Audit Service could better serve departmental management by:

- Performing more reviews in significant areas of high level Defense organizations.
- Using a more systematic method for following up on audit recommendations.
- Reviewing contemplated staffing levels to bring required workload and capability of planned staff into balance.



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

DIVISION OF FINANCIAL AND  
GENERAL MANAGEMENT STUDIES

B-160759

The Honorable  
The Secretary of Defense

Dear Mr. Secretary:

We have completed a survey of the Office of the Secretary of Defense internal audit operations headed by the Deputy Assistant Secretary of Defense (Audit). Our objectives included determining whether internal audit operations were being efficiently and effectively carried out and whether the organization's practices and procedures conformed to standards prescribed by the Comptroller General.

The Deputy Assistant Secretary (Audit) is responsible for internal audit functions assigned to the Assistant Secretary of Defense (Comptroller). When our survey began, functional responsibilities were carried out by three offices-- Audit Operations, Audit Policy, and Audit Reports.

During our fieldwork, the Deputy Secretary directed that a new agency, the Defense Audit Service, be established. The Defense Audit Service will combine the Deputy Assistant Secretary's audit operations with the internal audit function of the Auditor General, Defense Supply Agency. Also, 125 personnel spaces are being transferred to the new service from the Army, Navy, and Air Force internal audit agencies.

Since planning for the implementation of the Deputy Secretary's directive was still underway when we completed our survey, we limited our analyses of the internal audit function to the existing internal audit system.

We have concluded that before the reorganization, internal audit policies, plans, and operations generally complied with requirements for an effective internal audit system, and we have no reason to believe that the new organization will be any less effective. However, we believe that the effectiveness of the new internal audit organization could be enhanced by:

- Performing more reviews in significant areas of high level Defense organizations, such as the Joint Chiefs of Staff and the Office of the Director, Defense Research and Engineering. We noted that some reviews of these and other higher level Defense offices had been made but limited to relatively minor functions.
- Using a more systematic method for following up on audit recommendations to help insure that appropriate corrective action is taken.
- Reviewing contemplated staffing levels of the new Defense Audit Service to get a better idea as to whether they are adequate to meet minimum required audit cycles established by the Department of Defense.

We believe it is important to see that audit staffs are of adequate size to perform required audits within established time frames. We therefore believe that whether an audit staff of the authorized size can do the required audit work effectively, needs further study. These matters are discussed in more detail in appendix I.

The Deputy Assistant Secretary (Audit) generally agreed with our observations. He said that actions are being taken to improve the first two areas as a part of the reorganization and that staffing levels will continue to get attention in accordance with established procedures.

We believe that the improvements contemplated can make the new Defense Audit Service more responsive to management's needs if properly implemented. However, we consider the matching of staffing levels of the new organization with the size of the workload to be critical to its success.

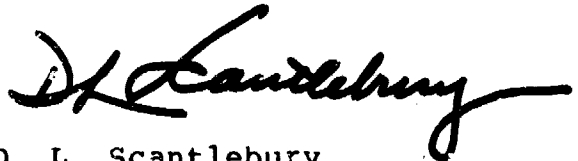
We, therefore, recommend that you assess the minimum required workload and the capability of the planned staff to perform that work and give appropriate consideration to bringing workload and staff capability into balance.

Section 236 of the Legislative Reorganization Act of 1970 requires the head of a Federal agency to submit a written statement on actions taken on our recommendations to the House and Senate Committees on Government Operations not later than 60 days after the date of the report and to the House and Senate Committees on Appropriations with the agency's first request for appropriations made more than 60 days after the date of the report. We would appreciate receiving copies of these statements.

We are sending copies of this report to the Chairmen of the House and Senate Committees on Government Operations, and the Chairman of the Subcommittee on Defense, Senate Committee on Appropriations. We are also sending copies to the Director, Office of Management and Budget; the Assistant Secretary of Defense (Comptroller); and the Deputy Assistant Secretary of Defense (Audit).

We appreciate the courtesies and cooperation extended to our representatives during our survey. We shall appreciate receiving your comments on any actions you take or plan to take on the matters discussed in this report.

Sincerely yours,

A handwritten signature in black ink, appearing to read "D. L. Scantlebury". The signature is written in a cursive style with a long, sweeping underline.

D. L. Scantlebury  
Director

ACTIONS NEEDED TO STRENGTHENTHE NEW DEFENSE INTERNAL AUDIT SERVICE

Section 133 of the Accounting and Auditing Act of 1950 made top management within each agency responsible for its internal auditing by providing that:

"\* \* \* the head of each executive agency shall establish and maintain systems of accounting and internal control designed to provide \* \* \* effective control over and accountability for all funds, property, and other assets for which the agency is responsible, including appropriate internal audit \* \* \*."

In the Department of Defense (DOD), the Deputy Assistant Secretary (Audit) is responsible for internal audit functions assigned to the Assistant Secretary (Comptroller) by the provisions of title 10, United States Code, section 136(b). This includes establishing policies and procedures for DOD's contract and internal audit activities; providing audit service to the Office of the Secretary, Office of the Joint Chiefs of Staff, and assigned Defense agencies; conducting audits of DOD-wide and other selected programs; serving as the DOD focal point for liaison with GAO, and processing GAO and other reports for top management attention and timely corrective action. These functions have been carried out by three offices--Audit Operations, Audit Policy, and Audit Reports.

While our survey of the DOD internal audit system was in process, the Deputy Secretary directed that the Defense internal audit function be reorganized. The organizational change established a new Defense internal audit agency that reports directly to the Secretary of Defense with staff supervision provided by the Assistant Secretary (Comptroller). Personnel and audit functions of the Auditor General, Defense Supply Agency and the Assistant for Audit Operations in the office of the Deputy Assistant Secretary (Audit) are being combined, reduced by 15 percent and transferred to the new agency. Also, 125 personnel spaces are being transferred to the new agency from the Army, Navy, and Air Force audit organizations to perform interservice audits.

Since reorganization had not been fully implemented during our survey, our work was limited to the organization existing at that time. However, we discussed our observations periodically with the Deputy Assistant Secretary to advise him of matters we believed could be useful in establishing the new organization. The principal matters brought to his attention are set forth below.

NEED FOR MORE REVIEW OF  
HIGH LEVEL DOD ORGANIZATIONS

To be of maximum usefulness, the scope of the internal auditor's activity should extend to all agency activities and related management controls. The internal auditor's duties should be clearly stated by the head of the agency and information concerning these duties should be disseminated throughout the organization to insure full recognition of the nature of his functions at all levels.

The Deputy Assistant Secretary (Audit) has generally provided regular internal audit coverage to the larger Defense agencies.

We noted, however, that only three reviews of the Office of the Joint Chiefs of Staff activities had been made during fiscal years 1974 through 1976 and these were of relatively minor functions. Two of the reviews were audits of the Chairman's dining room and the third was a review of the welfare and recreation association. There were no reviews of the Office of the Director, Defense Research and Engineering; Assistant Secretary of Defense for Manpower and Reserve Affairs; and other high level Defense offices.

The Deputy Assistant Secretary said that audit coverage of these offices has been limited in the past because of the size of the audit workload and shortfalls in staffing. He also said that although he had conducted audits of components of the Office of the Secretary of Defense, more could be done. He said that he plans to take advantage of the increased size of the new organization to make such reviews.

NEED TO IMPROVE  
REPORT FOLLOWUP SYSTEM

Our guidance on internal auditing in Federal agencies recognizes that primary responsibility for action and followup on audit recommendations rests with management. Provision should be made for regular inquiry into whether proposed corrective actions have, in fact, been taken and their effectiveness. Status reports on such actions should be prepared for management officials and internal auditors. Where operating officials disagree with the internal auditors' recommendations, a mechanism should be established to reconcile the differences or to call for a decision at a higher management level.

Department of Defense Instruction 7600.3, amended November 28, 1975, specifies that an independent office should be assigned responsibility for monitoring action taken on audit findings and recommendations, maintaining time schedules for responding to and acting on recommendations, keeping a record of the disposition of recommendations, and submitting periodic reports to top management on problem areas needing management attention.

The system for followup was inadequate at the time of our survey. Although the Deputy Assistant Secretary had provided for some followup and status reporting by the internal audit staff on recommendations where the dollar impact was \$100,000 or more, followup was not systematic, and there was no assurance that it would be accomplished even on significant matters. For example, in two fiscal year 1975 cases, there was no evidence that followup had been made, even though the auditors estimated potential savings of \$836 million. We also noted that certain DOD components were not always responding to final reports in a timely manner.

The Deputy Assistant Secretary (Audit) said that he plans to augment the staff of the Assistant for Audit Reports to monitor the disposition of all audit recommendations to comply with the amended DOD instruction. We believe that this new emphasis should help insure that the full benefits of audit recommendations are realized.

#### AUDIT STAFF MAY BE SHORT HANDED

The internal auditors responsibilities to management are broad. They can and should cover every facet of all agency activities and related management controls. To do this, the audit organization should be properly staffed with sufficient personnel to do the job.

Before the reorganization was announced in August 1976, the Deputy Assistant Secretary (Audit) had about 90 staff members in his office of audit operations. We noted that in forecasting their annual 1976 workload, before the reorganization, the Office of Audit Operations had recorded significant staffing shortfalls as compared with workload requirements as follows:



	<u>Fiscal years</u>	
	<u>1976</u>	<u>1975</u>
Total estimated annual workload in staff years	295	264
Less: direct staff years available	<u>64</u>	<u>68</u>
Estimated staff shortage	<u>231</u>	<u>196</u>

In our report to the Congress, "Suggested Improvements in Staffing and Organization of DOD Top Management Headquarters in the Department of Defense" (FPCD-76-35), dated April 20, 1976, we noted that the internal audit staff could cover only a part of their workload responsibilities. We also pointed out that without a detailed functional analysis, efforts to streamline headquarters can overburden, frustrate, and demoralize staff unless the workload decreases along with staff reductions.

Under the reorganization, the Defense Audit Service was given more responsibility. It included not only the work of the old office of audit operations and the staff of the Defense Supply Agency but also a broader responsibility for conducting DOD-wide reviews. Before the Defense Audit Service got underway, its staff was reduced by 15 percent. We believe this reduction was made without a careful determination of whether the staff was adequate to perform the assigned workload.

Because the reorganization was new, we did not have the information necessary to compare workload and staff size. However, since the old office of audit operations was so badly understaffed, it appears likely that the new organization might have the same problem.

#### RECOMMENDATION

We recommend that the Secretary of Defense assess the minimum required workload and the capability of the planned staff to perform that work and that appropriate consideration be given to bringing workload and staff capability into balance.