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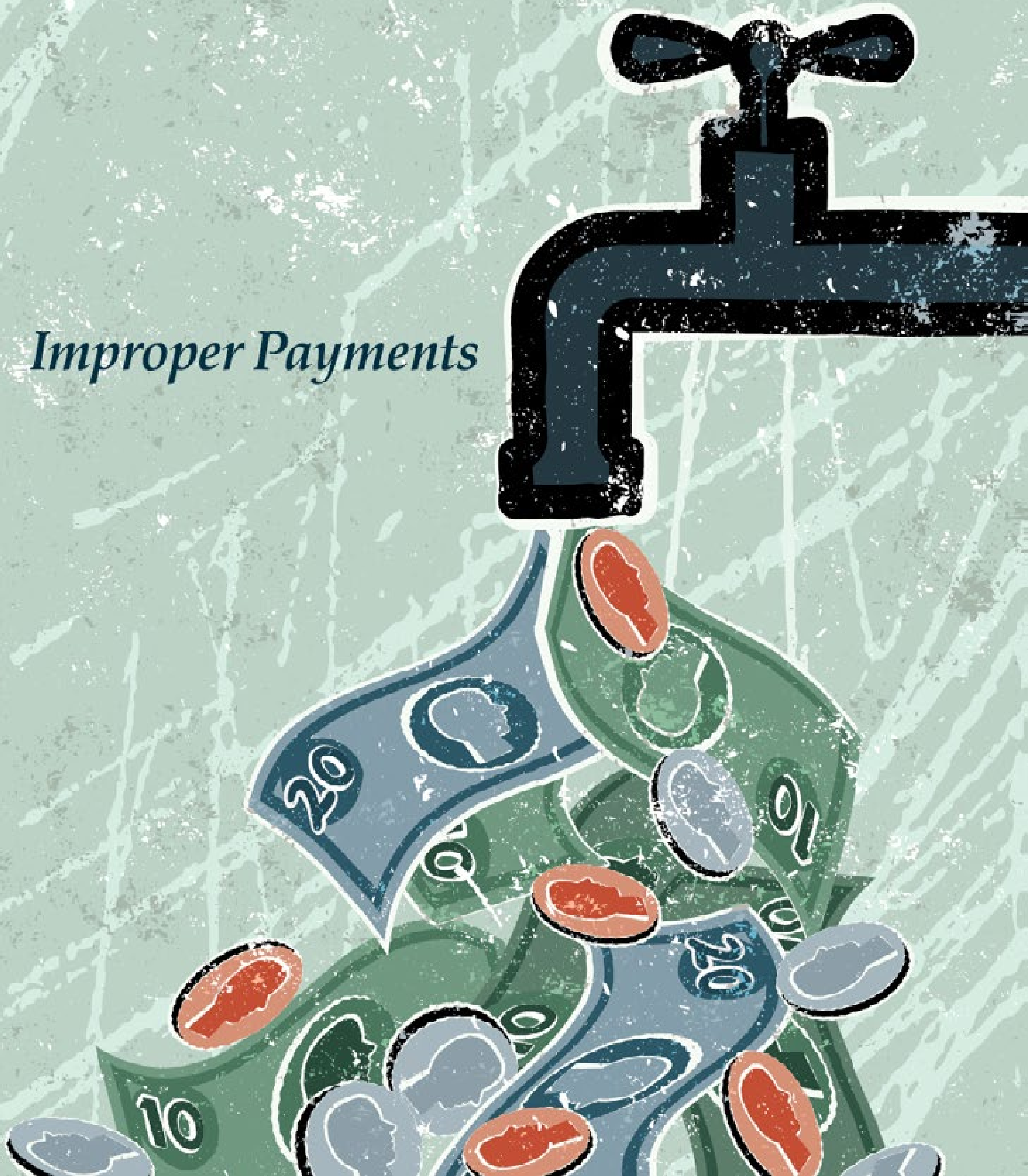
Improper Payments



We Are Here to Help

By: Geoffrey Frank, MPA, CGFM; and Rich Rasa, CGFM

Redefining External Auditors' Role

Traditionally, external auditors[1] review government programs, make recommendations for improving payment and other program controls or for recovering program costs, and pass-on their recommendations to management to design and implement appropriate corrective actions. Clearly, one responsibility of an external auditor is to issue objective reports that detail control deficiency findings and recommend corrective actions, including actions to improve controls to prevent or detect improper payments. In accordance with the U.S. Government Accountability Office (GAO) Yellow Book,[2] maintaining the external auditor's independence is essential to such objective reporting. Just as clear in the Yellow Book, is the principle that auditors are not to take any management responsibilities for implementing corrective actions. This traditional approach, built on a clear divide between auditor and management roles, is effective in maintaining essential external auditor independence. However, it may foster an adversarial relationship between the external auditor and management, and most importantly, may lead to lengthy delays or ineffective actions to correct program and payment control deficiencies.

Recently, an alternative model for the external auditor's role in government program performance has emerged, the *Cooperative Audit Resolution and Oversight Initiative* (CAROI) model. This alternative model is built on working within the audit standards framework to establish a shared auditor-management vision and commitment to effective program performance. The importance of establishing such a universally-shared vision was evident in the early days of our nation's program to put a man on the moon. This shared vision model is illustrated through an exchange that occurred during President Kennedy's 1962 tour of the National Aeronautics and Space Administration (NASA) space flight center. During the tour, President Kennedy noticed a man carrying a broom, walked over to the man and said, "Hi, I'm Jack Kennedy. What are you doing?" The man responded, "I'm helping put a man on the moon, Mr. President." In much the same way, government external auditors have an opportunity to collaborate with management on a shared vision of government operations and necessary improvements. Adopting such a collaborative model will better enable external auditors to claim, "We are here to help!"

Increasing Expectations for External Auditors

Expectations have increased dramatically over the years for the external auditors' role in improving government operations. After World War II, GAO began carrying out audits directed at examining the efficiency and effectiveness of federal government operations. In the 1960s, GAO began performance auditing and program evaluations directed at determining whether federal government programs were meeting their objectives. In 1976, Ellsworth Morse, the GAO Assistant Comptroller General at the time, expressed the view that, "Managers and policymakers, particularly in the government, want and need more from auditors… They want independently and objectively obtained and evaluated information on operations and performance and advice on such things as how improvements can be made."[3]

In 1978, Congress further buttressed external auditors' responsibilities in this area with the passage of the Inspector General Act, which established Inspectors General (IGs) in major federal departments and agencies. These newly created IGs were charged with conducting independent and objective audits and investigations of agency programs and operations.[4] In 1988, Congress amended the IG Act to, among other provisions, stress the importance of resolving federal auditor recommendations. With today's evolving, fiscally-constrained, and increasingly interdependent program operations environment, government managers are, more than ever, looking for help from their external auditors.[5]

Innovative Cooperative Approach Successfully Applied to Grant Programs

Since the mid-1990s, the U.S. Department of Education (Education) has successfully developed and applied an innovative cooperative approach to resolve deficiencies identified through audits of its intergovernmental grant-making programs. At the time, Education determined that the traditional approach to resolving auditors' findings resulted in:

- Adversarial relationships;
- Protracted legal battles over questioned costs charged to grants; and
- Repeat auditor findings resulting from ineffective corrective actions.

As a result, Education developed and began testing a new alternative collaboration-based approach to resolving audit findings. This approach became known as CAROI. The central concept of the approach was that by working together, federal and state audit, program, fiscal and legal officials could more readily develop and implement comprehensive solutions to audit-identified control deficiencies. In the late-1990s and early-2000s, Education tested the CAROI approach to address lingering audit deficiencies involving Education's grant programs to several states, including: Florida, Mississippi, Washington, and Pennsylvania. The Pennsylvania experience with CAROI in the late-1990s is illustrative of the testing results. In Pennsylvania, the test showed not only did CAROI resolve all 119 deficiencies (some of which dated back seven years), but it also enabled a more expeditious resolution of issues as they were discovered. Pennsylvania's Comptroller at the time stated that using the CAROI approach enabled Pennsylvania to take 'a giant step' forward in resolving lingering audit deficiencies and credited the process with establishing a solid foundation for effective future collaboration.

CAROI Approach Has Broad Applicability

In May 2010, AGA issued its "Guide to Improving Program Performance and Accountability Through Cooperative Audit Resolution and Oversight" (Guide). The AGA-sponsored, diverse intergovernmental workgroup developed the Guide as a tool intended to provide a structured, but flexible approach to audit resolution that would have broad applicability to all types and levels of government programs and operations.

Mindful of GAO's Yellow Book standards, the Guide explicitly recognized that external auditors must not compromise their audit independence by participating in any managerial decisions or taking on any other management function related to their recommendations. However, it also highlights ways in which external auditors can be a valuable resource to management in the audit resolution process, without impairing their independence. For example, the Guide provides that independent auditors can serve as a resource for management in better understanding the nature and extent of their audit findings, the causes of the identified deficiencies, and potential solutions.

Recent CAROI Experience

In December 2013, the Office of Management and Budget (OMB) issued policy guidance encouraging grant-making federal agencies to use cooperative audit resolution practices.[6] One of the stated intents of OMB's policy directive was to provide a clear message that continuing failure to correct auditor-identified conditions likely to cause improper grant payments was unacceptable. OMB's guidance also encouraged adopting audit resolution practices to include:

- A shared commitment to program integrity;
- Cooperation between federal and non-federal agencies and their audit partners;
- A forward-looking focus on needed corrective actions; and
- Prompt actions to correct audit deficiencies.

Further, initial reports from recent pilot efforts to apply the CAROI approach to non-grant-making federal agencies have been encouraging. Specifically, pilot efforts are underway to apply the CAROI model at the Equal Employment Opportunity Commission (EEOC), and in addressing backlogs of unresolved audit findings involving tribal government programs crossing jurisdictions of multiple agencies. The EEOC is the first federal agency whose primary mission operations did not rely heavily on grant-making to test implementing the CAROI approach to resolve lingering auditors' findings. Initial reporting from EEOC's IG indicates that adopting the CAROI approach better enabled their office to provide assistance and practical advice without compromising independence. Similarly, initial reports from tribal government CAROI pilots indicate the approach has enabled, for the first time, a constructive dialogue among the multiple auditors, tribal governments and federal agencies involved, on underlying issues that prevented resolution of long-standing external auditor findings.

Encouragingly, AGA's September 2013 Federal IG Survey indicated that federal program management leadership is now more supportive of establishing such cooperative working relationships with IGs. The most recent survey of federal IGs shows that from their perspective, efforts to establish supportive auditor and management relationships have been successful[7]. Specifically, all IGs interviewed rated the level of support for their audit work from agency management ('Tone at the Top') as either 'very good' or 'excellent.' Several federal IGs cited their experience, working with agency management, to identify fraud, waste and abuse risks associated with implementation of the American Recovery and Reinvestment Act of 2009 (ARRA), as an example of a collaborative working relationship between agency management and external auditors.

Where Do We Go From Here?

While initial pilots — and top level support for applying the CAROI approach more broadly to resolving audit findings for all types and levels of government programs — are encouraging, questions and challenges remain to be addressed. By design, the CAROI model is flexible and can be tailored to address a variety of broad agency or specific program needs. However, as the old saying goes, "the devil is in the details." As external auditors and their agency management counterparts develop their detailed plans for considering and appropriately applying the CAROI approach, the following questions should be considered in explicitly defining external auditors' roles and responsibilities to most effectively ensure they meet their dual 'assistance vs. independence' challenge:

- Is that really the problem?
- Is there a quick fix?
- Is there a better way?
- How much is enough?

Is that Really the Problem?

Can external auditors be more proactive in assisting management by more explicitly articulating the "cause" of the control deficiency they identified in their audit work? CAROI points out the importance of auditors developing sufficiently detailed, measurable and actionable audit recommendations. How often do external auditors' reports contain recommendations that essentially say to management, "Here's the deficiency we found, you figure out how to best fix it, and then take whatever action you judge appropriate?" In some cases, these open-ended recommendations are entirely appropriate. For example, AGA's Federal IG Survey noted that federal IGs recently introduced a new audit report product line designed to provide management with an early warning of risks or vulnerabilities. By design, these products focus on timely reporting. Recommendations, if any, from these types of reports are generally not prescriptive. It falls to management to identify the extent and nature of the cause of the identified risks or vulnerabilities and appropriate related corrective actions.

However, in other instances, external auditors have an opportunity to provide greater assistance to management by focusing their audit planning and reporting not only on identifying a control deficiency, but also on identifying the underlying cause(s) of a deficiency. Through the process of planning and carrying out cross-cutting agency or program

audits, external auditors may acquire a unique, entity-wide understanding of controls and an entity or program's overall control environment that surpasses management's understanding.

Is There a Quick Fix?

> "Unless commitment is made, there are only promises and hopes... plans are only good intentions unless they immediately degenerate into hard work."
>
> — Peter Drucker, 'Father' of Modern Management

Management's agreement to correct a control deficiency may not be the appropriate point to end the external auditor's collaboration with management. For example, an audit-identified deficiency that resulted in an improper payment may have a cause deeply embedded in control flaws involving multiple systems, organizations, or organizational levels. Even with management agreement to address such deficiencies, they may take years to fully correct. Consequently, it is essential that external auditors consider the extent of their own commitment to sustaining a collaborative working relationship with management, which may require a multi-year commitment. Further, a high turnover rate in many agency leadership positions has sometimes left the auditors in a position as the preserver of the institutional details regarding the extent and nature of the deficiency to be addressed.

Is There a Better Way?

External auditors should assess their openness to alternative, more cost-effective approaches to correcting deficiencies identified. That is, the external auditor should consider whether an approach, different from their recommendation, may provide a more efficient or cost-effective means of corrective action. External auditors should be mindful that while their recommendation may provide a set of steps they believe will correct the identified deficiency, that approach may not be the only or necessarily the best approach. Furthermore, external auditors should consider whether circumstances have changed that would make their recommended corrective actions invalid. Or, while not explicitly the actions the auditor recommended, are there alternative approaches that provide different sets of actions that also address the underlying cause of the auditor's identified control deficiency? Would alternative actions not only also correct the underlying cause of the deficiency, but also provide for more cost-effective use of scarce resources?

How Much Is Enough?

The CAROI model recognizes that the external auditor can provide management advice on constructing an effective audit resolution process. In this regard, external auditors should consider whether they should play a role in assisting management with advice on designing corrective actions that provide 'reasonable' (rather than 'absolute') assurance that resulting controls effectively address identified deficiencies. In addition, external auditors should consider the extent to which they serve a role in advising management on the distinction between audit resolution (agreement and a plan of action to correct a deficiency) and recommendation closure (substantially correcting the cause of a deficiency leading to the recommendation).

External auditors may also consider whether they should play a role in providing an independent 'after-the-fact' assessment of the extent to which management has completed actions to close recommendations. In this regard, external auditors can add value by independently and objectively assessing the extent to which management's actions have substantially addressed the identified control deficiencies. For example, the external auditor may be able to assess whether sufficient training has been provided to the extent and nature of the recommended procedural control changes, tailored to reflect the unique roles and responsibilities of each level of agency or program operations. Such training can be critical in ensuring all personnel have a shared entity-wide understanding of the benefits and risks associated with endorsing and implementing auditors' recommended corrective actions as designed.

Conclusions

> "The secret of success is changing the way you think."
>
> — Jack Welch, former CEO, General Electric

In light of increasing expectations for external auditors to add value to government program operations, the traditional external auditor and management model with a clear divide may not be the most effective for developing comprehensive solutions to program and payment control deficiencies. As an alternative, the CAROI approach, built on fundamentally rethinking the external auditor and management relationship as a more collaborative model, has demonstrated encouraging results. At its heart, the CAROI model is designed to work within the parameters of audit standards to facilitate greater external auditor and management cooperation to develop more timely and effective solutions to long-standing audit findings.

Building on initial successes in Education's grant programs, OMB recently endorsed the CAROI model for consideration by all federal grant programs. The approach is also sufficiently flexible to be more broadly applicable to other types of government programs. Initial reports from pilot tests of the approach at non-grant making agencies show promise. However, important questions and challenges remain as to how best to redefine the external auditor's role within the audit independence standard framework to most effectively facilitate preventing or remediating improper payments, while also improving government program performance. Successfully addressing these remaining questions and challenges may well result in giving new meaning to the auditors' claim, "We are here to help."

Endnotes

1. External auditors refer to Inspector General (IG), Government Accountability Office (GAO), and independent public accounting firm auditors involved in conducting audits, as differentiated from nonaudit services.
2. GAO, Government Auditing Standards, GAO-12-331G (Washington, D.C.: December 2011).
3. GAO, Performance Auditing, GAO-094640 (Washington, D.C.: April 21, 1976), p.26.
4. 5 U.S.C. app. 3 § 2.
5. Id. § 5.
6. Federal Register, Vol. 78, No.248, December 26, 2013, Rules and Regulations.
7. AGA, Inspector General Survey: Effective Oversight in a Changing Environment, September 2013.

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