



DEPARTMENT OF THE ARMY
OFFICE OF THE ASSISTANT SECRETARY
MANPOWER AND RESERVE AFFAIRS
111 ARMY PENTAGON
WASHINGTON, DC 20310-0111

March 31, 2003

MEMORANDUM FOR THE AUDITOR GENERAL

SUBJECT: The Auditor General, Army Audit Agency, and Internal Review
Exemption

Reference memoranda, U.S. Army Audit Agency, 15 January and 7 February 2003 and The Auditor General Briefing on 18 March 2003 to the Assistant Secretary of the Army (Manpower and Reserve Affairs).

Function. This decision includes civilian employees performing internal audit services for all levels and functions throughout the Department of the Army (DA); approves contracts for all audits; implements audit standards; coordinates and consults throughout the federal auditing community; coordinates Army internal review; and generally oversees the Army audit function. In addition, this decision includes the internal review function. (A decision is pending on whether internal review becomes a function of the Auditor General, as opposed to the local commander.) Audits fall into two categories—financial/compliance and economy and efficiency/program results (performance) audits:

- **Financial/Compliance Audits.** Financial auditing usually relates to attesting on a firm's financial statements. Compliance audits involve examining, reviewing, or performing agreed upon procedures on a subject matter or an assertion about a subject matter and reporting on the results. Financial and compliance audits are based on well established criteria that result in a favorable or adverse opinion that the financial statements either are presented fairly or not and the organization either complied with applicable laws and regulations or it did not.
- **Economy and Efficiency/Program Results (Performance) Audits.** Economy and efficiency/program results audits (both are referred to as performance audits) are directed towards reviewing specific operations to determine if the objectives are being achieved and if performance can be improved. Performance audits result in conclusions and recommendations that Army managers are required to reply to—stating if they agree or disagree and when they will take action on the recommendations. If the auditors and command cannot agree on the recommendations, the adjudication is raised—up to the Secretary of the Army level to establish the official Army position on the recommendations and the audit report. For recommendations that the Army

agrees with, Army auditors follow up to make sure the recommendations were implemented and fixed the cited problem.

Decision. The auditing function is not a core war-fighting competency of the Army as defined in Army Field Manual 1. However, it is required by Title 10, U.S. Code, Section 3014 requires the Secretary of the Army to establish a single office within the office of the Secretary of the Army to conduct the audit function; therefore, it cannot be divested or transferred to another agency. The audit function is not inherently Governmental. However, performance audits are functions of The Auditor General as an extension of the oversight responsibilities of the Secretary of the Army in Title 10. Congress mandated by statute that the Secretary of the Army has an auditing function. The Army Audit Agency is the Secretary's independent means to execute his fiduciary and statutory responsibilities to ensure public resources are used efficiently, effectively and legally. (This decision on performance audits applies to internal review if it becomes a function of The Auditor General. If Internal Review is not merged, it would be reviewable only if a whole base study is performed. Until either of these actions occur, Internal Review positions currently coded as reviewable will be recoded as Code X (Candidate for Alternatives to A-76). Accordingly, implementation plans for competing financial audits are required (comprising 10 percent of the audit function), but performance audits are exempted from competition (comprising 90 percent of the audit function). Alternatives to A-76 that are consistent with the rationale of this holding will be explored by The Auditor General in conjunction with my staff for the performance audit function. The Auditor General will deem if an alternative to A-76 merits further consideration and will provide me a briefing on his conclusion. If alternatives to A-76 are deemed not viable, the FAIR Act coding for the performance audit function will change from Code X (Candidate for Alternatives to A-76) to Code M (Restricted by DOD Management Decision). If an Alternative to A-76 is accepted, enabling legislation will be required to implement that Alternative.

Requestors Positions on Issues. The Chief Counsel of the Army Audit Agency's Office of Counsel opined that, due to the statutory requirement set forth in 10 U.S. Code, Section 3014 and Executive Branch policy, performance of the audit function is inherently Governmental while conceding that 50 civilians performing other various (e.g., financial) audit functions are reviewable and should remain so coded, also based on legal analysis. The Auditor General offered as an alternative position that 510 of the 560 auditor positions be exempt from review based on the invisible relationship that exists between the Secretary, the auditing function and the Army Audit Agency.

Standard of Review. The senior HQDA functional official for a function must describe and substantiate specifically how preparation and implementation of a Third Wave implementation plan for each course of action poses substantial and specific risks to a core war-fighting mission of the Army (i.e., a core competency) or violates a

statutory requirement affecting a function. The following are the risk factors to evaluate this request: force management risk; operational risk; future challenges; and institutional risk. How these risk criteria are applied may vary based on each course of action evaluated (i.e., A-76; alternatives to A-76; military conversions; transfer to another agency; divestiture). Therefore, exemption requests and decisions must assess the potentially adverse impact of each course of action.

Core Competency Relevant to Risk Issue. The auditing function is not one of the six recognized core competencies of the Army, as provided for in Army Field Manual 1 and The Army Plan: Shape the Security Environment (Deter Forward); Prompt Response; Forcible Entry Operations; Mobilize the Army; Sustained Land Dominance; or Support Civil Authority. Therefore, there is no force management risk (i.e., career progression issue) or operational risk associated with divesting this function.

Statutory Requirement Relevant to Divestiture Issue. Title 10, U.S. Code, Section 3014 requires the Secretary of the Army to establish an auditing office, therefore; the auditing function cannot be divested or transferred to another agency. However, the size of the auditing office is not specified by statute, and is subject to overall management headquarters constraints in competition with other management headquarters functions. Performance audits are functions of the Auditor General as an extension of the oversight responsibilities of the Secretary of the Army in Title 10.

Inherently Governmental Relevant to Outsourcing Issue. An inherently governmental function includes those activities that require either the exercise of substantial discretion in applying Government authority or the making of value judgments in making decisions for the Government. An inherently governmental function is so intimately related to the public interest as to require performance by Federal Government employees; it does not include providing advice to Federal Government officials. The FAIR Act statutory definition of inherently governmental, analysis and advisory (to include auditing and internal review) functions are normally not inherently governmental.

Although the functions included in Appendix B of the Office of Federal Procurement Policy Letter 92-1 are ordinarily not inherently governmental, the level of contractual support in specific circumstances may approach being inherently Governmental because of the way in which the contractor performs the contract or the manner in which the government administers the contract. The current exemption requests have not been substantiated or have made the case that current levels of contractual support are approaching a level that would risk the independent

decision-making of Army principal officials.

It is acknowledged that audit recommendations are distinct from other types of advice in that there is a formal Army process requiring a decision maker presented with audit recommendations to agree or disagree, and to further justify his or her disagreement to the Secretary of the Army. However, the decision maker still makes the decision that binds the Government, not the auditors.

Statutes Relevant to Sourcing Decision. Apart from the requirement for an audit office, auditing functions are subject to the normal process provided by Section 2461, Title 10 and Section 8014 of appropriations acts mandating public-private competition in certain circumstances, subject to the standard exceptions for 10 or fewer civilian employees, and preferential procurement programs.

Personal Services. Where supervision by an official required by statute in a management headquarters is required for effective performance of an activity in support of that official, there may be a basis for exempting that activity to avoid an inappropriate personal services contract provided no mitigation is possible.

Conflicts of Interest. No conflict of interest issues have been substantiated in referenced exemption request. Any alleged conflict of interest can be avoided through appropriate safeguards in the administration of the contracted work.

Military Conversions. Internal Review activities have a small percentage of military auditors. Many of these are in the National Guard and Reserves and are part-time. There is no statutory requirement for military auditors.



Reginald J. Brown
Assistant Secretary of the Army
(Manpower and Reserve Affairs)

Enclosure

CODING RULES for Internal Review/AAA

1. The Auditor General
 2. Other audit and internal review personnel includes:
 - Office of the Auditor General (except TAG)
 - US Army Audit Agency
 - Civilians in GS-511 (Auditor) occupational series
 1. 90 % of the above personnel
 2. 10% of the above personnel

(specific billets TBD by AAA)
- Code L -- Protected by law, statute, treaty or agreement
- Code X -- Candidates for alternatives to A-76
- Code R -- Subject to Review