CHAPTER 8

INTERNAL CONTROL REVIEWS

0801 GENERAL

080101. Purpose. This chapter provides detailed guidance on the National Aeronautics and Space Administration's (NASA) financial management internal control program policies, procedures, and responsibilities within the Agency related to conducting financial management internal control reviews and identifying and monitoring recommended corrective action plans (CAP) as a result of the review. This process supports the internal control process developed by the Office of Quality Assurance (OQA) in compliance with Office of Management and Budget (OMB) Circular A-123 "Management's Responsibility for Internal Control" (revised 12/21/04) and Government Accountability Office (GAO) internal control standards.

080102. Internal controls. Internal controls are safeguards built into a process or work-flow that provides a degree of assurance that resources are being used as intended to achieve the best results at the lowest possible cost. Controls may also highlight variances after an activity has been completed (e.g., methods used to detect errors in payroll processing). Such safeguards exist in all organizations or functional entities whether or not they are recognized as internal controls. Controls should not be considered additional work that is imposed on activities from a higher organizational level. Instead they should be viewed as safeguards that are embedded in normal activities. Controls are developed and put in place by managers and employees within each activity. When managers or employees take action to assure that activities will proceed, are proceeding, or have proceeded as planned, controls are at work. The formal identification of these safeguards, determination of whether the controls are actually used, and an evaluation of their adequacy are major goals of an internal control review.

080103. Reviews. An internal control review (ICR) is an in-depth examination of management controls that exist within an activity. The review may focus on either administrative, financial, or program activities. ICRs examine significant control weaknesses, activities with high inherent risk, or other areas of concern to management. The results of the ICRs should be used by managers as a tool to improve the management process within the organization, or to provide a level of confidence that controls are in place and operating effectively.

080104. Internal control review benefits. ICRs provide a variety of benefits which promote sound management.

A. ICRs assure that administrative, financial, and programmatic risks have been adequately addressed.

B. If control gaps or weaknesses exist, the ICR identifies the weakness and recommends action to correct the problem(s) and establish the optimum control system within existing operational and resource restrictions.

C. Excess controls that may have accumulated over the years may be identified and eliminated, allowing a more efficient operation.

D. Since the ICR process forces managers to consider risks in relation to the cost of instituting or maintaining management controls, operational risks that are not fully covered by controls will remain so because of a logical decision process rather than simple oversight.

E. Especially during this period of diminishing resources, the ICR helps managers reassess their control systems to establish the maximum level of control while reducing associated control costs.

F. After appropriate ICR recommendations have been implemented, the manager has a reasonable degree of confidence that his/her responsibilities are being carried out according to plan.

G. The process under review will be brought in line with GAO's "Standards for Internal Control in the Federal Government" through a formal, systematic approach to control.

H. Assist the Office of the Chief Financial Officer (CFO) and the Administrator comply with the requirements of the Federal Managers' Financial Integrity Act (FMFIA) and OMB Circular A-123, Revised.

I. Provide part of the necessary support for the CFO's annual assurance statement on financial management internal controls to the Administrator.

J. Contribute to the general management improvement in the OCFO and in NASA.

0802 REQUIREMENTS

080201. Responsibility. Financial management internal control reviews are performed by the OQA. OQA will be responsible for identifying the internal control review team for each review to be conducted. OQA will have primary responsibility for conducting the reviews, but may request review support from appropriate organizations, such as the Financial Management Internal Control (FMIC) point of contact or the assessable unit (AU) contact that is responsible for financial management internal controls for the area to be evaluated. Selection to participate on the review team will be based on the following criteria: (1) working knowledge of the area being reviewed, (2) subject matter expert, (3) expertise in planning and conducting studies or (4) other factors, as necessary. Review team members will participate in all aspects of the review.

080202. Review areas. OQA, in coordination with OCFO, Center CFOs, Mission Directorates, Mission Support Offices, the Competency Center, and the NASA Shared Services Center (NSSC) will select specific areas for which internal control reviews will be conducted. This selection will occur on an annual basis and OQA will develop a review plan for the year at the beginning of each fiscal year. Review selection will be based on prior internal control evaluation information, such as that identified when conducting risk assessments, activities with high inherent risk, or other areas of concern to management or the Office of Inspector General (OIG). The OQA will inform the OIG of the specific areas for which internal control reviews will be conducted.

080203. The internal control reviews will be conducted in compliance with NASA Policy Directive (NPD) 1210.2 NASA Surveys, Audits, and Reviews Policy. The following are key requirements OQA will follow to ensure standard and effective ICRs:

A. OQA must coordinate with the Director of Center Fiscal Operations and provide advanced written notification to the CFO office or Headquarter organization, FMIC point of contact, and AU contact planned for review thirty days prior to arrival to allow the office to make necessary arrangements for interviews, work space, and documentation preparation. In the notification memorandum, OQA will provide a clear and concise scope of what the review will be covering. If the review needs to be delayed for operational or other reasons, management needs to inform OQA at this time and provide alternate dates for the ICR.

B. A brief entrance conference must be held to meet/introduce the points of contact, discuss the scope of the review and relevant logistics, as well as any potential problems/issues. Financial management officials should take advantage of this opportunity to assure that they have a clear understanding of the ICR objectives. Management from the area being reviewed shall inform OQA of areas or activities needing special attention or any other pertinent information that would assist in planning the ICR.

C. Each assessable unit internal control contact should be available for a part of the review period to provide materials, discuss internal controls and findings, and direct reviewers to additional points of contact or sources for follow-up/discussion. Continual contact with points of contact is critical throughout the review. During the review, OQA will hold periodic meetings with officials of the areas being reviewed to discuss progress of the review and matters being developed. During these discussions, the area being reviewed shall express views on the review results and disclose any facts not previously known that could alter conclusions.

D. All documentation included in the scope of the review should be available to the OQA team in both electronic and paper format.

E. An exit conference should be held at the end of the ICR to debrief the assessable unit points of contact and present and discuss findings. This conference closes out the on-site review. In order to make these discussions effective, the appropriate senior management official shall encourage affected officials and personnel to openly and candidly discuss with OQA: review findings that fall within such officials' areas of responsibility; and those recommendations upon which such officials have the authority to act. These discussions of

review results help assure that ICR reports are factual and that conclusions and recommendations are sound and reasonable.

F. OQA must document all review findings and they must be fair and objective, based on the materials/review completed. A draft ICR report should be prepared and submitted to the CFO office, Headquarter organization, FMIC point of contact, and AU contact. In response to the draft report, the officials who have responsibility will be given the opportunity to submit written comments. The responsible financial management officials will respond to the draft report and specifically state concurrence or reasons for non-concurrence, and make other pertinent comments about the findings. After comments have been received, an ICR report will be issued, including the comments received.

G. OQA is responsible for following-up on all open ICR recommendations. Semiannually (March and September) a list of all open recommendations will be provided to each IC coordinator to request a status on the implementation of the recommendations. At the preference of the responsible office, a meeting may be requested or an e-mail response may be provided to update the status on the open recommendations. The final review process begins once all recommendations have been adequately addressed. At that point, OQA should prepare a memo to the CFO indicating that all recommendations have been adequately addressed. The memo should include a brief summary of how each of the recommendations was addressed. OQA, as part of its quality assurance process, will perform follow-up reviews to assure adequate implementation of recommendations.

0803 PROCESS

080301. Internal control review steps. An internal control review should consist of the following steps. All steps should be fully documented, per the requirements outlined in this volume.

A. Identifying the ICR focus and the Center(s)/office(s) involved. NASA's financial management community has been divided into discrete entities called assessable units (refer to Chapter 3, Establishing Assessable Units for further information). In many cases, the assessable units will not be the same as the review component's organizational breakdown. The assessable unit is the focus of evaluative work in the internal control process. ICRs should focus primarily on areas with known control problems or high inherent risk (activities which are more susceptible to problems because of the nature of their work). Much of the information used to select the ICR focus areas can be taken from the risk assessment and self assessment evaluations previously conducted.

B. Detailed planning of the ICR. After the review's focus is determined, OQA should prepare a detailed plan of the review, considering each step of the review separately, and developing a realistic time frame.

C. Investigating/reviewing background material. The team should outline the process or work flow for the internal control area being reviewed. This will help the ICR review

team identify controls that exist within that process. This phase will also provide an adequate basis to develop a flowchart of the process under review, the next step in the ICR process. The flowchart will serve as a stable point of reference when determining risks, control objectives, and control techniques.

D. Documenting the event cycle (narrative description/flowchart). To properly examine the system of controls that exists within the area being reviewed, the ICR team must use a stable point of reference. A narrative description of the work that takes place and a flowchart will provide a firm basis for a logical, structured examination of controls within the event cycle(s). These conceptual aids will assist the ICR team in evaluating all controls throughout the event cycle.

E. Analyzing the general control environment. The environment in which the process under review operates has a major impact on the effectiveness of its internal control system. Poor training or lack of adequate delegation of authority may negate the effectiveness of even the best control system. Therefore, an analysis of the control environment is an important phase of the internal control review.

F. Determining risks within the event cycle(s) selected. All financial, administrative and programmatic areas have some degree of risk. A statement of risk will be related to a negative event or situation that would occur if all or a part of the process under review was not carried out as planned. What could go wrong? This phase of the ICR should also include an evaluation of the impact of the risk. Who would be affected? What would be the magnitude? The ICR team needs to consider all risks, even to persons or situations outside the assessable unit. Each risk identified will describe an event or situation that the organization does not want to occur. The team should consult the risk assessment results and documentation to better understand the risks for the area under review.

G. Identifying control objectives. Simply stated, control objectives are the opposite of the risks that have been previously identified -- conditions that an agency does not want to occur. The control objectives developed in this phase of the ICR will be used as a point of reference to identify and evaluate control techniques.

H. Determining existing control techniques. Control techniques are the safeguards that management put in place to help assure that operations proceed according to plan and are protected from fraud, waste and abuse. Effective control techniques allow management to feel confident that their responsibilities are being carried out properly. The team should identify and document the control techniques that are in place for each control objective.

I. Testing internal control techniques. Once the internal control techniques have been identified, the team must determine whether each of these techniques is routinely used and whether it achieves the stated objectives. The team should use an appropriate test exercise to determine whether each control technique is being used.

J. Evaluating internal controls. After the specific control environment has been defined and the existing controls identified and their usage tested, the control system should

be evaluated. Even if the specific control environment is satisfactory and the control techniques currently in place are being used, the ICR team cannot necessarily conclude that the existing control system is adequate. The control system should be evaluated to make sure that the best system possible is in place, given existing resources, to counteract the existing risks.

K. Reporting on internal controls. The draft and final ICR report should be prepared in accordance with the procedures outlined in Section 080203 F of this chapter.