



INSPECTOR GENERAL

U.S. Department of Defense

JUNE 30, 2014



Implementation of 2011 Generally Accepted Government Auditing Standards Independence Standards at the DoD Audit Organizations



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Results in Brief

Implementation of 2011 Generally Accepted Government Auditing Standards Independence Standards at the DoD Audit Organizations

June 30, 2014

Objective

We conducted this review to determine whether the DoD audit organizations implemented the December 2011 generally accepted government auditing standards (GAGAS) independence standards and whether the standards were being followed. We reviewed 16 of the 21 DoD audit organizations (see Appendix A Scope and Methodology for our rationale).

Findings

Of the 16 DoD audit organizations reviewed, 10 had fully implemented, 4 had partially implemented, and 2 had not implemented the 2011 GAGAS independence standards.

In addition, four audit organizations performing nonaudit services did not fully assess and document potential impairments to independence as required by GAGAS 3.34. GAGAS 3.34 requires the auditor to assess the skill, knowledge, or experience of the audited entity management's designated individual who will oversee and accept responsibility for the nonaudit service.

Also, some auditors' statements of independence were either missing or improperly completed. In addition, one audit organization failed to comply with the standards when performing control self-assessments and continuous auditing.

Recommendations

We recommend that the specified DoD agencies or audit organizations:

- establish internal policies or procedures implementing the December 2011 GAGAS independence standards,
- create internal policies and procedures detailing how nonaudit service requests will be processed,
- perform all the required independence analyses and document the results before accepting a nonaudit service,
- include policies and procedures for performing control self-assessments and continuous auditing, and
- remove language from agency operational procedures that appears to direct the functions of an internal review office.

Management Comments and Our Response

Five of the seven respondents agreed with our recommendations. The Auditor General, Department of the Army agreed with the intent of our recommendation but only partially addressed all the specifics of the recommendation, and the Commander, Naval Supply Systems Command, responding for the Chief Executive Officer, Naval Exchange Service Command, disagreed with two recommendations and did not adequately address one of the four recommendations. We request these two agencies provide comments to this final report. Please see the Recommendations Table on the back of this page.

Recommendations Table

Management	Recommendations Requiring Comment	No Additional Comments Required
The Auditor General, Department of the Army	B.1	
Director, Defense Information Systems Agency		A.2
Director, National Geospatial-Intelligence Agency		A.2
Director, Missile Defense Agency		A.3, B.1
Commander, United States Special Operations Command		A.1
Director and Chief Executive Officer, Army and Air Force Exchange Service		A.3, B.1
Chief Executive Officer, Naval Exchange Service Command	B.1, B.2, and B.3	A.1

Provide management comments by July 30, 2014.



**INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
4800 MARK CENTER DRIVE
ALEXANDRIA, VIRGINIA 22350-1500**

June 30, 2014

MEMORANDUM FOR COMMANDER, UNITED STATES SPECIAL OPERATIONS COMMAND
DIRECTOR, DEFENSE INFORMATION SYSTEMS AGENCY
DIRECTOR, MISSILE DEFENSE AGENCY
DIRECTOR, NATIONAL GEOSPATIAL-INTELLIGENCE AGENCY
AUDITOR GENERAL, DEPARTMENT OF THE ARMY
DIRECTOR AND CHIEF EXECUTIVE OFFICER, ARMY AND AIR FORCE
EXCHANGE SERVICE
CHIEF EXECUTIVE OFFICER, NAVAL EXCHANGE SERVICE COMMAND

SUBJECT: Implementation of the 2011 Generally Accepted Government Auditing
Standards Independence Standards at the DoD Audit Organizations
(Report No. DODIG-2014-089)

We are providing this report for your review and comment. Five of the seven respondents fully concurred with their specific recommendation(s). However, the Auditor General, Department of the Army concurred with the intent of our recommendation but only partially addressed all the specifics of the recommendation, and the Commander, Naval Supply Systems Command, responding in place of the Chief Executive Officer, Naval Exchange Service Command, nonconcurred with two and did not adequately address one of the four recommendations.

We considered management comments on a draft of this report when preparing the final report. DoD Directive 7650.3 requires that recommendations be resolved promptly. Comments from the Directors, Defense Information Systems Agency, National Geospatial-Intelligence Agency, and Missile Defense Agency, the Commander, United States Special Operations Command, and the Director and Chief Executive Officer, Army and Air Force Exchange Service were responsive, and we do not require additional comments. The Auditor General, Department of the Army also provided comments that were partially responsive on Recommendation B.1. The Commander, Naval Supply Systems Command also provided comments to Recommendations A.1, B.1, B.2, and B.3. Comments to Recommendation A.1 were responsive, and we do not require additional comments. However, comments to Recommendations B.1, B.2, and B.3 did not adequately address the recommendations. Therefore, we request additional comments on Recommendation B.1 (Auditor General, Department of the Army) and Recommendations B.1, B.2, and B.3 (Commander, Naval Supply Systems Command) by July 30, 2014.

Please provide comments that conform to the requirements of DoD Directive 7650.3. Please send a PDF file containing your comments to the email address cited in the last paragraph on this memorandum. Copies of your comments must have the actual signature of the authorizing official for your organization. We cannot accept the /Signed/ symbol in place of the actual signature.

We appreciate the courtesies extended to the staff. Please direct questions to Carolyn R. Davis at (703) 604-8877 (DSN 664-8877), carolyn.davis@dodig.mil.

A handwritten signature in black ink, appearing to read 'R. Stone', with a long horizontal flourish extending to the right.

Randolph R. Stone
Deputy Inspector General
Policy and Oversight

cc:

Director, Defense Commissary Agency
Director, Defense Contract Management Agency
Director, Defense Finance and Accounting Service
Director, Defense Intelligence Agency
Director, Defense Logistics Agency
Director, National Reconnaissance Office
Director, National Security Agency
Deputy Inspector General for Audit, DoD Office of Inspector General
Auditor General, Naval Audit Service
Auditor General, Air Force Audit Agency
Assistant Deputy Commandant for Programs and Resources, and Fiscal Director,
United States Marine Corps

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Acronyms and Abbreviations



Introduction

Objectives

We conducted this review to determine whether the DoD audit organizations implemented the December 2011 generally accepted government auditing standards (GAGAS) independence standards and whether the standards were being followed. See Appendix A for our scope and methodology.

Background

Generally Accepted Government Auditing Standards

The Government Accountability Office (GAO) revised GAGAS in December 2011.¹ The most significant area that changed was the independence standards (to include nonaudit services). GAO created a new GAGAS Conceptual Framework for Independence (see Appendix B for the framework) to provide a means for auditors to assess their independence for activities that are not expressly prohibited in the standards. This more principles-based approach to analyzing independence provides the framework for auditors to assess the unique facts and circumstances that arise during their work that could impair independence. This new framework covers auditor, organizational, and audit (to include nonaudit services) independence.

In addition, a new requirement was added to nonaudit services: to assess and evaluate the audited entity management's ability and willingness to oversee the nonaudit service and for management to designate an individual who possesses suitable skill, knowledge, or experience, and that the individual understands the service to be performed sufficiently to oversee it.

¹ The 2011 revision of generally accepted government auditing standards is effective for financial audits and attestation engagements for periods ending on or after December 15, 2012, and for performance audits beginning on or after December 15, 2011. Early implementation was not permitted.

Finding A

DoD Audit Organizations' Internal Policies for Implementing the 2011 GAGAS Independence Standards

Of the 16 DoD audit organizations reviewed, 10 had fully implemented, 4 had partially implemented, and 2 had not implemented the 2011 GAGAS independence standards. As a result, potential organizational impairments to independence existed for the six audit organizations that had not fully implemented the new independence standards.

GAGAS Independence Standards

The GAO December 2011 GAGAS revision requires audit organizations to establish policies and procedures on independence. GAGAS 3.88 states:

Audit organizations should establish policies and procedures on independence, legal, and ethical requirements that are designed to provide reasonable assurance that the audit organization and its personnel maintain independence and comply with applicable legal and ethical requirements. Such policies and procedures assist the audit organization to: (a) communicate its independence requirements to its staff, and (b) identify and evaluate circumstances and relationships that create threats to independence, and take appropriate action to eliminate those threats or reduce them to an acceptable level by applying safeguards, or, if consider appropriate, withdraw from the audit where withdrawal is not prohibited by law or regulation.

The December 2011 GAGAS revision included a new conceptual framework for independence. GAGAS 3.08 states that this framework should be used by all auditors to assess their independence in three areas for any project undertaken: auditor, organizational, and audit (to include nonaudit services).

- Auditor: An individual auditor needs to evaluate whether there are threats to his/her independence. GAGAS 3.22 states:

Auditors should determine whether identified threats to independence are at an acceptable level or have been eliminated or reduced to an acceptable level. A threat to independence is not acceptable if it either (a) could impact the auditor's ability to perform an audit without being affected by influences that

compromise professional judgment or (b) could expose the auditor or audit organization to circumstances that would cause a reasonable and informed third party to conclude that the integrity, objectivity, or professional skepticism of the audit organization, or a member of the audit team, had been compromised.

- **Organizational:** An audit organization needs to be free of impairments to independence, both externally and internally. DoD audit organizations generally fall under the category of an internal audit organization.

GAGAS 3.31 states:

. . . internal auditors who work under the direction of the audited entity's management are considered independent for the purposes of reporting internally if the head of the audit organization meets all the following criteria: (a) is accountable to the head or deputy head of the entity or those charged with governance; (b) reports the audit results both to the head or deputy head of the government entity and to those charged with governance; (c) is located organizationally outside the staff or line-management function of the unit under audit; (d) has access to those charged with governance; and (e) is sufficiently removed from political pressures to conduct audits and report findings, opinions, and conclusions without fear of political reprisal.

- **Audit (to include nonaudit services):** All work performed at the audit level must be free of impairments to independence. One of the biggest threats to independence for an audit organization is the performance of a nonaudit service. The 2011 GAGAS revision contains a significant amount of guidance for evaluating threats to an audit organization's independence; this must be done before agreeing to perform a nonaudit service. Two key provisions in determining whether to accept a nonaudit service are stated in GAGAS 3.34 and 3.35. GAGAS 3.34 requires the auditor to assess the audited entity management's ability to oversee the nonaudit service and to determine whether the management's designated individual possesses suitable skill, knowledge, or experience. GAGAS 3.35 states:

If an auditor were to assume management responsibilities for an audited entity, the management participation threats created would be so significant that no safeguards could reduce them to an acceptable level. Management responsibilities involve leading and directing an entity, including making decisions regarding the acquisition, deployment and control of human, financial, physical, and intangible resources.

Quality of the Independence Policies

Most of the DoD audit organizations implemented internal policies on or after the December 2011 issuance of GAGAS to guide their organizations with the new independence standards (to include nonaudit services). See Appendix C for a detailed summary of our review.

The quality of the internal policies ranged from just a reference to the new standards to comprehensive internal guidance. Internal policies that just referenced the new standard generally stated that the independence standards were revised and referred to the December 2011 version of GAGAS. The comprehensive policies outlined specific procedures to follow to assess and document auditor, organizational, and audit (to include nonaudit services) independence. For example, some policies contained requirements for both annual and project-specific auditor independence statements. In addition, some policies showed that the audit organization reported to the head of the agency, and other policies contained detailed instructions on how to process a request for a nonaudit service.

Every DoD audit organization is unique in size, mission, and complexity. As such, a one-size-fits-all policy for independence is not appropriate. However, each organization must ensure that their internal policies adhere to the standards promulgated in GAGAS. Our recommendations are directed to DoD audit organizations that either did not create internal policies implementing the December 2011 revision of the GAGAS independence standards or only partially created new policies (for example, performed nonaudit services but had no internal policy on receiving and documenting the request for the service and assessing any threat to independence).

Recommendations, Management Comments, and Our Response

Recommendation A.1

We recommend that the Commander, United States Special Operations Command, and the Chief Executive Officer, Navy Exchange Service Command, ensure their audit organizations create internal policies implementing the December 2011 generally accepted government auditing standards independence standards.

Commander, United States Special Operations Command Comments

The Commander, United States Special Operations Command, agreed and stated its Audit Division of the Office of Inspector General updated its independence policies on April 17, 2013, and included this policy in its updated Standard Operating Procedure dated June 27, 2013.

Our Response

Comments from the Commander, United States Special Operations Command addressed all specifics of the recommendation. No additional comments are required.

Commander, Naval Supply Systems Command Comments

The Commander, Naval Supply Systems Command, responding for the Chief Executive Officer, Naval Exchange Service Command, agreed with the intent of the recommendation. The Commander stated that NEXCOM's internal policies and procedures will be reviewed annually to ensure they reference the current version of the generally accepted government auditing standards (Yellow Book). He further stated that NEXCOM's Office of Internal Audit (OIA) procedural manual is general in nature by design and that the NEXCOM OIA recognizes the Yellow Book as the overarching guidance.

Our Response

Comments from the Commander, Naval Supply Systems Command, addressed the intent of the recommendation. No additional comments are required from NEXCOM.

Recommendation A.2

We recommend that the Directors, Defense Information Systems Agency, and National Geospatial-Intelligence Agency, ensure their audit organizations fully implement the December 2011 generally accepted government auditing standards independence standards.

Directors, Defense Information Systems Agency, and National Geospatial-Intelligence Agency Comments

The Directors, Defense Information Systems Agency, and National Geospatial-Intelligence Agency agreed with the recommendation. Both agencies provided

updated internal audit policies dated January 2014 and March 21, 2014, respectively, fully implementing the December 2011 generally accepted government auditing standards independence standards.

Our Response

Comments from the Directors, Defense Information Systems Agency, and National Geospatial-Intelligence Agency addressed all specifics of the recommendation. No additional comments are required.

Recommendation A.3

We recommend that the Director, Missile Defense Agency, and the Director and Chief Executive Officer, Army and Air Force Exchange Service, ensure that their audit organizations create internal policies and procedures detailing how nonaudit service requests will be assessed and documented for potential impairments to independence.

Director, Missile Defense Agency Comments

The Director, Missile Defense Agency, agreed with the recommendation. MDA is updating their internal audit policies and procedures for assessing and documenting potential impairments to independence for nonaudit services. The estimated completion date is the fourth quarter of FY 2014.

Our Response

Comments from the Director, Missile Defense Agency, addressed all specifics of the recommendation. We request that the Director, Missile Defense Agency, provide a copy of the updated policies and procedures upon issuance. No additional comments are required.

Director and Chief Executive Officer, Army and Air Force Exchange Service Comments

The Director and Chief Executive Officer, Army and Air Force Exchange Service, agreed with the recommendation. AAFES provided new internal audit policy dated December 31, 2013, which establishes procedures detailing how nonaudit service requests will be assessed and documented for potential impairments to independence.

Our Response

Comments from the Director and Chief Executive Officer, Army and Air Force Exchange Service, addressed all specifics of the recommendation. No additional comments are required.

Finding B

DoD Audit Organizations' Adherence to the 2011 GAGAS Independence Standards

Of the five audit organizations that performed a nonaudit service, four did not fully assess and document potential independence impairments before agreeing to perform the service. Also, some auditors' statement of independence were either missing or improperly completed. In addition, one audit organization failed to comply with the standards when performing control self-assessments and continuous auditing. All of these conditions placed the audit organizations in a position of potentially impairing their independence.

GAGAS-Required Analysis and Documentation for Nonaudit Services

The December 2011 revision of the GAGAS independence standards provided more comprehensive guidance to auditors for assessing potential threats to independence when evaluating whether to provide a nonaudit service. One key area of assessment was determining the ability of management at the audited entity to oversee the nonaudit service.

GAGAS 3.34 states:

Before an auditor agrees to provide a nonaudit service to an audited entity, the auditor should determine whether providing such a service would create a threat to independence, either by itself or in aggregate with other nonaudit services provided, with respect to any GAGAS audit it performs. A critical component of this determination is consideration of management's² ability to effectively oversee the nonaudit service to be performed. The auditor should determine that the audited entity has designated an individual who possesses suitable skill, knowledge, or experience, and that the individual understands the services to be performed sufficiently to oversee them. The individual is not required to possess the expertise to perform or reperform the services. The auditor should document consideration of management's ability to effectively oversee nonaudit services to be performed.

² Management, as referred to in GAGAS 3.34, refers to the audited entity's management, not the DoD audit organization's management.

Additionally, GAGAS 3.59(c) states:

[D]ocument consideration of audited entity management's ability to effectively oversee a nonaudit service to be provided by the auditor as indicated in [GAGAS] paragraph 3.34.

Three of the five DoD audit organizations that were performing nonaudit services and had nonaudit service projects that fell within the parameters of our review period had issued policy, created a memorandum of understanding or held meetings (or both), or documented what services were to be provided and who was responsible for the service being provided. However, four³ of the five organizations did not determine and document whether the audited entity's management designated an individual who possessed suitable skill, knowledge, or experience, and that the individual understood the services to be performed sufficiently to oversee them, as required by GAGAS 3.34. Our review of the project files, to include the issued final memo or report, did not disclose any impairment to independence because of this oversight.

A best practice for consideration to meet the requirements of GAGAS 3.34 would be for the auditor to obtain the position description, a resume, or a biography for the designated individual. Then, use professional judgment to determine if the information contained in these documents is adequate to meet the intent of GAGAS 3.34, and document this analysis in the project file as required by GAGAS 3.59(c).

Missing or Improperly Completed Auditor Statements of Independence

For most projects we reviewed, there were instances of missing or improperly completed auditor statements of independence. The improperly completed statements ranged from not being signed by the supervisor to a potential independence impairment being listed but no documented evidence from the supervisor stating how this potential impairment would be mitigated.

Although GAGAS does not specifically require auditor statements of independence, it does require audit organizations to establish policies and procedures on independence. Some statement of independence forms created by the audit organizations referenced the GAGAS 2007 revision, some were in draft form and

³ See Recommendation B.1 for a listing of the four DoD audit organizations.

referenced the GAGAS 2011 revision, and some were current, completely revised, and referenced the GAGAS 2011 revision. However, because the concept of auditor independence has not changed from previous revisions, any statement of independence form declaring an auditor's independence and having supervisory review and concurrence would satisfy the intent of documenting auditor independence. Therefore, our review determined whether an audit organization required statements of independence to be completed by their auditors, and if so, were they completed and filed. Because of the minor nature of the issues found, we did not make any recommendations in this report to any DoD audit organization concerning statements of independence. Appendix D contains suggested best practice for audit organizations to use in formatting auditor statements of independence.

Naval Exchange Service Command Internal Audit's Application of the GAGAS Conceptual Framework

We reviewed the Naval Exchange Service Command Internal Audit's (NEXCOM IA's) control self-assessment (CSA) activities and continuous auditing activities to determine whether those activities complied with the December 2011 GAGAS independence standards⁴.

GAGAS 2.13 states:

When audit organizations provide nonaudit services to entities for which they also provide GAGAS audits, they should assess the impact that providing those nonaudit services may have on auditor and audit organization independence and respond to any identified threats to independence in accordance with the GAGAS independence standard.

GAGAS 3.03 (b) states:

Independence in Appearance

The absence of circumstances that would cause a reasonable and informed third party, having knowledge of the relevant information, to reasonably conclude that the integrity, objectivity, or professional skepticism of an audit organization or member of the audit team had been compromised.

⁴ We became aware in November 2012 during a DoD Small Audit Working Group Meeting that NEXCOM was performing control self-assessments and continuous auditing – activities not normally performed by most DoD audit organizations. Therefore, we decided to review these activities at NEXCOM as part of this project.

GAGAS 3.20 states:

Auditors should evaluate threats to independence using the [GAGAS] conceptual framework when the facts and circumstances under which the auditors perform their work may create or augment threats to independence. Auditors should evaluate threats both individually and in the aggregate because threats can have a cumulative effect on an auditor's independence.

Control Self-Assessments

CSA is a technique that allows managers and work teams directly involved in business units, functions, or processes to participate in assessing the organization's risk management and control processes. To better understand NEXCOM's CSA activities, we observed NEXCOM Internal Audit's staff and the entity's management conducting a CSA at a Navy Exchange store. We concluded that NEXCOM Internal Audit should include in their audit policies how they will safeguard and maintain their independence when performing CSA activities.

Continuous Auditing Activities

To better understand NEXCOM IA's continuous auditing activities and their role in the government purchase card program, we interviewed NEXCOM IA staff and a NEXCOM contracting office staff member and reviewed the NEXCOM government purchase card program regulations and procedures. During our review, we were informed by NEXCOM IA that the continuous auditing activities they conducted in the NEXCOM Government Purchase Card program were a pilot program and their continuous auditing activities had not been fully implemented. However, NEXCOM IA personnel stated that once the continuous auditing activities are fully implemented, they will expand them to other areas of NEXCOM and conduct continuous auditing activities as performance audits.

The NEXCOM Corporate Contracts office internal operating procedure⁵ identifies the responsibilities of the NEXCOM offices and authorized card-holders in the purchase card program, the allowed uses for the purchases card, the internal controls over the purchase card program, and the internal and external reviews of the program. The internal operating procedure identifies the NEXCOM IA as the NEXCOM organization that will schedule and conduct a purchase card desk audit or onsite review.

⁵ "The Navy Non-Appropriated Fund Purchase Card Program - Internal Operating Procedure, Revision Date: 12/8/2009 (edited 10/2012)."

During our review of the internal operating procedure, we noted that the procedure contained language directing the NEXCOM IA to perform transactional reviews, internal management control reviews, and reviews of other specific purchase elements. The internal operating procedure also contained detailed guidance on how NEXCOM IA would perform these reviews. We consider this to be a potential independence impairment, as it appears the operational unit was directing NEXCOM's IA function.

Further, we determined that the NEXCOM IA continuous auditing activities as considered under the pilot program were a nonaudit service. NEXCOM did not apply the 2011 GAGAS independence standards to their continuous auditing activities pilot program for the NEXCOM purchase card. The acceptability of, and GAGAS compliance over, the conduct of continuous auditing as a performance audit was not determined as part of this review. In addition, NEXCOM IA did not document its consideration of the audited entity management's ability to effectively oversee the nonaudit services it was performing, to include documenting the assigned individual's skill, knowledge, or experience.

Recommendations, Management Comments, and Our Response

Recommendation B.1

We recommend that the Auditor General, Department of the Army; the Director, Missile Defense Agency; the Director and Chief Executive Officer, Army and Air Force Exchange Service; and the Chief Executive Officer, Navy Exchange Service Command, ensure their audit organizations perform all the required independence analyses and document the results before accepting a nonaudit service.

Auditor General, Department of the Army Comments

The Auditor General, Department of the Army, agreed with the intent of the recommendation as it relates to documenting the results of their independence analysis. However, the Auditor General did not agree that his auditors were deficient in the independence analysis as required by GAGAS 3.34. The Auditor General stated that they considered the audited entity's management subject matter experts and as such, were fully aware of the nonaudit service they requested and could determine if it met their requirements. Further, as subject matter experts, they also had sufficient knowledge of the area and had the ability to either accept or reject the results. The

Auditor General also stated that before accepting the nonaudit service, they performed a thorough and comprehensive evaluation to determine if the requested nonaudit service would impair the agency's or the auditors' independence. The evaluation included determining the client's understanding of the results and the services. He further stated that the client was provided with a memorandum of understanding describing the services agreed to and how the results can and cannot be used.

Our Response

Comments from the Auditor General, Department of the Army, did not address the specifics of the recommendation. GAGAS 3.34 requires the auditor to assess the audited entity management's ability to oversee the nonaudit service and to determine whether the management's designated individual possesses suitable skill, knowledge, or experience. We acknowledged that the Army Audit Agency created memoranda of understanding and performed other procedures when agreeing to perform a nonaudit service. However, no evidence was provided showing how the auditors evaluated and documented the skill, knowledge, or experience of the designated management individual, as required by GAGAS 3.34. The Auditor General's comments did not address GAGAS 3.34. Our report provided a best practice for some types of documentation that would satisfy the GAGAS requirement of determining whether the management's designated individual possessed suitable skill, knowledge, or experience. We request that the Auditor General, Department of the Army, reconsider his position on the recommendation and provide comments in response to the final report.

Director, Missile Defense Agency Comments

The Director, Missile Defense Agency, agreed with the recommendation. MDA is updating its internal audit policies and procedures to include guidance to evaluate and document the skills, knowledge, or experience of the management-appointed individual overseeing the nonaudit service. The estimated completion date is the fourth quarter of FY 2014.

Our Response

Comments from the Director, Missile Defense Agency, addressed all specifics of the recommendation. We request that the Director, Missile Defense Agency, provide a copy of the updated policies and procedures upon issuance. No additional comments are required.

Director and Chief Executive Officer, Army and Air Force Exchange Service Comments

The Director and Chief Executive Officer, Army and Air Force Exchange Service, agreed with the recommendation. AAFES provided new internal audit policy dated December 31, 2013, which establishes procedures on evaluating and documenting the skills, knowledge, or experience of the management-appointed individual overseeing the nonaudit service.

Our Response

Comments from the Director and Chief Executive Officer, Army and Air Force Exchange Service, addressed all specifics of the recommendation. No additional comments are required.

Commander, Naval Supply Systems Command Comments

The Commander, Naval Supply Systems Command, responding for the Chief Executive Officer, Naval Exchange Service Command, agreed with the recommendation, stating that if and when NEXCOM OIA accepts to perform a nonaudit service, the proper documentation will be prepared in accordance with GAGAS. The Commander also stated that the NEXCOM OIA uses control self-assessments and continuous auditing to facilitate traditional audits, and does not consider these processes to be nonaudit services. Further, the Commander stated that GAGAS 3.40 specifies that routine activities performed by auditors that relate directly to the performance of an audit, such as providing advice and responding to questions as part of an audit, are not nonaudit services, according to GAGAS. Such routine activities generally involve providing advice or assistance to the entity on an informal basis as part of an audit. Routine activities typically are insignificant in terms of time incurred or resources expended and generally do not result in a specific project or engagement or in the auditors producing a formal report or other formal work product.

Our Response

Comments from the Commander, Naval Supply Systems Command partially addressed the recommendation. NEXCOM OIA stated its review of the NEXCOM government purchase card program, using ACL Services Ltd. ACL Audit Exchange software program, was a continuous audit. However, based on our observation, the continuous audit program was not fully developed. NEXCOM OIA stated that its continuous auditing program was still in a testing phase, and as such, lacked a formal process for reporting findings and recommendations and tracking management's actions on those recommendations. During this pilot program, the

auditors were providing management, on a monthly, informal basis, all the anomalies they found when running this continuous auditing program on the government purchase card transactional database, thereby creating the potential for independence impairment. NEXCOM OIA stated that they were going to fully implement the ACL Audit Exchange software program to perform audits in accordance with GAGAS on this and other NEXCOM programs in the near future. Based on the above, we determined that the way NEXCOM OIA was performing this continuous auditing pilot program was a nonaudit service, and therefore, NEXCOM OIA should have performed all the GAGAS-required independence analyses and documented the results before performing this service to mitigate any potential independence impairments. Upon NEXCOM OIA's full implementation of its continuous auditing program, to include reporting on findings and recommendations, and tracking management action on those recommendations, the appearance of a potential independence impairment would no longer exist. We request the Commander, Naval Supply Systems Command, reconsider his position on the recommendation and provide comments in response to the final report.

Recommendation B.2

We recommend that the Chief Executive Officer, Naval Exchange Service Command, ensure that his audit organization revise its internal audit policies to include procedures for performing control self-assessments and continuous auditing.

Commander, Naval Supply Systems Command Comments

The Commander, Naval Supply Systems Command, responding for the Chief Executive Officer, Naval Exchange Service Command, disagreed with the recommendation. The Commander stated that control self-assessments and continuous auditing are not nonaudit services; and therefore, a revision to NEXCOM OIA's policies would be inaccurate. He further stated that NEXCOM OIA's procedural manual would provide routine internal control advice to NEXCOM's management.

Our Response

Comments from the Commander, Naval Supply Systems Command, did not address the specifics of the recommendation. We recognize that performing control self-assessments and continuous auditing are proactive measures. However, since there are no GAGAS standards or International Standards for the Professional Practice of Internal Auditing (Standards) specifically covering

control self-assessments and continuous auditing, it would be incumbent upon NEXCOM OIA to document in its internal audit policies how it performs these processes. We request the Commander, Naval Supply Systems Command, reconsider his position on the recommendation and provide comments in response to the final report.

Recommendation B.3

We recommend that the Chief Executive Officer, Navy Exchange Service Command, remove the language from “The Navy Non-Appropriated Fund Purchase Card Program-Internal Operating Procedure, Revision Date: 12/8/2009 (edited 10/2012)” that appears to direct the functions of the Office of Internal Audit.

Commander, Naval Supply Systems Command Comments

The Commander, Naval Supply Systems Command, responding for the Chief Executive Officer, Naval Exchange Service Command, disagreed with the recommendation. The Commander stated that NEXCOM OIA’s organizational independence is safeguarded by having NEXCOM OIA reporting directly to the Chief Executive Office, Navy Exchange Service Command. He further stated that the language in the internal operating procedure manual was prepared by NEXCOM OIA, and this can be viewed as an additional safeguard for NEXCOM OIA’s independence. Additionally, the Commander stated that this language in the internal operating procedure manual is compliant with GAGAS.

Our Response

Comments from the Commander, Naval Supply Systems Command, did not address the specifics of the recommendation. Having an internal audit organization write policy contained in the audited entity’s management’s operational procedural manual creates the potential for impairment to independence. NEXCOM OIA is responsible for auditing all policies and programs of NEXCOM’s operations and as such, should not write management policy it would potentially be auditing. Additionally, any policies protecting NEXCOM OIA’S independence should be part of NEXCOM OIA’s policies. We request the Commander, Naval Supply Systems Command, reconsider his position on the recommendation and provide comments in response to the final report.

Appendix A

Scope and Methodology

We reviewed the policies of 16 of the 21 DoD audit organizations to determine whether they implemented the December 2011 GAGAS independence standards. Five audit organizations were not included in this review for the following reasons.

- The United States Army Internal Review is currently in the process of converting their personnel back to GS-0511 auditors from GS-0510 accountants, and therefore, requires time to reestablish itself as an audit organization.
- The National Guard Bureau Internal Review recently fell back under the oversight authority of the DoD Inspector General (IG) and is scheduled for a full review in the near future.
- The Defense Intelligence Agency (DIA), National Reconnaissance Office (NRO), and National Security Agency (NSA) were, or are being, covered as a part of the normal peer review process that the DoD IG administers, to include review of their policy and implementation relative to the 2011 GAGAS independence standard.⁶

Of the 16 audit organizations we reviewed, we judgmentally selected projects from 11 of the organizations. We did not select projects from five organizations for the following reasons.

- The Defense Contract Audit Agency's policies and procedures are overseen by the DoD Deputy Inspector General, Policy and Oversight, Audit and Policy Oversight, Contract Audit Policy and Oversight division.
- The Defense Contract Management Agency received a pass rating from an external quality control review.
- The Defense Information System Agency and the Defense Logistics Agency will receive a full quality control review in the near future due to their failure in a recent external Quality Control Review.
- The National Geospatial-Intelligence Agency did not have any completed projects within the scope of our review.

⁶ NSA's peer review report was issued on February 27, 2013; NRO is currently undergoing a peer review; and DIA is due a peer review this fiscal year.

As part of our review, we:

- obtained the current policies from the audit organizations;
- obtained a listing of all performance projects, to include nonaudit services projects;
- contacted the GAO; and
- contacted other Federal Offices of Inspectors General to benchmark their implementation of the December 2011 Version of GAGAS.
 - Department of Justice,
 - Department of Housing and Urban Development,
 - House of Representatives,
 - National Aeronautics and Space Administration,
 - National Science Foundation, and
 - Legal Services Corporation.

Our review covered the period December 15, 2011, through January 29, 2013. We performed this review from December 2012 through November 2013 in accordance with the standards published in the Council of the Inspectors General on Integrity and Efficiency, “Quality Standards for Inspection and Evaluation,” January 2012.

Use of Computer-Processed Data

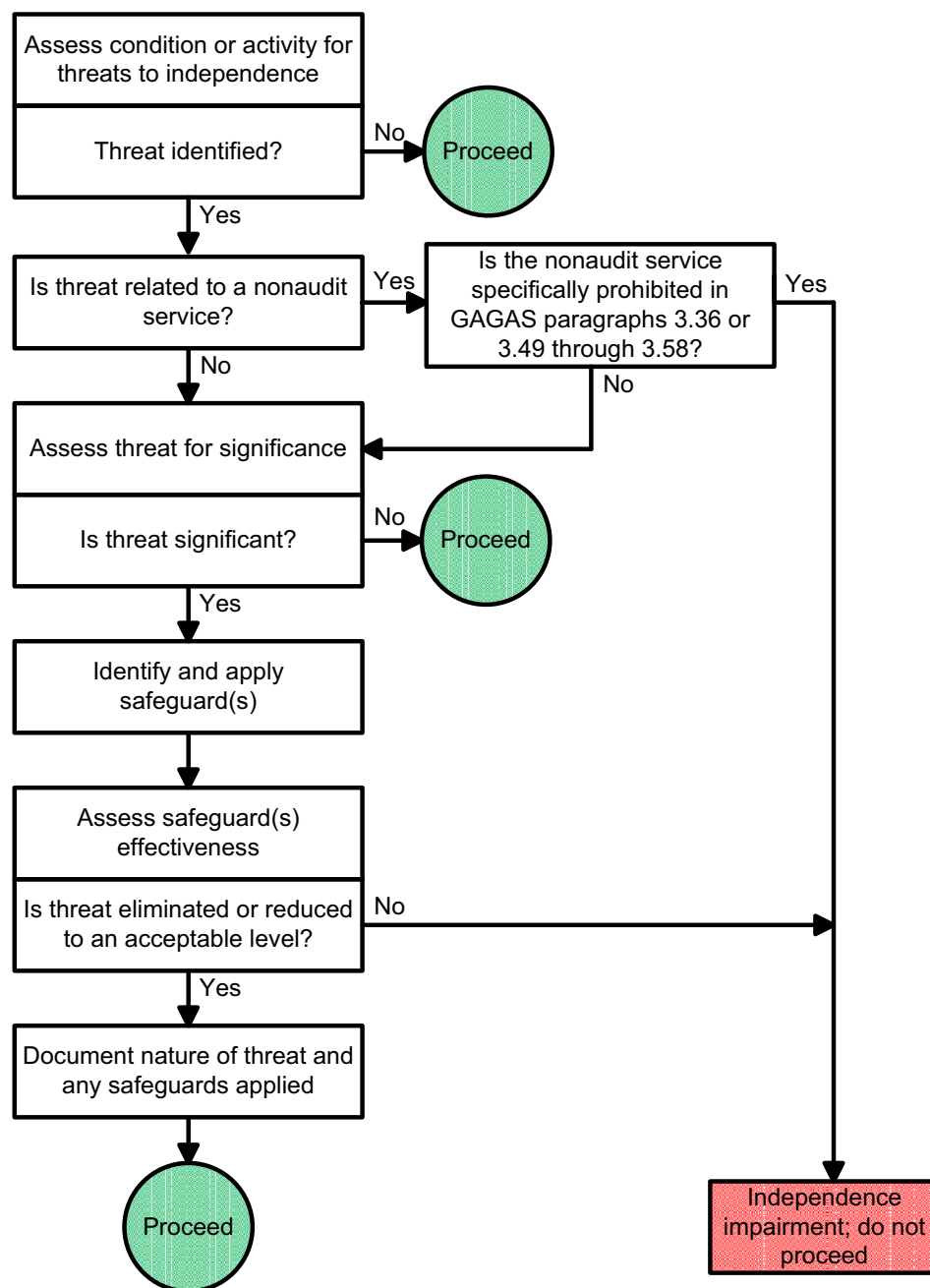
We did not use computer-processed data to perform this audit.

Prior Coverage

During the last 5 years, no prior coverage has been conducted on implementation of the December 2011 GAGAS independence standards.

Appendix B

GAGAS Conceptual Framework for Independence



Source: GAO

Appendix C

DoD Audit Organizations' Policies on Independence

DoD Audit Organizations' Policies on Independence (to include Nonaudit Services) Implementing Government Auditing Standards, December 2011 Revision			
DoD Audit Organization	Auditor Independence GAGAS 3.08, 3.20, and 3.88	Organizational Independence ¹ GAGAS 3.31	Nonaudit Services GAGAS 3.33-3.58, and 3.88
AAA	YES	YES	YES
AAFES	YES	YES	NO ³
AFAA	YES	YES	NO ⁴
Army IR ²	N/R	N/R	N/R
DeCA	YES	YES	YES
DCAA	YES	YES	YES
DCMA	YES	YES	YES
DFAS	YES	YES	YES
DISA	NO ⁵	YES	NO ⁵
DIA	N/R	N/R	N/R
DLA	YES	YES	YES
DOD IG	YES	YES	YES
MCNAFAS	YES	NO ⁶	YES
MDA	YES	YES	NO ³
NGA	NO ⁵	YES	NO ⁴
NGB	N/R	N/R	N/R
NRO	N/R	N/R	N/R
NSA	N/R	N/R	N/R
NAS	YES	YES	YES
NEXCOM	NO ⁷	YES	NO ³
USSOCOM	NO ⁸	YES	NO ⁴

¹ Organizational Independence in this table refers to whether the audit organization reports to the head of the agency.

² In a June 14, 2013, memorandum, the Secretary of the Army directed all Army Internal Review personnel to convert back to GS-0511 series auditors.

³ AAFES, MDA, and NEXCOM perform nonaudit services, but neither AAFES nor MDA had internal policies governing the performance of a nonaudit service, and NEXCOM did not have updated policies. MDA fills out a nonaudit services statement form to document who requested the service; that the service was not done in accordance with GAGAS; and that they used the GAGAS Conceptual Framework for Independence in determining whether to perform the requested nonaudit service. However, this form does not contain a section to document the new nonaudit services requirement in GAGAS 3.34 to evaluate and document the skill, knowledge, or experience of the management-appointed individual who would oversee the nonaudit service.

- ⁴ AFAA, NGA, and USSOCOM stated they do not perform nonaudit services.
- ⁵ DISA's current audit policies are dated March 2011, and NGA's are dated September 29, 2009. DISA and NGA are in the process of updating their policies. However, DISA and NGA revised their statement of independence form to implement the December 2011 GAGAS independence standard for auditor independence; and DISA developed a nonaudit services checklist.
- ⁶ The Marine Corps Nonappropriated Fund Audit Service (MCNAFAS) does not report directly to the Commandant or Assistant Commandant, United States Marine Corps. MCNAFAS is situated in the Deputy Commandant, Programs and Resources (P&R) office and reports directly to the Assistant Deputy Commandant, P&R.
- ⁷ NEXCOM IA current audit policies are dated 1997 (and updated as needed, but not re-dated). Based on the policies provided, we concluded that their audit policies were not updated to reflect the December 2011 GAGAS.
- ⁸ USSOCOM did not have internal audit policies implementing the December 2011 GAGAS independence standards. However, during our review, they issued new internal audit policies on April 17, 2013, and these policies adequately implement the December 2011 GAGAS independence standards.

NR = Not Reviewed (see Appendix A Scope and Methodology for reasons).

Appendix D

Best Practice for Formatting Auditor Statement of Independence

After comparing 16 different auditor statements of independence from the DoD audit organizations we reviewed, we suggest that the following be included in an auditor statement of independence:

- document title (for example, Annual Statement of Independence or Project-Specific Statement of Independence);
- fields for name, title, and fiscal or calendar year (for annual statement of independence) and project title, project number, team member's name, and team member's title (for project specific statement of independence);
- a paragraph referencing GAGAS and the audit organization's internal policies for independence;
- fields for auditors to state they are independent or they have a potential impairment (and stating the potential impairment), and a place to sign and date; and
- fields for the auditor's supervisor to concur with the auditor's stated independence or how a potential impairment is dealt with (for example, the auditor cannot audit in a certain area of the organization or the auditor has been reassigned to another audit) and a place to sign and date.

Management Comments

The Auditor General, Department of the Army Comments



DEPARTMENT OF THE ARMY
U.S. ARMY AUDIT AGENCY
OFFICE OF THE PRINCIPAL DEPUTY AUDITOR GENERAL
6000 6TH STREET, BUILDING 1464
FORT BELVOIR, VA 22060-5609

SAAG-ZB

14 April 2014

MEMORANDUM FOR Mr. Randolph R. Stone, Deputy Inspector General, Policy and Oversight, 4800 Mark Center Drive, Alexandria, VA 22350-1500

SUBJECT: Official Reply to DODIG Report Implementation of 2011 Generally Accepted Government Auditing Standards Independence Standards at the DOD Audit Organizations, 7 March 2014 (Project No. D2013-DAPOIA-0011.001)

1. The U.S. Army Audit Agency (AAA) has reviewed the subject draft report. We concur with the intent of the recommendation but not fully with the details in the report.
2. The following paragraphs contain the review objective, conclusion, recommendation and our response:
 - a. **Objective:** To determine whether the DOD audit organizations implemented the December 2011 Generally Accepted Government Auditing Standards (GAGAS) independence standards and whether the standards were being followed.
 - b. **Conclusion:** [As the report relates to non-audit service provided to an audited entity] "...four of the five organizations did not determine and document whether the audited entity's management designated an individual who possessed suitable skill, knowledge, or experience, and that the individual understood the services to be performed sufficiently to oversee them, as required by GAGAS 3.34. Our review of the project files, to include the issued final memo or report, did not disclose any impairment to independence because of this oversight."
 - c. **Recommendation:** We recommend that The Auditor General, Department of the Army ensure their audit organization perform all of the required independence analysis and document the results before accepting a non-audit service.
 - d. **AAA Response:** AAA agrees with the intent of the recommendation as it relates to documenting the results of our independence analysis. However, we don't agree that that Agency's auditors were deficient in the independence analysis as required by GAGAS 3.34. When discussing the intent of the standard and our projects with technical assistance at GAO, we concluded that we did meet the intent of GAGAS 3.34, but did not adequately document our analysis. Agency non-audit service engagements, which are small in number, are not overseen by personnel from the audited entity, and for the projects selected by the DoDIG audit team, clients receiving our products did not oversee our work. We considered them functional subject matter experts, and,

The Auditor General, Department of the Army Comments (cont'd)

SAAG-ZB

SUBJECT: Official Reply to DODIG Report Implementation of 2011 Generally Accepted Government Auditing Standards Independence Standards at the DOD Audit Organizations, 7 March 2014 (Project No. D2013-DAPOIA-0011.001)

therefore, these clients were fully aware of the service they requested and could decide whether our product met their intent. As subject matter experts, they also had sufficient knowledge of the area and had the ability to either accept or reject our results. This is the essence of oversight.

Before accepting a non-audit service, we performed a thorough and comprehensive evaluation to determine if the requested nonaudit services would impair either the Agency's or the auditor's independence for conducting present or future engagements at the entity that requested such services. This evaluation includes determining the client's understanding of the results of our services and our products. On future engagements we plan to better document our evaluation and the client's understanding.

In the case of the project in question, management only provided the basic information needed for us to perform our analysis. They did not oversee the project. The audit team provided the client with a memorandum of understanding (MOU) that had a comprehensive description of the services we agreed to provide and how the results can and cannot be used. The MOU was included in the audit files.

3. We want to thank the DODIG audit team for their review. If you have any additional questions or concerns, [REDACTED]

FOR THE AUDITOR GENERAL:



JOSEPH P. BENTZ
Principal Deputy Auditor General

CF:
Program Director, Audit Policy and Coordination, USAAA

Director, Defense Information Systems Agency Comments



DEFENSE INFORMATION SYSTEMS AGENCY

P. O. BOX 549
FORT MEADE, MARYLAND 20755-0549

APR 07 2014

MEMORANDUM FOR DEPARTMENT OF DEFENSE INSPECTOR GENERAL (DoDIG)

SUBJECT: Defense Information Systems Agency (DISA) comments and responses to the Draft Audit Report on the Implementation of 2011 Generally Accepted Government Auditing Standards Independence Standards at the DoD Audit Organizations, dated March 7, 2014, (Project No. D2013-DAPOIA-0011.001)

The Defense Information Systems Agency (DISA) has reviewed the draft report referenced above and provides comments as enclosed.

[REDACTED]


RONNIE D. HAWKINS, JR.
Lieutenant General, USAF
Director

Attachment:
As stated

Director, Defense Information Systems Agency Comments (cont'd)

Defense Information Systems Agency (DISA) responses to the Draft Report on the Implementation of 2011 Generally Accepted Government Auditing Standards Independence Standards at the DoD Audit Organizations, dated March 7, 2014, (Project No. D2013-DAPOIA-0011.001)

DISA COMMENTS TO RECOMMENDATIONS:

RECOMMENDATION A.2: The Directors, DISA, and National Geospatial-Intelligence Agency, ensure their audit organizations fully implement the December 2011 Generally Accepted Government Auditing Standards Independence Standards.

DISA RESPONSE: Concur

DISA IG has fully implemented the December 2011 Generally Accepted Government Auditing Standards Independence Standards into its audit manual. DISA IG provided the new independence section to the DoDIG in the exit conference, dated January 15, 2014.

Estimated Completion Date: Completed

Director, National Geospatial-Intelligence Agency Comments



NATIONAL GEOSPATIAL-INTELLIGENCE AGENCY

7500 GEOINT Drive
Springfield, Virginia 22150 APR 4 2014

U-2014-1019

MEMORANDUM FOR INSPECTOR GENERAL, DEPARTMENT OF DEFENSE
DEPUTY INSPECTOR GENERAL FOR POLICY AND
OVERSIGHT

SUBJECT: (U) National Geospatial-Intelligence Agency Response to Project
No. D2013-DAPOIA-0011.001

REFERENCES: (U) "Implementation of 2011 Generally Accepted Government
Auditing Standards Independence Standards at the DoD Audit
Organizations," Project No. D2013-DAPOIA-0011.001,
07 March 2014

1. Thank you for the opportunity to comment on the subject draft report. This memorandum is in response to the recommendation issued in the reference.

2. (U) Recommendation A.2.

a. (U) Department of Defense Inspector General Recommendation: That the Directors of the Defense Information Systems Agency and the National Geospatial-Intelligence Agency (NGA) ensure their audit organizations fully implement the December 2011 generally accepted government auditing standards.

b. (U) NGA Response: NGA concurs with the recommendation. The NGA Audit Division, Office of Inspector General, updated its independence statement form to reflect December 2011 generally accepted government auditing standards prior to this review. Subsequently, the division published an updated handbook to reflect the changes in standards and revised the independence statement form based on best practices found at another agency. Enclosed are copies of the relevant section of the handbook and revised independence statement form.

A handwritten signature in blue ink, appearing to read "Letitia A. Long", is positioned above the printed name.

Letitia A. Long
Director

Enclosures as stated

Director, National Geospatial-Intelligence Agency Comments (cont'd)



NATIONAL GEOSPATIAL-INTELLIGENCE AGENCY

Know the Earth... Show the Way... Understand the World

**OFFICE OF INSPECTOR GENERAL
AUDIT DIVISION**

AUDIT HANDBOOK



THIRD EDITION

21 March 2014



Director, National Geospatial-Intelligence Agency Comments (cont'd)

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Section 1. GENERAL STANDARDS

Generally Accepted Government Auditing Standards (GAGAS), as promulgated by the Government Accountability Office, are broad statements of auditors' responsibilities to help ensure that auditors have sufficient competence, integrity, objectivity, and independence to plan, conduct, and report their work. The general standards provide the underlying framework that is critical in effectively applying the fieldwork and reporting standards, and are required to be followed by all auditors and the audit organization performing work under GAGAS. The general standards are independence, professional judgment, competence, and quality control and assurance.

Chapter 1-1: Independence

Independence means that an auditor must be independent in mind and in appearance.¹ GAGAS 3.02–3.59 requires auditors, consultants, technical experts, and other team members need to consider threats to independence that may affect their ability to do the work and report the findings impartially. In addition, they must identify any potential threat that could cause them not to be viewed as impartial by knowledgeable third parties. The NGA Office of Inspector General (OIG), which includes OIG senior leadership at the Inspector General (IG), Deputy IG (DIG), Counsel to the IG, and Assistant Inspector General levels, unless otherwise noted, is organizationally independent when reporting externally because it is a Designated Federal Entity and removal of the IG requires notification to Congress. The IG, DIG, and Counsel to the IG are expected to recuse themselves from projects where they have an independence threat.

Determining Independence

GAGAS 3.07-3.26 provides the conceptual framework for independence. It requires auditors to make independence determinations by identifying threats to independence, evaluating the significance of those threats, applying safeguards to eliminate the threats or reduce them to an acceptable level, and, if the threat cannot be eliminated or reduced to an acceptable level, concluding that independence is impaired. Where threats to independence are not at an acceptable level requiring the application of safeguards, GAGAS 3.24 and 3.59(a) require the auditors to document the threats identified and the safeguards applied to eliminate the threats or reduce them to an acceptable level.

¹ Independence in mind is a state of mind that permits the expression of a conclusion without being affected by influences that compromise professional judgment, thereby allowing an individual to act with integrity, and exercise objectivity and professional skepticism. Independence in appearance is the avoidance of facts and circumstances that are so significant that a reasonable and informed third party would be likely to conclude, weighing all the specific facts and circumstances, that an auditor's integrity, objectivity, or professional skepticism has been compromised.

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Director, National Geospatial-Intelligence Agency Comments (cont'd)

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Threats. Threats to independence are circumstances that could impair independence. Threats do not necessarily impair independence but must be evaluated using the conceptual framework. GAGAS 3.14 provides the following seven broad categories of threats to independence:

- **Self-interest.** The threat that a financial or other interest will inappropriately influence an auditor's judgment or behavior.
- **Self-review.** The threat that an auditor or audit organization that has provided nonaudit services will not appropriately evaluate the results of previous judgments made or services performed as part of the nonaudit services when forming a judgment significant to an audit.
- **Bias.** The threat that an auditor will, as a result of political, ideological, social, or other convictions, take a position that is not objective.
- **Familiarity Over Time.** The threat that aspects of a relationship with management or personnel of an audited entity, such as a close or long relationship, or that of an immediate or close family member, will lead an auditor to take a position that is not objective.
- **Undue Influence.** The threat that external influences or pressures will impact an auditor's ability to make independent and objective judgments.
- **Management Participation.** The threat that results from an auditor's taking on the role of management or otherwise performing management functions on behalf of the entity undergoing an audit.
- **Structural.** The threat that an audit organization's placement within a government entity, in combination with the structure of the government entity being audited, will impact the audit organization's ability to perform work and report results objectively.

Safeguards. If identified threats to independence are significant, the auditor must then determine whether safeguards could be put in place to mitigate those threats to an acceptable level. Safeguards are controls designed to eliminate or reduce threats to independence to an acceptable level. GAGAS 3.17 and 3.19 provide examples of safeguards and may be used as a starting point to auditors who have identified threats to independence and are considering what safeguards could eliminate those threats or reduce them to an acceptable level.

The threat assessment and application of safeguards requires professional judgment. If the auditor concludes that there are no safeguards sufficient to reduce a threat to an acceptable level then the auditor should decline to perform the project.

Documenting Independence

The Project Lead will ensure the IC, DIG, Assistant Inspector General for Audit (AIGA), Deputy AIGA (DAIGA), technical experts, and the team members sign the Statement of Independence as part of the announcement package prior to beginning a project. New team members will sign

Director, National Geospatial-Intelligence Agency Comments (cont'd)

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the Statement of Independence when they join the team. Independent Reference Reviewers will sign the Statement of Independence before they perform the independent reference review. The AIGA will recuse him/herself in the event of any threat. In these cases, the DAIGA will take on the responsibilities of the AIGA for the project. If a team member considers their independence impaired, they must notify management in writing immediately. The AIGA or DAIGA must review and determine the extent of the threat, and either remove the employee from the project or take appropriate action to limit the effect of the threat. If a threat to independence is identified after the auditor's report has been issued, the auditor should notify the AIGA and DAIGA of the situation at which time they should review the extent and impact of the threat on the project. If the AIGA and DAIGA conclude that independence is impaired and the report issued would have been different had the auditors been aware of it, the impact should be communicated to management in the same manner as the report was originally distributed. The signed Statements of Independence must be included in the workpapers for each project.

Chapter 1-2: Professional Judgement

GAGAS 3.60–3.68 establishes standards for professional judgment in planning and performing audits and in reporting the results. Auditors must exercise reasonable care and professional skepticism in accordance with professional standards and ethical principles.

Professional judgment requires the evaluation and determination of the required level of understanding for a project and related circumstances. It represents the application of the collective knowledge, skills, and experiences of all personnel involved with a project. The auditor should consider the risk of the project and the standards, scope, and methodology that should be applied to the project. Professional judgment should also be used to determine the sufficiency and appropriateness of evidence used to support findings and conclusions.

Reasonable care is applied by acting diligently in accordance with applicable professional standards and ethical principles. An auditor should use their professional knowledge, skills, and experience to gather information and evidence while maintaining the highest degree of integrity, objectivity, and independence in applying professional judgment to their work. Professional skepticism implements an attitude where an auditor assumes that management is neither dishonest nor of unquestioned honesty. This should occur when gathering evidence and objectively evaluating the sufficiency, competency, and relevancy of the evidence. Auditors must critically assess appropriate and persuasive evidence to reach a conclusion.

Professional judgment imposes responsibilities to assess situations for “reasonable assurance” and determine if non-compliance with GAGAS is occurring. Non-compliance with GAGAS must be justified and documented. If the team is unable to follow an applicable standard and not able to withdraw from the project, the team should disclose in the scope section of the report what applicable standard was not followed, the reasons it was not followed, and the known affect it had on the results of the project.

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Director, National Geospatial-Intelligence Agency Comments (cont'd)



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Auditor Statement of Independence

Project Title:	Project Number:
Auditor Name:	Title:
<p>Background Information</p> <p>In all matters relating to the audit work, the audit organization and the individual auditor, whether government or public, must be independent (GAGAS 3.02). Auditors and audit organizations maintain independence so that their opinions, findings, conclusions, judgments, and recommendations will be impartial and viewed as impartial by reasonable and informed third parties. Auditors should avoid situations that could lead reasonable and informed third parties to conclude that the auditors are not independent and thus are not capable of exercising objective and impartial judgment on all issues associated with conducting the audit and reporting on the work (GAGAS 3.04). Generally accepted government audit standards (GAGAS) consideration of independence consists of four interrelated sections seen at GAGAS 3.06, providing:</p> <p>*Conceptual framework for making independence determinations based on facts and circumstances that are often unique to a specific environment,</p> <p>*Requirements for and guidance on:</p> <ul style="list-style-type: none"> -independence for audit organizations that are structurally located within the entities they audit, -independence for auditors performing non-audit service, and -documentation necessary to support adequate consideration of auditor independence. 	
Conceptual Framework to be applied by individual auditors	
<i>Threats to Independence</i>	
	Yes/No
1. Self Interest Threats The threat that a financial or other interest will inappropriately influence an auditor's judgment or behavior (examples: GAGAS A3.03). Do you have any self interest threats?	
2. Self Review Threats The threat that an auditor or audit organization that has provided nonaudit services will not appropriately evaluate the results of previous judgments made or services performed as part of the nonaudit services when forming a judgment significant to an audit (examples: GAGAS A3.04). Do you have any self-review threats?	
3. Bias Threats The threat that an auditor will, as a result of political, ideological social, or other convictions, take a position that is not objective (examples: GAGAS A3.05). Do you have any bias threats?	
4. Familiarity Threats The threat that aspects of a relationship with management or personnel of an audited entity, such as close or long relationship, or that of an immediate or close family member, will lead an auditor to take a position that is not objective (examples: GAGAS A3.06). Do you have any familiarity threats?	

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Director, National Geospatial-Intelligence Agency Comments (cont'd)



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Auditor Statement of Independence

5. Undue Influence Threats The threat that external influences or pressures will impact an auditor's ability to make independent an objective judgments (examples: GAGAS A3.07). <i>Do you have any undue influence threats?</i>		
6. Management Participation Threats The threat that results from an auditor's taking on the role of management or otherwise performing management functions on behalf of the entity undergoing an audit (examples: GAGAS A3.08). <i>Do you have any management participation threats?</i>		
7. Structural Threats The threat an auditor organization's placement within a government entity, in combination with the structure of the government entity being audited, will impact the auditor organization's ability to perform work and report results objectively (examples: GAGAS A3.09). <i>Are you aware of any structural threats?</i>		
For Nonaudit Services-Documentation (GAGAS 3.59)		
8. Have you read and understand the requirements for performing nonaudit services as discussed in GAGAS 3.33-3.48?		
9. Have you performed any nonaudit service for the period to be covered by the audit?		
Independence Statement		
I have read and understand GAGAS 3.02 through 3.58 and applicable Audit Handbook Chapters		
<input type="checkbox"/>	I am independent in mind and appearance according to GAGAS Conceptual Framework Approach to Independence in GAGAS 3.07. I will notify this project's Audit Manager and my supervisor immediately if I become aware of the potential existence of any actual or perceived personal or external threats on my part or a coworker's part between the date I signed this statement and the issuance of the final report.	
<input type="checkbox"/>	I believe I cannot be independent or impartial on the assignment due to the following potential threats:	
Auditor Signature		
<input type="checkbox"/>	I have reviewed this certification and I agree that it appears that no threat(s) to independence exist.	
<input type="checkbox"/>	I have reviewed the above potential threat(s) to independence and have taken the following actions to mitigate or eliminate the threat to an acceptable level (attach continuation sheet if necessary):	
Supervisor		

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2

Director, National Geospatial-Intelligence Agency Comments (cont'd)



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Auditor Statement of Independence

***Only complete this section if threat to independence occurred during the performance of the project.**

Auditor	
<input type="checkbox"/>	A potential threat(s) occurred/arose during the performance of the project. The potential threat(s) were discussed with the Supervisor and is detailed below (attach continuation sheet if necessary):
Auditor Signature	
Supervisor	
<input type="checkbox"/>	I have reviewed the above potential threat to independence and have taken the following action (attach continuation sheet if necessary):
Supervisor	

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Director, Missile Defense Agency Comments



DEPARTMENT OF DEFENSE
MISSILE DEFENSE AGENCY
5700 18TH STREET
FORT BELVOIR, VIRGINIA 22060-5573

MAR 31 2014

Mr. Randolph R. Stone
Department of Defense Inspector General
Deputy Inspector General
Policy and Oversight
4800 Mark Center Drive
Alexandria, Virginia 22350-1500

Dear Mr. Stone:

The Missile Defense Agency (MDA) appreciates the opportunity to review and comment on DoD IG Draft Report, "Implementation of 2011 Generally Accepted Government Auditing Standards Independence Standards at the DoD Audit Organizations," dated March 7, 2014 (Project No. D2013-DAPOIA-0011.001).

The MDA has no technical comments and concurs with recommendations A.3 and B.1 in the draft report. The attached comments address how we are complying with these recommendations.

[REDACTED]

Sincerely,

J.D. SYRING
Vice Admiral, USN
Director

Enclosures:
As stated

[REDACTED]

Director, Missile Defense Agency Comments (cont'd)

**DODIG Project No. D2013-DAP0IA-0011.001 - Implementation of 2011
GAGAS Independence Standards at the DoD Audit Organizations
DRAFT REPORT
March 7, 2014**

Missile Defense Agency Response to DoD IG Recommendations

RECOMMENDATIONS

Recommendation A3:

The DoD IG recommends that the Director, Missile Defense Agency, and the Director and Chief Executive Officer, Army and Air Force Exchange Service, ensure that their audit organizations create internal policies and procedures detailing how nonaudit service requests will be assessed and documented for potential impairments to independence.

MDA Response to Recommendation A3: Concur.

MDA is updating policies and procedures for assessing and documenting potential impairments to independence of nonaudit services. The policy update addresses receiving and documenting requests for nonaudit services and assessing threats to independence. MDA Instruction 7600.05-INS, "Internal Review Policies and Procedures," is in the review cycle and approval estimated by 4th quarter 2014.

Recommendation B1:

The DoD IG recommends that the Auditor General, Department of the Army; the Director, Missile Defense Agency; the Director and Chief Executive Officer, Army and Air Force Exchange Service; and the Chief Executive Officer, Navy Exchange Service Command, ensure their audit organizations perform all the required independence analysis and document the results before accepting a nonaudit service.

MDA Response to Recommendation B1: Concur.

Updates to the MDA Instruction 7600.05-INS, "Internal Review Policies and Procedures," require the performance, and documentation, of independent analysis for all nonaudit service requests. The update requires evaluating and documenting skills, knowledge, or experience, of management-appointed individuals overseeing the nonaudit service. The update to the Instruction is in the review cycle and approval estimated by 4th quarter 2014.

Commander, United States Special Operations Command Comments



UNITED STATES SPECIAL OPERATIONS COMMAND
OFFICE OF THE COMMANDER
7701 TAMPA POINT BOULEVARD
MACDILL AIR FORCE BASE, FLORIDA 33621-5323


21 March 2014

MEMORANDUM FOR DEPARTMENT OF DEFENSE OFFICE OF THE INSPECTOR
GENERAL, 4800 MARK CENTER DRIVE, ALEXANDRIA, VA 22350-1500

SUBJECT: Audit of Implementation of 2011 Generally Accepted Government Auditing
Standards Independence Standards at the DoD Audit Organizations (Project No.
D2013-DAPOIA-0011.001)

1. This memorandum responds to subject audit report dated 7 March 2014. We concur with recommendation A.1. On 17 April 2013 we took action to close this recommendation. We issued a new internal audit policy implementing the December 2011 Generally Accepted Government Auditing Standards Independence Standards. In addition, this policy is included in our updated Standard Operating Procedure dated 27 June 2013.

[REDACTED]


WILLIAM H. McRAVEN
Admiral, U.S. Navy
Commander

Director and Chief Executive Officer, Army and Air Force Exchange Service Comments



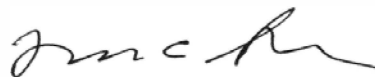
31 March 2014

FROM: Director and Chief Executive Officer, Army & Air Force Exchange Service

TO: Department of Defense Inspector General, Deputy Inspector General for Policy and Oversight

SUBJECT: Management Response, Implementation of 2011 Generally Accepted Government Auditing Standards Independence Standards at the DoD Audit Organizations, Project No. D2013-DAPOIA-0011.001

1. We concur with the findings and recommendations. Noted below are our management responses:
 - a. Recommendation A.3 Concur. The AAFES Audit Division established internal policies and procedures detailing how nonaudit service requests will be assessed and documented for potential impairments to independence. Completion date was 31 December 2013.
 - b. Recommendation B.1 Concur. The AAFES Audit Division established internal policies and procedures to ensure the audit organization performs all the required independence analysis and documents the results before accepting a nonaudit service. Completion date was 31 December 2013.
2. Thank you for your team's assistance in identifying the procedures required and suggestions for complying with the requirements for providing nonaudit services in accordance with generally accepted government auditing standards.



THOMAS C. SHULL
Director/CEO

Commander, Naval Supply Systems Command Comments



DEPARTMENT OF THE NAVY
NAVAL SUPPLY SYSTEMS COMMAND
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Ser NOIG/017

APR 10 2014

From: Commander, Naval Supply Systems Command (NAVSUP)
To: Deputy Inspector General, Policy and Oversight,
Department of Defense Inspector General

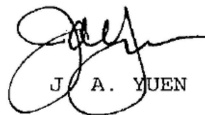
Subj: DODIG DRAFT AUDIT REPORT ON IMPLEMENTATION OF 2011
GENERALLY ACCEPTED GOVERNMENT AUDITING STANDARDS
INDEPENDENCE STANDARDS AT THE DOD AUDIT ORGANIZATIONS
(D2013-DAPDIA-0011.001)

Ref: (a) DoDIG Draft Audit Report (D2013-DAPDIA-0011.001)

Encl: (1) NAVSUP comments on subject Draft Audit Report

1. Per reference (a), enclosure (1) provides our comments on
the Audit Results and Recommendations A.1, B.1, B.2 and B.3.

2. For any questions, please contact [REDACTED]
[REDACTED]


J. A. YUEN

Copy to:
NAVINGEN

Visit the NAVSUP Home Page at www.navsup.navy.mil

Commander, Naval Supply Systems Command Comments (cont'd)

DEPARTMENT OF DEFENSE INSPECTOR GENERAL (DODIG) DRAFT REPORT,
"Implementation of 2011 Generally Accepted Government Auditing
Standards Independence Standards at the DoD Audit Organizations"
(Project No. D2013-DAPOIA-0011.001) of 7 March 2014

Recommendation A.1: We recommend that the Commander, United States Special Operations Command, and the Chief Executive Officer, Navy Exchange Service Command, ensure their audit organizations create internal policies implementing the December 2011 generally accepted government auditing standards independence standards.

NAVSUP Response: Concur. NEXCOM Office of Internal Audit (OIA) has implemented the 2011 Generally Accepted Government Auditing Standards (GAGAS). We will ensure annually that NEXCOM's internal policies and procedures specifically reference the most current version of the Yellow Book, currently the 2011 Yellow Book. NEXCOM OIA recognizes Yellow Book as the overarching guidance and NEXCOM's Procedural Manual is general in nature by design, while referencing Yellow Book as the primary guidance.

Recommendation B.1: We recommend that the Auditor General, Department of the Army; the Director, Missile Defense Agency; the Director and Chief Executive Officer, Army and Air Force Exchange Service; and the Chief Executive Officer, Navy Exchange Service Command, ensure their audit organizations perform all the required independence analysis and document the results before accepting a nonaudit service.

NAVSUP Response: Concur. If and when OIA takes on a nonaudit service engagement, the proper documentation will be prepared in accordance with GAGAS. However, in point of fact, OIA did not undertake any nonaudit services during the period reviewed and does not concur that control self-assessments and continuous auditing are nonaudit services. Discussions with Government Accountability Office auditors confirm our position that control self-assessments and continuous auditing are not considered to be non-audit services. OIA uses continuous audit and Control Assessment data to facilitate its traditional audits. Both are tools sanctioned by the Institute of Internal Auditors and comply fully with GAGAS standard 3.31 which states, "Certain

Enclosure (1)

Commander, Naval Supply Systems Command Comments (cont'd)

entities employ auditors to work for entity management. These auditors may be subject to administrative direction from persons involved in entity management process. Such audit organizations are internal audit functions and are encouraged to use the Institute of Internal Auditors (IIA) International Standards for the Professional Practice of Internal Auditing, in conjunction with GAGAS."

In addition, GAGAS 3.40 states "Routine activities performed by auditors that relate directly to the performance of an audit (i.e. current, future or past), such as providing advice and responding to questions as part of an audit, are not considered nonaudit services under GAGAS. Such routine activities generally involve providing advice or assistance to the entity on an informal basis as part of an audit. Routine activities typically are insignificant in terms of time incurred or resources expended and generally do not result in a specific project or engagement or in the auditors producing a formal report or other formal work product."

Recommendation B.2: We recommend that the Chief Executive Officer, Navy Exchange Service Command, ensure that his audit organization revise its internal audit policies to include procedures for performing control self-assessments and continuous auditing.

NAVSUP Response: Non-concur. Control self-assessments and continuous auditing are not nonaudit services, rather they are conducted in compliance with GAGAS 3.31 and 3.40. Therefore, a revision to OIA's internal procedures to define these as nonaudit services would be inaccurate. We will, however, ensure that OIA's procedural manual outlines general procedures both for providing routine internal control advice to NEXCOM's management and for the conduct of nonaudit services.

Recommendation B.3: We recommend that the Chief Executive Officer, Navy Exchange Service Command, remove the language from "The Navy Non-Appropriated Fund Purchase Card Program - Internal Operating Procedure, Revision Date: 12/8/2009 (edited 10/2012)" that appears to direct the functions of the Office of Internal Audit.

Commander, Naval Supply Systems Command Comments (cont'd)

NAVSUP Response: Non-concur. Organizationally, OIA's independence is safeguarded by reporting directly to the Chief Executive Officer and to the NEXCOM/Morale Welfare Recreation audit committee. To mitigate risk of personal impairment, each auditor signs a personal impairment statement on each audit engagement attesting to independence. The language noted in the Non-Appropriated Fund Purchase Card Program - Internal Operating Procedure manual was prepared by OIA and describes its role for conducting Government Purchase Card (GPC) audits and does not violate GAGAS, and can be viewed as an additional safeguard that clearly delineates OIA's role for performing GPC audits only. According to GAGAS 3.31, "Certain entities employ auditors to work for entity management. These auditors may be subject to administrative direction from persons involved in the entity management process. Such audit organizations are internal audit functions and are encouraged to use the Institute of Internal Auditors (IIA) International Standards for the Professional Practice of Internal Auditing, in conjunction with GAGAS."

Acronyms and Abbreviations

AAA	Army Audit Agency
AAFES IR	Army and Air Force Exchange Service Internal Review
AFAA	Air Force Audit Agency
ARMY IR	U.S. Army Internal Review
CONUS	Continental United States
CSA	Control Self-Assessment
DCAA	Defense Contract Audit Agency
DCMA IR	Defense Contract Management Agency Internal Review
DeCA IA	Defense Commissary Agency Internal Audit
DFAS IR	Defense Finance and Accounting Service Internal Review
DIA OIG	Defense Intelligence Agency Office of Inspector General
DISA IR	Defense Information Systems Agency Internal Review
DLA IR	Defense Logistics Agency Internal Review
DoD OIG	Department of Defense Office of Inspector General
GAGAS	Generally Accepted Government Auditing Standards
GAO	Government Accountability Office
GPC	Government Purchase Card
IG	Inspector General
MCNAFAS	Marine Corps Nonappropriated Funds Audit Service
MDA IR	Missile Defense Agency Internal Review
NAS	Naval Audit Service
NEXCOM IA	Naval Exchange Service Command Internal Audit
NEXCOM OIA	Naval Exchange Service Command Office of Internal Audit
NGA OIG	National Geospatial-Intelligence Agency Office of Inspector General
NGB IR	National Guard Bureau Internal Review
NRO OIG	National Reconnaissance Organization Office of Inspector General
NSA OIG	National Security Agency Office of Inspector General
OCONUS	Outside Continental United States
OIG	Office of Inspector General
USSOCOM OIG	U.S. Special Operations Command Office of Inspector General



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U.S. DEPARTMENT OF DEFENSE

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