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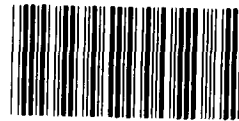
Comptroller General

OF THE UNITED STATES

The Office Of The Comptroller Of The Currency's Internal Auditing Needs Strengthening

The Office of the Comptroller of the Currency should strengthen its internal audit operations by:

- Renewing top management's commitment to internal audit.
- Improving audit program planning and implementation.
- Strengthening audit reporting and followup policies and procedures.



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COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON, D.C. 20548

B-168904

The Honorable John G. Heimann
Comptroller of the Currency

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Dear Mr. Heimann:

This report describes the status of your office's internal auditing activities and suggests ways to improve audit planning, implementation, and reporting.

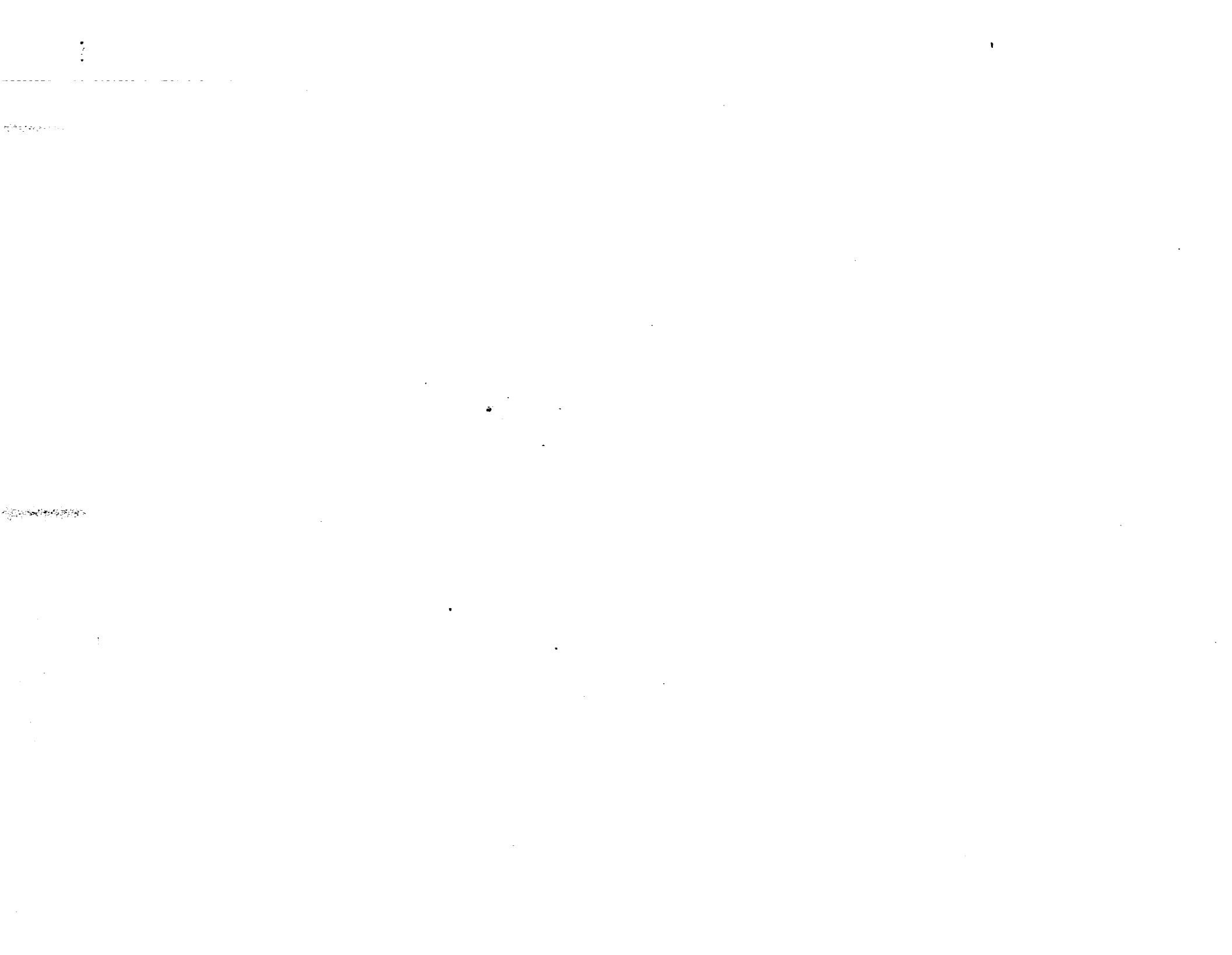
We recommend that internal audit be provided with additional staffing resources to effectively accomplish its organizational responsibilities.

This report contains additional recommendations to you on pages 13, 20, and 24. As you know, 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 Senate Committee on Governmental Affairs and the House Committee 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. ✓

Sincerely yours,

James B. Stets
Comptroller General
of the United States

*Arch 1
Internal
reports
audits*



D I G E S T

Top management should renew its commitment to maintaining a strong and effective internal audit group within the Office of the Comptroller of the Currency. Without consistent management support and direction, Internal Audit, whose function is to review the agency's financial and operational activities, has suffered from a lack of staff resources and limited coordination with other review efforts.

With a small staff and in the absence of clear, current, and written operating policies, informal operating practices have evolved. This, in turn, has resulted in an audit process needing more effective program planning, more consistent audit implementation, clearer reporting, and better followup on recommendations.

The Senior Deputy Comptroller for Operations has recently approved a plan to reorganize and strengthen the Agency's internal audit activities. The plan should be further strengthened by clarifying Internal Audit's role and relationship with other review groups.

MANAGEMENT SHOULD RENEW
ITS COMMITMENT TO
INTERNAL AUDIT

Top management needs to support its internal audit organization more consistently. Since 1970, staffing decisions have limited the organization's size to three professional auditors. As a result, Internal Audit's efforts have left many important areas of the agency's activities unaudited. (See p. 4.)

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In addition, Internal Audit's operating policies have not been regularly updated, thereby resulting in limited coordination with two other review efforts--the external financial auditor and an Operations Review Group, which is being reorganized into a Program Evaluation Division. Internal Audit has not taken advantage of opportunities to coordinate its efforts with the external financial auditors and, in some instances, has duplicated their work. (See p. 11.) In the case of the Operations Review group, Internal Audit had to share its independent operational review authority in a way that effectively limited the scope of its own reviews. (See p. 10.)

Management recently approved a plan to reorganize Internal Audit. The plan, which creates an Inspections and Audits Division, consists of an organization chart, position descriptions, and budget instructions for additional positions. The plan, however, does not include an update of the governing administrative circular for Internal Audit. (See p. 12.)

AUDIT PROGRAM PLANNING AND IMPLEMENTATION SHOULD BE IMPROVED

Audit planning and implementation policies should be improved to better meet the needs of a productive internal audit effort. Audit planning, although conforming with a formal agency planning process, omits some specific information important for informed management decisions and required by Office of Management and Budget guidance. (See p. 16.)

In addition, audit implementation policies and procedures are based on oral instructions rather than the firm guidance of a written audit manual. As a result, complete, written audit programs are seldom used to guide Internal Audit's efforts, workpapers sometimes do not support the scope of reports, and supervisory reviews are generally not documented. (See p. 18.)

AUDIT REPORTING AND
RECOMMENDATION FOLLOWUP
PROCESS SHOULD BE STRENGTHENED

Internal audit policies for reporting and recommendation followup are inconsistent because they too are based on oral instructions. Reports are sometimes untimely and contain unnecessary detail in lengthy appendixes which are often composed of raw documents. (See p. 21.)

Oral instructions and the lack of written documentation have also impaired Internal Audit's ability to follow up report recommendations, with the result that very little followup by Internal Audit has occurred. (See p. 22.)

RECOMMENDATIONS

GAO recommends the Comptroller of the Currency:

--As part of the effort to reorganize Internal Audit:

1. Provide Internal Audit with the additional staff resources necessary to effectively accomplish its organizational responsibility. (See p. 13.)
2. Improve the technical skills of the Internal Audit staff, particularly in the area of computer auditing. (See p. 13.)
3. Update the 1970 internal audit administrative circular to (1) clarify Internal Audit's operational relationships, particularly with the external auditor and other internal review groups, and (2) reemphasize Internal Audit's broad scope of audit responsibilities, particularly the responsibility to perform economy and efficiency reviews and program evaluations of all important operational areas. (See p. 13.)

- Provide additional information in Internal Audit's annual program plan to make it conform with Office of Management and Budget guidance. (See p. 20.)
- Instruct the head of Internal Audit to immediately develop a written audit manual which includes standards, policies, and procedures for the (1) development and use of written audit programs, (2) preparation of audit workpapers, and (3) establishment of consistent supervisory practices. (See p. 20.)
- Develop written reporting procedures which provide guidance on report form, processing and timing. (See p. 24.)
- Develop written recommendation followup procedures to assure that internal and external audit recommendations are receiving appropriate attention. (See p. 24.)

COMPTROLLER OF THE CURRENCY'S COMMENTS

The Comptroller of the Currency agrees with the recommendations presented in this report and has expressed his assurance that every effort will be made to achieve them.

A copy of the Comptroller's letter commenting on a draft of this report is contained in appendix I. Specific comments from the Comptroller's letter addressing the agency's use of the other internal review groups are summarized on pages 13 and 14, along with GAO's response.

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APPENDIX

- I Letter dated August 22, 1979, from
the Comptroller of the Currency,
commenting on this report

ABBREVIATIONS

ADP	automatic data processing
CPA	Certified Public Accountant
GAO	General Accounting Office
OCC	Office of the Comptroller of the Currency
OMB	Office of Management and Budget



CHAPTER 1

INTRODUCTION

This report evaluates the Office of the Comptroller of the Currency's (OCC) internal audit function. Internal auditing is an independent appraisal function established in an organization to examine and evaluate its activities as a service to the organization. The overall objective of internal auditing is to assist management in discharging its responsibilities by furnishing information, analyses, appraisals, and recommendations pertinent to the organization's execution of management policies and procedures. The internal audit function uniquely supplements routine management checks through its independent approach and review.

STANDARDS USED TO EVALUATE INTERNAL AUDIT ORGANIZATIONS

We assessed OCC's internal audit function against widely accepted internal audit standards which have been formulated for Government and private industry, including banking. In the Government sector, we have published policies and procedures for auditing government programs and functions. The Office of Management and Budget (OMB) embodied these policies and procedures in its directives to executive agencies. For private industry, several organizations, including the Institute of Internal Auditors, Inc., and the Bank Administration Institute, have issued sets of internal auditing standards.

While the organization of these sets of standards may differ slightly, they can be subdivided into three categories--general standards, examination or evaluation standards, and reporting standards. General standards applicable to an organization's internal audit activity include:

- Independence of auditors from activity audited.
- Professional proficiency of audit staff.
- Full review scope (financial operations, economy and efficiency and program results).
- Due professional care.

Examination and evaluation standards include:

- Sound audit planning.
- Proper supervision of assistants.
- Adequate supporting evidence.
- Reviews of compliance with applicable laws and regulations.
- Evaluation of internal controls.

Reporting standards include:

- Timely reports to appropriate officials.
- Clarity and accuracy of language.
- Adequate support of findings.
- Recommendations for improvement and consideration of issues requiring further study.
- Constructive tone, including mention of positive findings.
- Report of auditee's views.
- Description of scope, including mention of information omitted for purposes of confidentiality.

STATUS OF OCC INTERNAL AUDIT

Although internal auditing has been an ongoing OCC activity since 1927, it was not until the late 1960s that the program acquired professional staff. By June 1970, an Internal Audit Division consisting of three professional auditors, reporting to the Administrative Assistant to the Comptroller, was in operation.

In February 1976, the internal audit function, which had been reduced to two professionals, was reorganized under the Deputy Comptroller for Operations Review. In 1978, the internal audit function was again reorganized under the Director of Internal Affairs, who reported directly to the Comptroller of the Currency. In May 1979, the Office of Internal Affairs was reorganized into the Inspections and Audits Division. At present, the internal audit unit consists of three auditors with a fiscal year 1979 budget of \$87,700.

SCOPE OF REVIEW

Our findings and conclusions are based primarily on work done at OCC headquarters in Washington, D.C. We also visited OCC's Boston and New York regional offices and met with officials of the Treasury Department audit staff. Our review covered OCC internal audit activities through March 1979 and examined eight areas: scope of activities, organizational placement, program planning, staffing, training programs, report quality, report recommendation followup, and coordination with external auditors.

CHAPTER 2

MANAGEMENT SHOULD RENEW ITS COMMITMENT TO INTERNAL AUDIT

OCC's top management should support its internal audit organization more consistently. While OCC established a professional internal audit group in 1970, with broad independent review responsibilities, subsequent management staffing decisions have limited the size of this group to three professional auditors, thereby reducing significantly Internal Audit's capabilities. As a result, Internal Audit's limited efforts have left many important areas of OCC activity unaudited.

In addition, Internal Audit's efforts have not been effectively coordinated with either the activities of OCC's external financial auditor or the activities of OCC's former Operations Review group. Instances of duplication of effort have resulted and informal limitations have been placed on Internal Audit's work.

After we completed our review, OCC management approved a plan to reorganize and redirect its internal audit activities. We believe the plan should also include an update of the administrative circular governing Internal Audit's activities to emphasize the broad scope of internal audit activities and clarify Internal Audit's operational relationships.

MANAGEMENT SHOULD PROVIDE INTERNAL AUDIT WITH BETTER STAFFING

Although recognizing the need for an internal audit function, OCC top management has not provided Internal Audit with adequate staffing to effectively perform its audit responsibilities. Because of inadequate staff, Internal Audit's efforts have been limited to narrow areas, leaving many important agency activities unaudited. In addition, Internal Audit's current staff lacks the technical skills necessary to effectively review OCC's computer-related operations.

Inadequate staff level results in inadequate audit coverage

In 1970, recognizing the need to establish a formal role for Internal Audit, the Comptroller of the Currency

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issued Administrative Circular No. 52. According to this policy, Internal Audit assists management in achieving an effective, efficient, and economical administration of OCC's financial and operational activities by determining whether:

- Accounting data and reports are timely and useful.
- Resources are properly accounted for and adequately safeguarded.
- Applicable policies and rules are complied with.
- Policies, regulations, and underlying procedures achieve operational objectives.

The scope of Internal Audit's work included both financial and operational examinations. This circular also stated that maximum audit effectiveness requires the various levels of financial and operational activities to be subject to audit in a coordinated and systematic manner by a professionally competent and independent staff of auditors, qualified to render objective audit service to management.

To accomplish these responsibilities in an organization which in 1970 had 1,920 employees and expenses of \$31.7 million, OCC set up an internal audit unit consisting of three professional auditors. The new internal audit group followed an aggressive audit plan which included financial statement audits, reviews of administrative procedures (such as travel policies and payroll operations) and reviews of bank and trust examination activities. Reviews of regional office operations were also conducted.

A 1972 Treasury Department evaluation of Internal Audit noted that, while this group had made exceptional progress, maintaining the rate of progress would depend on "further increasing the audit staff, particularly at the junior level." Treasury's report also noted that this increase would "enable some expansion of audit services, relieve the senior auditors of lower-level work, and provide a hedge against personnel turnover." The report's specific recommendation of adding one junior auditor was rejected by OCC's Administrative Assistant who advised Treasury that, under the existing personnel ceiling, an additional auditor could not be obtained until a full complement of bank examiners had been acquired to meet statutory examination responsibilities.

From 1972 to 1977, Internal Audit's role, particularly in the area of operational reviews of bank examination policies and procedures, continued to receive only minimal staffing support. In 1975, the Chief of Internal Audit proposed that an operational audit capability, aimed at reviewing OCC's bank examination function, be developed. The proposal suggested that Internal Audit's staff be increased specifically to provide the capability to perform systematic operational reviews of OCC bank examination activities. Management rejected this proposal, deciding instead to set up a separate Operations Review group to perform independent operational reviews of bank examination activities. This new group was staffed by four bank examiners brought in from OCC field offices on a rotational basis. Meanwhile, Internal Audit's staff was allowed to drop to only two professional auditors. A 1976 limited Treasury review of Internal Audit again recommended that Internal Audit's staff be increased.

While OCC has experienced significant growth since 1970, Internal Audit's current staffing level remains at the 1970 level. From 1970 to 1978 OCC experienced a 60 percent increase in permanent positions (from 1,920 to 3,069) a 187 percent increase in annual expense levels (from \$31.7 million to \$91.1 million) and the addition of 10 new organizational units. Meanwhile, Internal Audit continues to consist of three professional auditors--one GS-13, one GS-12, and one GS-7.

This small staff size contributes to limiting the scope of Internal Audit's reviews to narrow areas of relatively minor importance. The 25 reviews conducted from 1976 through 1978 were concentrated in one of the 27 divisions in OCC (Finance and Administration). These efforts included reviews of graphic arts, plant and container purchase orders, mail messenger services, waste paper collection and disposal, and limited reviews of imprest funds and travel vouchers. In addition, no audit work outside OCC headquarters has been performed in the last 5 years.

Because of the small size of the internal audit staff, many important areas of OCC have remained unreviewed by Internal Audit. Although the former Operations Review group reviewed bank examination and consumer activities, Internal Audit has not directly audited these or the following activities in the last 3 years:

--Design and implementation of training programs.

- Implementation and direction of the OCC management planning process.
- Recruitment activities.
- Management of compensation programs.
- Payroll processing activities.
- Establishment and implementation of an employee data center.
- Management of data systems, programming and operations.
- International banking policy research.
- Management of financial information system.
- Special review activities (including review process of multi-national banks).
- Trust examination activities.

In addition, Internal Audit also did not review the methods or procedures used by the former Operations Review group.

According to the Senior Internal Auditor, the lack of adequate staff support has required him to devote much of his time to low-level staff work. As a result, other audit-related duties, such as program planning, audit report recommendation followup, and the development of an audit manual, have suffered.

Lack of adequate computer auditing skills limits audit effectiveness

Internal Audit currently lacks adequate staff with the technical skills necessary to effectively audit OCC's computer-related operations. A recent OCC study found internal control problems in OCC's data processing activities. As a result, an area in need of effective audit coverage is not receiving it.

An adequate staff of professional auditors is needed to support an effective internal audit effort. Audit standards relating to qualifications provide that auditors should collectively possess the necessary professional proficiency for the tasks required.

The standards further provide that the audit staff should be knowledgeable in

"Auditing theory and procedures, statistical techniques--including sampling--computer operations and applications, management information systems, economics, operations research, government organization and operations, and other facets of modern management practices."

A recent study questioned Internal Audit's ability to effectively audit computer operations. In late 1978, at the request of the Senior Deputy Comptroller for Operations, a field examiner from an OCC regional office reviewed OCC's data processing activities. He concluded that OCC management should devote its efforts and resources to "cleaning up" automatic data processing (ADP) operations and activities. This study was also extremely critical of the lack of an effective internal audit presence in the ADP area. Specifically, it characterized Internal Audit's coverage of ADP as "inadequate."

"The internal audit function of OCC has never performed a detailed audit of the data processing activity of this organization. Aside from a limited review of the Systems and Data Processing Division's procurement activity and related incurred cost, (evaluated in audit report 76-8), internal audit has had no presence in the ADP function. This significant weakness can be attributed to inadequate staffing and lack of technical ADP training. If senior management of the OCC is committed to a strong internal audit function, staffing and technical training for the Internal Audit Division must be significantly increased."

While noting his experience with ADP, the senior internal auditor concurred with this assessment of his staff's capabilities. Our review of internal audit staff experience profiles confirmed the lack of ADP expertise.

MANAGEMENT NEEDS TO COORDINATE INTERNAL AUDIT EFFORTS WITH OTHER REVIEW ACTIVITIES

While OCC top management has provided Internal Audit with a broad policy mandate, operational policies and procedures necessary to effectively implement and coordinate this overall policy have not been clearly defined and updated. As a result, Internal Audit's efforts have not been effectively coordinated with other OCC management review efforts,

thereby causing instances of duplication of effort and informal limitations to be placed on Internal Audit's activities.

Internal audit operating policies
are unclear and outdated

OCC top management has not provided Internal Audit with a clear, current set of written operational policies. Although the Comptroller recognized in 1970 the need for operational policies for Internal Audit, these policies have not been updated, thereby allowing informal understandings to guide Internal Audit's adjustments to subsequent organizational changes.

In 1970, recognizing the need for a broad internal audit policy document, the Comptroller of the Currency issued Administrative Circular No. 52. This circular defined Internal Audit's broad objectives and scope of work and addressed operational relationships and responsibilities regarding audit planning, implementation, and reporting. This document remains the only policy and operational directive given to Internal Audit by the Comptroller.

Since 1970, however, OCC has undergone significant organizational and operational changes, some of which directly altered Internal Audit's organizational status and role. For example, in 1975, an Operations Review group was established which effectively limited Internal Audit's ability to independently audit bank examination activities. A Treasury Department appraisal of OCC's internal audit activity conducted in July 1976, criticized the 1970 guidance for failing to recognize both the organizational changes which had taken place and the introduction of new Government-wide auditing guidance. An OCC management official told the Treasury auditors that the 1970 guidance would be updated. This has not occurred. Instead, Internal Audit's adjustments to organizational changes continue to be shaped through informal understandings.

Uncertain roles of Internal Audit and other
internal review groups limit their effectiveness

Internal Audit's organizational role directly overlapped OCC's Operations Review group, since both claimed the responsibility to perform independent operational reviews. In the absence of a formal clarification of their individual roles, each group generally limited its efforts, thereby limiting their overall effectiveness. Recently, the Operations Review group was reorganized into

a Program Evaluation Division reporting to the Senior Deputy Comptroller for Operations.

Established in 1975 as a result of a 1974 to 1975 study, the Operations Review group originally had a broad mandate to perform independent operational reviews under the Deputy Comptroller for Operations Review. In March 1978, however, this group, along with Internal Audit, was reassigned under the Director of Internal Affairs, although the two groups continued to operate separately. Staffed by four examiners, with a 1979 budget of \$120,700, this unit claimed responsibility for:

- Reviewing, evaluating and monitoring the quality of OCC's bank supervision and regulation functions.
- Serving as ombudsman to national banks and bankers.
- Initiating or recommending studies, to ascertain the need for revising OCC policy, practice, or procedure.
- Making recommendations on individual situations.
- Responding to proposed statutory amendments.
- Administering and/or performing operational performance reviews of OCC activities.

Since Internal Audit also shares some of these responsibilities, and since the 1970 policy statement did not anticipate this dual authority, the relative role of the two groups was uncertain. Because of this, the head of the Operations Review group formally requested role clarification on several occasions. For its part, Internal Audit, while acknowledging a broad operational review authority, chose to limit its operational review efforts.

In August 1979, OCC reorganized the Operations Review group into a Program Evaluation unit reporting to the Senior Deputy Comptroller for Operations. According to OCC officials this new unit will be a quality control mechanism subject to internal audit review. A new administrative circular defining Internal Audit's role relative to all internal review groups is currently being drafted.

Internal Audit does not effectively coordinate with OCC's external financial auditor

In the absence of formal guidance, Internal Audit's relationship with OCC's external financial auditor has

In the absence of formal guidance, Internal Audit's relationship with OCC's external financial auditor has evolved informally. As a result, their respective efforts have not been effectively coordinated. Opportunities for increasing effectiveness have been missed and occasional unnecessary duplications of effort have occurred.

OCC currently uses an external independent auditor to annually examine the agency's financial statements. The scope of this review includes tests of accounting records and the application of generally accepted auditing standards. In addition, the external auditor reviews OCC's accounting procedures and system of internal accounting controls. The firm reports to OCC on any improvements the review might suggest. OCC officials view this audit as an important management and financial control.

Because the 1970 OCC policy guidance does not address Internal Audit's role in this annual review, Internal Audit's relationship with the external auditors has evolved informally. Thus, while some informal coordination does occur, other areas of potential coordination recommended by both government and private industry internal audit standards have been neglected. For example, Internal Audit has no definitive written policies and procedures regarding:

- Followup on external audit report recommendations.
- Access to either the external auditor's audit program or workpapers to identify the types of tests being performed and the coverage being given to various accounts.
- Participation in pre-audit planning, or supporting the external auditor in performing the annual financial examination, even though this participation may be a valuable source of training and a way of facilitating the audit effort.

This lack of formal coordination has also led to duplication of effort. Internal Audit's financial review work has emphasized the unilateral review of specific financial activities rather than a coordinated approach. Consequently, Internal Audit sometimes reviews activities also included in the external auditor's examination. For example, both the internal and external auditors conducted a similar 100 percent confirmation of the same investments-owned account as of the same date. If the external auditor's work is acceptable, then a direct duplication of the work by the internal auditor would not be an efficient use of resources.

MANAGEMENT'S REORGANIZATION PLAN
SHOULD BE STRENGTHENED

Although management's plan to reorganize Internal Audit recognizes the need to increase the staff size, the plan does not include an update of the governing administrative circular. This circular is necessary to define Internal Audit's review responsibilities and operating relationships with external auditors and other internal review groups.

The reorganization, approved on May 16, 1979, by the Senior Deputy Comptroller for Operations, established a new Inspections and Audits Division reporting directly to the Comptroller. The organization consists of two units: (1) Inspections and (2) Audits, with a projected staff of 16 professional and 5 clerical. The Inspections unit is primarily responsible for investigating allegations of misconduct by OCC employees and monitoring employees confidential financial statements filed in compliance with regulations; the Audit unit is responsible for auditing OCC activities. The Director (grade 16) and Assistant Director for Inspections (grade 15) will be selected under the Inspector General series (1899) criteria. The Assistant Director for Audits (grade 14) and supporting professional staff will be selected under the Accountant series (510) criteria.

The reorganization plan does not include an update of the 1970 administrative circular governing OCC internal audit activities. The circular has been used to define Internal Audit's scope of review, operational relationships, and audit liaison responsibilities. The early and careful definition of these areas is important in establishing the role and direction of the unit. As discussed in the prior section, Internal Audit's effectiveness was greatly diminished by a lack of strong support and guidance from top management. Without a clear operating charter, agreed among management, the problems besetting Internal Audit in the past may continue to frustrate it in the future. OCC officials indicated they are drafting an updated circular.

CONCLUSIONS

At OCC, Internal Audit's role in the agency needs to be more effectively supported by top management. Internal Audit's efforts have been limited by a lack of staff and have not been effectively coordinated with other OCC management review efforts. As a result, many important OCC activities remain unaudited, and poor coordination among review efforts has led to instances of duplication of effort and the acceptance of informal limits on Internal Audit's

review efforts has led to instances of duplication of effort and the acceptance of informal limits on Internal Audit's work. OCC officials have indicated they are committed to clarifying and strengthening the internal audit function. A reorganization plan has been approved by the Senior Deputy Comptroller for Operations. However, we believe the plan should be additionally strengthened.

RECOMMENDATIONS

We recommend, as a part of OCC's effort to restructure the internal audit function, that the Comptroller of the Currency:

- Provide Internal Audit with the additional staff resources necessary to effectively accomplish its organizational responsibilities.
- Improve the technical skills of Internal Audit, particularly in the area of computer auditing.
- Update OCC's 1970 internal audit administrative circular to:
 1. Clarify Internal Audit's operational relationships, particularly with the external auditor and other internal review groups, and
 2. Reemphasize Internal Audit's broad scope of audit responsibilities, particularly the responsibility to perform economy and efficiency reviews and program evaluations of all important operational areas.

OCC COMMENTS AND OUR EVALUATION

The Comptroller of the Currency agrees with the above recommendations. (See app. I.) In his letter, however, the Comptroller points out that certain operational activities, such as bank examinations and supervision, are under continual evaluation at both the policy and operational levels. He notes also that the Operations Review group and its successor, the Program Evaluation Division, have been charged with reviewing and evaluating such activities.

As part of our review of internal audit activities at OCC, we also considered the role and function of the Operations Review group. We noted certain limitations with the Group which we hope will not carry over to the new Program Evaluation Division. In particular, they included

- a limited staff size, considering the extent of

- unclear role definition and direction (for example, regarding the scope of bank examination review activities);
- weak independence (the Group's staff were bank examiners serving short tours with the Group and planning to return to bank examining);
- limited scope of work (only once did the Group perform evaluation activities outside of Washington, D.C.); and
- no active recommendation followup mechanism.

We believe the use of quality control mechanisms, such as the new Program Evaluation Division, represents a positive step toward achieving a sound system of management control. These mechanisms should not displace the role of Internal Audit, however. Internal Audit must have agency-wide responsibility to examine all activities, whether or not other quality control mechanisms are used.

CHAPTER 3

INTERNAL AUDIT PROGRAM PLANNING AND IMPLEMENTATION SHOULD BE IMPROVED

Internal audit planning at OCC should be strengthened to provide management the full range of information needed to make effective decisions on proposed audit programs. In addition, professional audit implementation policies and procedures--relating to using written audit programs, documenting supervisory reviews and preparing workpapers--should be formally established in a written audit manual. Currently, written audit programs are seldom used, supervisory reviews are only occasionally documented, and audit workpapers sometimes do not support the reported audit scope. This is not surprising since there are only three professional auditors. But, as the number of auditors increases, it becomes essential to have written policies and procedures.

INTERNAL AUDIT PROGRAM PLANS SHOULD CONTAIN ADDITIONAL INFORMATION

OCC's internal audit plans lack the full range of information required by Federal directives. As a result, OCC management decisions on audit program plans are currently based on only limited information.

OMB Circular No. A-73 and our audit standards state that each agency should develop an annual audit plan which identifies the programs, operations, and areas needing review. When implemented, this plan would ensure that each audit is worthwhile and that the combined scope of all audits will provide sufficient coverage for management.

OMB's guidance specifically calls for each agency's annual audit plan to reflect the

- audit universe (all programs and operations subject to audit);
- priorities and reasons for those priorities for all programs and operations selected for audit;
- frequency of audit, locations to be audited and reason for selection;
- scope of audit coverage, with supporting reasons;
and
- anticipated benefits to be obtained from each audit.

Audit program planning at OCC has deteriorated over the last several years. In 1972, Treasury was satisfied with Internal Audit's program planning efforts. Its report indicated that the Director of Internal Audit prepared an annual plan that met the approval of the Administrative Assistant to the Comptroller. Furthermore, Internal Audit regularly requested Regional Administrators and headquarters officials to suggest new audit areas for consideration. Internal Audit also had an informal 5-year audit plan which provided another input to the annual plan as well as long-range direction to the audit effort. In their second review, conducted in 1976, Treasury found that audit plans neither effectively determined audit priorities nor complied with Federal Management Circular 73-2, Internal Auditing Standards. This circular has since been reissued as OMB Circular No. A-73. OCC officials indicated that they were unaware of the 1976 Treasury report.

Currently, OCC employs a new agency-wide operational planning process. This process establishes agency policy objectives, goals, and targets. Each unit is responsible for developing its performance targets. Internal Audit, in contributing to OCC's planning process, prepares an annual plan, consisting of a list of planned reviews, estimated costs, staff-day requirements and approximate completion dates.

Although Internal Audit's annual plan complies with OCC's operational planning requirements, it lacks many important pieces of information. For example, specific information required by OMB, but not reflected in Internal Audit's plans, includes a

- definition of the audit universe,
- determination of audit priorities,
- description of the scope of audits to be performed,
and
- discussion of anticipated benefits to be derived
from each audit.

Consequently, OCC management is not supplied with important information when considering the agency's internal audit plan.

Future Internal Audit plans, according to OCC officials, will be structured to conform to both OCC requirements and OMB A-73 guidance. A summary portion will be submitted in accordance with the agency-wide operational planning process

and a more detailed portion will be submitted to the Comptroller for review and approval.

AUDIT IMPLEMENTATION POLICIES
AND PROCEDURES NEED STRENGTHENING

Internal Audit needs to strengthen the policies and procedures used to implement its audits by preparing a written audit manual. As a result of the current unwritten audit policies and procedures, written audit programs are seldom used, audit workpapers do not usually support the scope of audit work, and supervisory reviews are rarely documented.

Written audit programs are seldom used

Internal Audit does not regularly use written audit programs to control the implementation of audits. Written programs facilitate audit implementation by providing direction to the staff and a basis for performance evaluation.

According to professional standards, a written audit program should be prepared for each audit as a vehicle to

- effectively communicate audit objectives to all staff members,
- facilitate control of audit work during the review phase, and
- provide a permanent record of audit plans and performance.

Audit programs should state clearly:

- Objectives and scope of the audit.
- Background information.
- Definitions of unusual terms.
- Audit procedures.
- Report procedures.

Internal Audit's use of written audit programs has varied over the years. The Treasury Department's 1972 review of Internal Audit found that work programs, in the form of audit guides, had been developed for the major, recurring audits and that the programs were well-written and complete. Treasury's 1976 limited appraisal of Internal

Audit found, however, that the two-person staff was not observing all of the audit unit's policies. While some procedures could no longer be followed due to the small staff size, others, including the maintenance of audit programs, were still considered desirable and achievable. Internal Audit agreed to concentrate on observing the policies which were achievable.

In 1978, written audit programs were still not being consistently used. Our review of 13 of the 16 1977 and 1978 audit efforts (workpapers for the other three efforts were not available at the time of our review) found only one effort using a written audit program. In three other instances, partial programs had been used. The senior internal auditor indicated that he will begin to prepare written audit programs at the end of each assignment. Unless the audit is recurring, however, preparing a written program at the end does not allow for its use as a planning and control tool during the assignment.

Audit workpapers sometimes do not support the scope of audit work

Currently, Internal Audit does not use written guidelines to ensure consistent workpaper preparation. According to the Senior Internal Auditor, oral instructions are normally used because of the small staff size. Such instructions have resulted in instances of incomplete workpapers. Internal audit standards require consistent and complete workpapers in order to facilitate supervisory reviews and establish documentary support for audit reports.

Our review of 13 sets of 1977 and 1978 Internal Audit workpapers identified three instances where we could not find adequate support to substantiate the reported scope of audit. While workpaper support for nine reviews appeared adequate, all of these reviews were narrow in scope. In four instances, the scopes were so narrow that the supporting workpapers were five pages or less. In the three instances where the support appeared incomplete, the audits were relatively broad in scope, including reviews of the internal control system. At the end of our review, the Senior Internal Auditor supplied us with the workpapers for a broadly scoped audit which had just been completed. These workpapers did appear to support the reported audit scope.

Supervisory reviews are rarely documented

Internal audit supervision at OCC is based on informal instruction rather than on procedures specified in a written

manual. This has led to inconsistent supervisory review practices.

According to professional internal auditing standards, Internal Audit should have a written manual which includes standards for

- monitoring auditors' activities,
- reviewing audit workpapers, and
- evaluating auditors' performance.

Specific procedures governing supervisory actions are also necessary to ensure fair and equitable treatment of staff members.

The Treasury Department noted in its 1972 review that Internal Audit had a well-written audit manual. However, in its 1976 review, Treasury discovered that Internal Audit was not following the standards included in the manual. Although Treasury agreed that some of the manual's standards were unreasonable for the two-man staff, Treasury recommended that the staff adhere to all feasible requirements.

Currently, Internal Audit has no internal audit manual. Supervisory procedures are informal and carried out on an as-needed basis. The informal nature of these procedures has led to inconsistencies in monitoring auditors' activities, reviewing workpapers, and evaluating auditor performance. For example, many workpapers contained no evidence of supervisory review. In addition, work progress reports were present in only a few sets of workpapers. While these practices may be acceptable for a small staff, considering Internal Audit's anticipated growth, formal supervisory procedures should be established.

The Senior Internal Auditor indicated that, as time permits, he will compile an internal audit manual which addresses supervisory procedures.

CONCLUSIONS

Audit planning at OCC, while part of a formal planning process, needs to be improved to provide management the full range of information required by OMB guidance.

Written audit implementation procedures need to be developed and incorporated into an audit manual. As a result of the current, unwritten audit policies and procedures,

audit programs are not consistently used, workpapers too often do not support reported audit scopes, and supervisory review procedures are rarely documented.

RECOMMENDATIONS

We recommend the Comptroller of the Currency instruct the head of Internal Audit to:

- Provide additional information in the annual program plan to bring it into conformance with OMB guidance; and
- Develop a written audit manual which includes policies, procedures and standards for the
 1. development and use of written programs,
 2. preparation of audit workpapers, and
 3. establishment of consistent supervisory practices.

These policies should be consistent with OMB's and our guidance.

OCC COMMENTS

The Comptroller of the Currency agrees with the above recommendations. (See app. I.)

CHAPTER 4

INTERNAL AUDIT REPORTING AND RECOMMENDATION FOLLOWUP

PROCESS SHOULD BE STRENGTHENED

While professional auditing standards stress the need for written policies and procedures, OCC audit report processing and report followup guidance consist entirely of verbal instructions. Internal Audit has relied on verbal instructions because of its small staff size. Nevertheless, these unwritten instructions have resulted in untimely reporting and cumbersome report formats. In addition, Internal Audit's followup on report recommendation has been infrequent, and, as a result, the impact of many recommendations is unknown.

INTERNAL AUDIT'S REPORTING PROCEDURES SHOULD PRODUCE MORE CONSISTENT RESULTS

In several instances, OCC's unwritten reporting procedures have produced untimely reporting and cumbersome report formats. Many OCC managers who receive these reports consider them too dated to be useful. In addition, many reports contain lengthy appendixes consisting of copies of original documents which users often find unnecessary.

Internal audit reporting standards require that audit reports be timely to the user and contain only pertinent information presented in a clear and concise format. Untimely reporting precludes management from effectively utilizing audit results. Reporting in too much detail tends to confuse or discourage report users.

Internal Audit's approach to the reporting process has varied over the years. The 1972 Treasury review of Internal Audit found reporting standards specified in an audit manual. Treasury noted that audit reports were generally well-organized, concise, and appropriate. Later, in a limited 1976 review, Treasury again found Internal Audit's reports to be well organized and concise.

In 1978, however, internal audit reporting was guided by unwritten, verbal instructions. According to the Senior Internal Auditor, no written policies for audit reporting had been developed because of the small staff size. As a result, unnecessary and sometimes confusing detail has begun to encumber Internal Audit's reports.

On several occasions, Internal Audit failed to report to management on a timely basis. Of the eight major audit

report users we surveyed, four considered Internal Audit's reports as generally too untimely for their needs. For example, an OCC official noted that an audit, which directly duplicated a test performed by a CPA firm on OCC records as of December 31, was not completed by Internal Audit until the following October--6 months after the CPA firm had reported the same information. In another instance, the results of a limited audit of December 31 records were also not reported until the following October. According to the Senior Internal Auditor, audit reports are untimely because the level of staffing resources is too low and audits are frequently interrupted by higher priority special requests.

Internal audit reports, while generally clear, contained excessive detail in several instances. Six of the eight audit report users we surveyed indicated the reports were generally easy to understand. However, these users individually criticized the audit reports for either including unneeded information or directly duplicating information from other sources.

Most of the unneeded information in these reports occurs in appendixes. Internal Audit has followed an unwritten policy of attempting to make "each report stand on its own." To achieve this, extensive documentary support is often included as appendixes to the reports, which often dominates them. For example, one report consisting of 4 pages had 62 pages of appendixes.

Copies of original documents appended to reports we reviewed included:

- 28 pages of individual travel vouchers.
- 27 pages of specific vendor invoices.
- 40 pages of individual bank applications.

The need to include such appendixes in formal audit reports is questionable. In addition, attempts to photocopy original documents have led to instances where entire sections of appendixes are unreadable.

REPORT RECOMMENDATION
FOLLOWUP SHOULD BE IMPROVED

While internal audit standards advocate establishing formal procedures to ensure consistent followup of audit report recommendations, OCC's followup practices consist entirely of oral instructions. The informal nature of these practices has led to infrequent report followup. As a

result, Internal Audit does not know whether management has implemented promised improvements.

Internal audit standards advocate that internal audit groups establish followup policies and procedures for their audit recommendations. These followup policies and procedures should include:

- A procedure for periodic review of recommendations to determine whether satisfactory corrective action has been taken.
- A mechanism to reconcile differences or call for a decision at a higher management level when the operating officials disagree with the internal auditor.
- A policy for following up GAO and other external auditor findings to determine whether agency officials have taken effective corrective action.

At OCC, the followup of audit report recommendations is guided by verbal instructions. This has contributed to inconsistent following up of report recommendations. In fact, since 1976, Internal Audit conducted only two documented followups of report recommendations. Furthermore, they had not conducted any direct followups of Operations Review report recommendations or reviewed their follow-up procedures. Instead, in most instances, recommendation followup is left to management. The following cases illustrate the lack of followup effort:

- The annual CPA audit results in an internal control memorandum with recommendations to management. Many of the recommendations in the last 3 years have been identical. However, Internal Audit followed up on these recommendations only once (1976). Closer monitoring of the external auditors' recommendations by Internal Audit may have reduced the need for such repetition.
- In conducting an unrelated review, Internal Audit found an instance where management had concurred with a recommendation but later failed to implement it.

Internal Audit generally does not know whether management has implemented promised actions. The 15 internal audit reports in 1977 and 1978 contained 33 recommendations. Management generally concurred either totally or partially with most of them. However, due to inconsistent

followup practices and a lack of written documentation, Internal Audit has been unable to determine which recommendations were actually implemented.

CONCLUSIONS

Reporting and followup activities are important elements in achieving an effective internal auditing function. At OCC, reporting and followup guidance consists of oral instructions. The result has been cumbersome and untimely reports and inconsistent followup on report recommendations.

RECOMMENDATIONS

We recommend the Comptroller of the Currency instruct the head of Internal Audit to

- Develop written reporting procedures which provide guidance on report form, processing, and timing.
- Develop written recommendation followup procedures to assure that internal and external audit recommendations are receiving appropriate attention.

OCC COMMENTS

The Comptroller of the Currency agrees with the above recommendations. (See app. I.)



Comptroller of the Currency
Administrator of National Banks

Washington, D. C. 20219

August 22, 1979

Mr. Allen R. Voss
Director
General Government Division
U. S. General Accounting Office
Washington, D. C. 20548

Dear Mr. Voss:


We have reviewed your draft of a proposed GAO Report "Internal Auditing Needs Strengthening in the Office of the Comptroller of the Currency." OCC staff members have had a number of conferences with GAO representatives and submitted comments and suggestions to GAO, and we understand that these suggested changes will be incorporated into the final report to Congress.

In the Report, GAO observes that OCC's Internal Audit Division did not directly audit important activities such as bank examination and supervision policies and procedures and trust examination activities. In our opinion, this statement is not comprehensive. These important OCC functions have been under continual evaluation at both a policy and an operational level. Additionally, an Operations Review Group was charged with reviewing and evaluating these functions. We intend that the new Program Evaluation Division will operate similarly with the results of their reviews available to the Internal Audit Division. Of course, the Program Evaluation function will be subject to Internal Audit reviews.

It should be noted that the Inspector General concept has been approved in this office more than one year ago but budgeting restraints precluded an earlier implementation. The reorganization plan creating the Division of Inspections and Audits is in keeping with that Inspector General concept.

As concerns the recommendations in the draft proposed GAO report, you have my assurance that every effort will be made to achieve them and you can be further assured of our continued cooperation.

Very truly yours,


John G. Neumann
Comptroller of the Currency



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