COLLABORATION SERIES

Successfully Implementing Cooperative Audit Resolution

AGA®

Intergovernmental Partnership

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SUCCESSFULLY IMPLEMENTING COOPERATIVE AUDIT RESOLUTION

A Playbook for Improving Programs and Reducing Improper Payments

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INTRODUCTION

This playbook outlines a proactive approach to implementing some of the broad policy reforms contained in the *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (*Uniform Guidance*). It illustrates how key provisions in the *Uniform Guidance* can be leveraged to create a continuous feedback loop for program improvement, not just for the federal government, but also for those who receive funds through federal awards. Specifically, it outlines a practical approach for building on the cooperative audit resolution provisions in the *Uniform Guidance* to expand oversight and address some of today's most persistent program problems, such as improper payments.

Issued by the U.S. Office of Management and Budget (OMB) in 2013, the *Uniform Guidance* is an expansive document that supersedes and streamlines eight previous OMB circulars. It articulates renewed federal goals to eliminate unnecessary or outdated requirements; improve performance and outcomes; increase accountability, integrity and transparency; improve communication and reduce improper payments. Among other things, it requires federal awarding agencies to use cooperative audit resolution, which was the focus of AGA's 2010 *Guide to Improving Program Performance and Accountability through Cooperative Audit Resolution and Oversight (CAROI Guide)*. (See **Appendix A** for the definition of cooperative audit resolution.)

Why CAROI?

For many years, the process of resolving single audits finding-by-finding was too often laden with frustration and distrust. The process was expensive to conduct and frequently ended in a legal process of appeals — only to have the same finding appear in the following year's audit, because the root or systemic cause was not addressed. The Cooperative Audit Resolution and Oversight Initiative (CAROI) was developed to refocus the audit resolution process to promote inclusion, cooperation, trust and sustained improvement. CAROI has been used successfully for more than 15 years with federal, state and local entities, and clearly demonstrates a proven track record of fixing complex problems while building strong and lasting relationships. The goals of CAROI are to:

- create and maintain a dialogue with the recipients of federal awards;
- resolve all audits cooperatively;
- improve (single) audits; and
- coordinate oversight (audits, monitoring and technical assistance activities) to improve program performance, and mitigate and reduce improper payments.

Why this Playbook?

The Cambridge Dictionary defines playbook as "a set of rules or suggestions that are considered to be suitable for a particular activity, industry or job." Most commonly used in the world of sports — especially in football — playbook simply means a notebook containing descriptions and diagrams of a team's plays. In this context, playbook refers to a collection of methods, tactics and resources designed to solve a problem or address a particular challenge or issue. The *Uniform Guidance* has presented us with a unique opportunity to address challenges in the area of audits, improper payments and internal controls in a variety of innovative and collaborative ways. AGA has collected many useful resources within this document to assist in this effort.

As with any playbook, users may opt to employ some, but not all, of the outlined plays. Aspects of some plays may be combined or modified; others may be excluded. This playbook is an extension of the *CAROI Guide* and is intended to be used as a supplemental tool. The reader is encouraged to consult both publications when embarking on a CAROI project.

The *CAROI Guide* addresses cooperative audit resolution ("CAR") in depth and also touches on the oversight initiative ("OI") of CAROI. This playbook expands upon the "OI" of CAROI by explaining how better oversight can be leveraged with other key provisions in the *Uniform Guidance* to establish a course for program improvement. And, while not all improper payments represent a loss to the government, this playbook also explains how the oversight can help establish a continuous feedback loop to reduce or mitigate improper payments.

CHAPTER 1

CONNECTING THE DOTS

When undertaking the oversight of programs funded by the American taxpayer, it is important to examine the extended federal enterprise, which encompasses federal agencies and non-federal entities, including states, local governments, tribal governments, educational institutions, nonprofits, and other organizations that receive, administer and account for federal funds. When the federal government makes an award to a non-federal entity, it may be exposed to risk when that entity takes actions, provides services or makes payments.

Improper payments are a case in point. The U.S. Government Accountability Office (GAO) reported that, government-wide, improper payment estimates totaled $124.7 billion in fiscal year (FY) 2014, which was an increase of approximately $19 billion from the prior year's estimate of $105.8 billion. From a non-federal perspective, the state-administered Medicaid program — with $17.5 billion in improper payments — ranked only behind Medicare Fee-for-Service and the Earned Income Tax Credit in improper payments.[1] Since the federal share for Medicaid has, on average, been 57 percent,[2] improper payments in this program, alone, pose a significant financial risk for the federal government. Other state- or locally-administered federal programs with high improper payments include Unemployment Insurance, the Supplemental Nutrition Assistance Program (formerly Food Stamps), the National School Lunch Program, Rental Housing Assistance Programs, School Breakfast and the Children's Health Insurance Program. Improper payments for these programs totaled more than $12 billion in FY 2014.[3]

> "From 2003 to 2014, the cumulative total of improper payments reported was close to $1 trillion."
>
> –U.S. Comptroller General Gene Dodaro

Legislation enacted by Congress in December 2015 to reauthorize the Elementary and Secondary Education Act (ESEA) is indicative of the interest in identifying trends and issues that may have repercussions across an entire enterprise. The 2015 legislation, reauthorized as the Every Student Succeeds Act (ESSA), was the first reauthorization of ESEA since the No Child Left Behind Act was passed 14 years ago. Section 9204 of the ESSA, which relates to *Accountability to Taxpayers through Monitoring and Oversight*, requires the secretary of the U.S. Department of Education to review and analyze the results of monitoring and compliance reviews, to understand trends and identify common issues. Data analytics, for example, may reveal trends or common issues that extend across multiple school districts. In addition to addressing the findings within an individual school district, it may be possible to provide an early warning to districts that have similar issues, but were unaware of them. By further requiring the secretary to "issue guidance to help grantees address these issues before the loss or misuse of taxpayer funding occurs," the legislation also recognizes that information obtained through monitoring and oversight can be used as part of a continuous feedback loop to reduce problems in the future.

Leveraging the *Uniform Guidance*

Federal awarding agencies incorporated the *Uniform Guidance* into regulations (2 CFR 200), which became effective December 26, 2014. Section 200.513, which applies to federal agencies' responsibilities, requires federal agencies use cooperative audit resolution with their recipients. According to a source at OMB, pass-through entities are encouraged to use cooperative audit resolution with their sub-recipients; however, they are not required to do so. Furthermore, although both pass-through entities and sub-recipients are required to comply with the audit requirements in the *Uniform Guidance*, Section 200.513 only directly addresses federal agencies' responsibilities.

While pass-through entities are not required to use cooperative audit resolution, sub-recipients may request it be used.

This playbook seeks to connect the dots among important — and related — requirements in the *Uniform Guidance* that pave the way for improving programs and reducing improper payments. These provisions relate to cooperative audit resolution, improper payments and internal controls. Cooperative audit resolution can be used to understand and address the underlying problems and internal control weaknesses that contribute to improper payments or poor program outcomes. Programs can then be improved and improper payments reduced by taking steps to address the weaknesses and problems identified through CAROI.

The interrelated provisions of the *Uniform Guidance* addressed in this playbook are:

- federal awarding agencies must use cooperative audit resolution mechanisms to improve federal program outcomes through better audit resolution, follow-up and corrective action;[4]
- Federal awarding agencies must provide the name of a single-audit-accountable official "responsible for ensuring that the agency fulfills all the requirements of *Section 200.513 Responsibilities* and effectively uses the single audit process to reduce improper payments and improve federal program outcomes;"[5] and
- non-federal entities must establish and maintain effective internal control over federal awards.[6]

Harnessing Cooperative Audit Resolution

The CAROI process is built on the premise that government programs improve when officials from all levels of government work together to resolve findings using coordinated, data-driven oversight practices. The "CAR" process was developed as a way to address long-standing audit issues. The "OI" component encompasses all aspects of agency oversight of grant programs, including audits, program monitoring, technical assistance, data collection and review activities.

CAROI does not change existing audit requirements; rather, it provides a principles-based foundation for audit resolution. CAROI's principles promote collaboration and trust, and stress program improvement and technical assistance rather than sanctions and litigation.

The CAROI principles, discussed in detail in the *CAROI Guide*, are:

- Facilitate the resolution of oversight findings.
- Improve communication.
- Foster collaboration.
- Promote trust.
- Develop understanding.
- Enhance performance.

While this playbook presents strategies and details of various implementation models for CAROI, the *CAROI Guide*, along with products developed by AGA's Intergovernmental Partnership, provide additional tools and strategies to enable federal, state and local partners to effect lasting, positive change in the implementation of joint programs. Some of the relevant AGA products include:

- *Making Better Decisions: Leveraging Government Resources in Challenging Financial Times*;
- *Blended and Braided Funding: A Guide for Policy Makers and Practitioners*;
- *Risk Assessment Monitoring Tool* and,
- the Fraud Prevention Toolkit.

All of these, and more, are available at: www.agacgfm.org/tools.

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Balancing Relief and Sanctions

The *Uniform Guidance* definition of cooperative audit resolution[7] outlines concepts key to successful implementation. The definition offers the federal government a blueprint for building a strong partnership with grantees. Federal agencies have the opportunity to offer not only encouragement, but also incentive for grantees to use the cooperative audit resolution and oversight process. The definition states CAROI is based upon:

- federal agencies offering appropriate relief for past noncompliance when audits show prompt corrective action has occurred;[8]
- a strong commitment by agency and non-federal-entity leadership to program integrity;
- federal agencies strengthening partnerships and working cooperatively with non-federal entities and their auditors; and non-federal entities and their auditors working cooperatively with federal agencies; and
- a focus on current conditions and corrective action going forward."[9]

As a result of cooperative audit resolution, grant recipients have the opportunity to focus on the most-critical issues affecting program performance and improper payments, and to begin designing and sustaining systems with stronger internal controls. Federal agencies have both an opportunity, and a directive, to work cooperatively with recipients, helping them understand the federal requirements that apply to their funding and the underlying causes of any noncompliance. This understanding will help non-federal entities develop and execute effective and sustainable corrective action plans.

While it is clear agencies can offer recipients appropriate relief, it is equally clear that continued failure to correct audit findings is unacceptable and will result in sanctions, as the definition of cooperative audit resolution also calls for: "Federal agency leadership sending a clear message

> While it is clear agencies can offer recipients appropriate relief, it is equally clear that continued failure to correct audit findings is unacceptable and will result in sanctions.

that continued failure to correct conditions identified by audits which are likely to cause improper payments, fraud, waste or abuse is unacceptable and will result in sanctions."[10]

What Happens if Fraud Is Detected?

During the CAROI process, the intentional misuse of funds (fraud), or red flags signaling fraud, may become evident. For assistance in identifying instances of fraud, AGA's free, online Fraud Prevention Toolkit helps users spot red flags by looking at:

- business processes, such as grants and program management;
- program areas, like human services; or
- fraud type, such as eligibility and credentialing schemes.

CAROI cannot be used in cases of fraud. If fraud, or the possibility of fraud, is revealed during the cooperative audit resolution process, make the required referrals to law enforcement. Section 200.113 of the *Uniform Guidance*, entitled Mandatory Disclosures, specifies:

> *The non-federal entity or applicant for a federal award must disclose, in a timely manner, in writing to the federal awarding agency or pass-through entity all violations of federal criminal law involving fraud, bribery, or gratuity violations potentially affecting the federal award. Failure to make required disclosures can result in any of remedies described in Section 200.338 Remedies for non-compliance, including suspension or debarment.*

Timely referrals to appropriate law enforcement agencies, and the federal awarding agency or pass-through entity, will help ensure that actions taken during cooperative audit resolution do not jeopardize a potential criminal proceeding. Consult the Office of Inspector General within any federal agency that provides funding, and ask who the appropriate law enforcement agencies are in a specific case.

Although CAROI cannot be used in addressing specific instances of fraud, CAROI techniques could be used to strengthen internal controls. In strengthening these internal controls, concrete steps would be taken to prevent improper payments and improve program performance.

Reducing Improper Payments

As previously mentioned, the *Uniform Guidance* requires that federal awarding agencies work with OMB to ensure the compliance supplement for single audits focuses the auditor's attention on requirements most likely to cause improper payments, fraud, waste and abuse (Section 200.513(c)(4)).

The federal website dealing with improper payments, PaymentAccuracy.gov, states improper payments occur when:

- funds go to the wrong recipient;
- the right recipient receives the incorrect amount of funds (including overpayments and underpayments);
- documentation is not available to support a payment; or
- the recipient uses funds in an improper manner.

Contrary to common perception, not all improper payments are fraud (i.e., an intentional misuse of funds). In fact, the vast majority of improper payments are due to unintentional errors.

Another prevalent misunderstanding is that all improper payments are a loss to the government, but that is not always the case. For example, although most of the $125 billion in improper payments in FY 2014 was caused by overpayments (payments that are higher than they should have been), a significant portion of that total amount was caused by underpayments (payments that are lower than they should have been). The difference between these two amounts (that is, overpayments minus underpayments) equals the net amount of payments that improperly went out the door.[11]

Strengthening Internal Controls

The *Uniform Guidance* repeatedly stresses the importance of implementing and monitoring internal controls. Internal controls, as defined by the *Uniform Guidance*, are processes, "implemented by a non-federal entity, designed to provide reasonable assurance regarding the achievement of objectives in the following categories:

a) effectiveness and efficiency of operations;

b) reliability of reporting for internal and external use; and

c) compliance with applicable laws and regulations."[12]

Section 200.303 of the *Uniform Guidance* specifically directs users to important guidance on internal control:

- "Standards for Internal Control in the Federal Government," known as the Green Book, issued by the comptroller general of the United States and
- the "Internal Control Integrated Framework," issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

COSO's Three Lines of Defense for Managers and Auditors

One framework that helps demonstrate this valuable relationship between management and auditors was defined by COSO, which is an initiative dedicated to providing thought leadership through the development of frameworks and guidance on enterprise risk management, internal control and fraud deterrence. In its publication, *Leveraging COSO Across the Three Lines of Defense*, COSO provided useful guidance that more clearly defines how audit and management functions can work together in a "three-way defense:"[16]

- Operational management lies with the program owners on the front line of achieving the mission — those whose activities create and/or manage the risks that can help or hinder successful delivery of programs. This includes taking the right risks at times when called for. The first line owns the risk along with the design and execution of the organization's methods of responding to those risks while carrying out the program.
- Internal monitoring is put in place to support management by bringing expertise (such as finance, information technology, security, human resources, legal, etc.) alongside the first line to assist program offices and help ensure that risk and controls are effectively managed. While separate from the first line of defense, the second line still shares the control, direction and coordination of senior management. The second line is essentially a management and/or oversight function that shares many aspects of the management of risk.
- Internal audit provides assurance to senior management and any oversight body that the first and second lines' efforts are consistent with the expectations of senior management. In order to maintain independence and protect its objectivity, the internal auditor typically does not perform management functions. Internal auditors usually report to the organization's ultimate oversight authority.[17]

Supplementary information in the *Uniform Guidance* further states, "The final guidance right-sizes the footprint of oversight and single audit requirements to strengthen oversight and focus audits where there is greatest risk of waste, fraud and abuse of taxpayer dollars. It improves transparency and accountability by making single audit reports available to the public online, and encourages federal agencies to take a more cooperative approach to audit resolution in order to more conclusively resolve underlying weaknesses in internal controls."

Similarly, the Institute of Internal Auditors (IIA) highlights the important role auditors can play in providing assurance that the internal controls are operating effectively. IIA research has shown "board directors and internal auditors agree that the two most important ways that internal auditing provides value to the organization are in providing objective assurance that the major business risks are being managed appropriately and providing assurance that the risk management and internal control framework is operating effectively."[13] The value of the relationship between management and auditors is further discussed in COSO's *Leveraging COSO Across the Three Lines of Defense* (see **sidebar**).

Employing Enterprise Risk Management

Because the federal government is a massive extended enterprise, it is unsurprising that Enterprise Risk Management (ERM) is becoming increasingly relevant for government managers.[14] ERM is a discipline that proactively addresses the full spectrum of an organization's risks, including challenges and opportunities, and integrates them into an enterprise-wide, strategically aligned portfolio. ERM has been a core principle of good corporate management in the private sector for many years.

There is an intersection between ERM and the principle-based culture of cooperative audit resolution and oversight: the principles contained in the *CAROI Guide* lift the conversation to a strategic and enterprise-wide level. Whereas the traditional audit resolution process all too often consisted of developing corrective actions on a finding-by-finding basis, CAROI looks at the whole picture of what the audit/oversight tells us. This enterprise-wide review helps identify patterns or the root cause of findings, which could include such items as substandard accounting, procurement or payroll systems, or a lack of or inadequate internal controls. Missing procedures manuals or not following those that exist, might also be root causes.

Including CAROI and its principles in organizational ERM structures can play a vital role in helping an organization assess current and future risks.

Including CAROI and its principles in organizational ERM structures can play a vital role in helping an organization assess current and future risks. ERM pulls all the risks together from various parts of the organization to make a portfolio view of risk available at the highest levels of leadership to help inform decision-making and support the achievement of an organization's mission, goals and objectives. "A good ERM framework recognizes that it is equally important to understand the internal controls related to key organizational risks and how internal controls are used to mitigate, treat, or reduce the level of exposure to risk."[15] ERM is not only a set of processes, but, most importantly, a culture that focuses the organization on mission achievement by solving problems that may get in the way or preventing them altogether.

CHAPTER 2

MAKING CAROI YOUR OWN

It is important to understand that cooperative audit resolution can be used in a variety of situations; its principles are applicable to any funding entity or recipient. The CAROI principles are not limited to the federal government. They can also be used when a state or local government is the primary source of funding and seeks to work with a sub-recipient(s) to make program improvements. Since AGA developed the *CAROI Guide* in 2010, the process has been used in a number of different circumstances and lessons continue to be learned. Experience continues to underscore the importance of making CAROI your own.

Flexibility is one of the major strengths of the CAROI approach. CAROI will look different from organization to organization, and sometimes from one activity to another within the same organization, depending on the need and the circumstances. Once an organization has embraced CAROI, it can develop an implementation approach that works within its organizational structure. The first steps are to review the implementation checklist and frequently asked questions in the *CAROI Guide*.

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Recent experience has helped identify three general approaches to CAROI implementation: simple CAROI, complex CAROI and self-initiated CAROI. There are no clear lines of demarcation dividing one approach from another. Some simple projects may only involve a shift in attitude. Other, more complicated projects, may benefit from the establishment of a Cooperative Audit Resolution Team (CART), as explained in the following section. In the same vein, projects that involve only a few, relatively simple findings might be initiated without extensive review of the findings; whereas larger projects with more complex findings may require a careful, deliberative analysis of the findings. The common elements across projects are a commitment to:

- the CAROI principles;
- identifying and addressing any underlying issues, not just the facts presented in the audit and oversight process; and
- exploring alternative, yet collaborative, solutions to persistent problems.

The three basic approaches to CAROI are:

1. Simple CAROI

Used in less-complicated situations, where findings do not cross multiple agencies or levels of government, where they do not reveal pervasive issues with program performance, and where protracted negotiation or litigation has not been employed. The approach may be as simple as adopting a new perspective on the audit resolution process and adding the CAROI principles to policies and procedures for audit resolution and follow-up. Rather than resolving findings in isolation, the audit resolution specialist consults with the auditee, program office representatives, the auditor, legal counsel and others, as necessary, to identify the root cause(s) of the finding(s) and to craft a solution/corrective action plan. It may not be necessary to create a CART in these situations. CAROI principles can and should be applied to all routine resolution activities, resulting in a common agreement, and understanding on behalf of all parties as to the cause of the problem and the proposed solution. Simple CAROI is not for audits with repeat findings, substantial questioned costs or findings that could significantly impact the entity's ability to administer programs.

Example of simple CAROI: An audit resolution specialist receives an audit that includes a finding in the area of unallowable expenditures with some questioned costs. After thoroughly reviewing the report, including the entity's proposed corrective action, the specialist contacts the grantee to determine the status of the corrective action(s), verify the facts as reported in the audit and discuss the circumstances that may have contributed to the finding. The specialist then consults with program office staff to verify that the expenditures cited in the report are, in fact, unallowable under program guidelines. The details of the corrective actions are then reviewed to ensure the proposed actions will adequately address the finding. The specialist then brings the program attorney into the conversation to discuss the questioned costs and, together, they determine the amount that can be sustained. Finally, the specialist contacts the grantee to discuss the decisions regarding resolution, which are written into a management decision.

2. Complex CAROI

As its name implies, involves the resolution of more complex findings. It may include recurring findings that span multiple programs and multiple years. Oversight findings may reveal pervasive problems with a program's performance, or it may reveal that protracted negotiations or litigation have already occurred. The issues/findings included in a complex CAROI project would be spelled out in a scope agreement. A CART, comprising both awarding and receiving entities, is likely to be needed.

Also, a scope agreement and a resolution agreement would be signed by the appropriate authorized officials. The *CAROI Guide* was developed with complex CAROI in mind. Organizations with responsibility for audit resolution should adopt formal policies and procedures for the complex CAROI approach.

> **Example of complex CAROI:** A state educational agency has had a series of audits with multiple, repeat findings and significant questioned costs. Prior efforts at resolution have not resulted in positive change over many years. In order to find a lasting solution to these problems, the federal awarding agency adopts a complex CAROI approach, involving a "multidisciplinary" team, with individuals with program, audit, oversight, fiscal and legal expertise to collaborate with the state agency. After agreement is reached on how the team would operate and the scope of the resolution effort, a scope agreement is signed. The next steps in the process involve face-to-face meetings with the entire CAROI team to understand the history of the findings and the circumstances that created or contributed to the persistent problems. The team discusses all options for remediation of the problems, the timelines and corrective action plan, and consequences for failure to execute the corrective action plan, before incorporating them into, and signing, the cooperative audit resolution agreement. Finally, the cooperative audit resolution agreement is signed by the appropriate, authorized officials.

3. Self-initiated CAROI

Involves a proactive approach intended to promote wide-spread, self-initiated program improvement by the recipients of funds. The process is initiated by the recipient of funds. The recipient develops a cooperative audit resolution plan that — subject to approval by the awarding entity — outlines its approach to resolving findings and improving program management. Because it is important to have broad stakeholder input, it is probably appropriate to include audit, fiscal, program and legal perspectives in the plan. The year after the agreement is signed, it is incumbent upon management in the entity receiving the funds to take the agreed-upon corrective actions and for the auditors, or other appropriate reviewers, to then follow up and verify that the actions were taken.

This approach allows an entity, which would ordinarily be subject to audit or review, to develop its own approach to resolving findings and improving program management. Responsibilities under this approach could be divided as follows:

- **The entity receiving funds would:**
  - adopt formal policies and procedures for the "self-initiated CAROI" approach;
  - design and establish a CART, if needed;
  - analyze the findings, along with any trends revealed, and determine appropriate corrective actions;
  - develop and submit a cooperative audit resolution agreement to the funding entity for approval;
  - execute the provisions of the agreement; and
  - provide information that enables the funding entity to review the agreement's execution.
- **The funding entity would:**
  - collaborate with other stakeholders;
  - approve the cooperative audit resolution agreement submitted by the entity receiving funds; and
  - verify that actions in the cooperative audit resolution agreement were executed within the specified timeframes.

> **Example of self-initiated CAROI:** The self-initiated approach is likely to be especially effective where an oversight entity has responsibility for a large number of recipient organizations. For example, according to the U.S. Department of Education's National Center for Education Statistics, more than 30 states have at least 150 school districts. If approved by the state, the school districts could proactively take responsibility for their own accountability and performance by implementing self-initiated CAROI. The school districts would not only analyze findings and develop a resolution agreement, they would also take steps to address the findings and then provide information needed by the state to verify that corrective action was taken. The ability for a recipient or a sub-recipient, like a school district, to proactively self-diagnose problems and offer solutions could have a decidedly positive impact on audit resolution and program improvement.

CHAPTER 3

PLAYS FOR IMPLEMENTING CAROI

This chapter of the playbook outlines recommended plays, or strategies, for those undertaking a CAROI project. Regardless of the approach used for CAROI, each party will likely execute some or all of the following plays. While the order in which the plays are presented will be appropriate for many CAROI projects, it may vary for others. Some plays may be taken independently by each party, like analyzing audit findings for a self-initiated process. Other plays, like formalizing the resolution agreement, require involvement or agreement by both parties. In considering these plays, it is important to note that, while they are based on concrete experience, each situation will differ. Playbook users will almost certainly add to, modify or eliminate some of these plays.

Analyze Audit and Oversight Findings

CAROI is not only a tool for resolving oversight findings and their underlying causes, but also for establishing program goals — at all levels of government — through the use of continuous monitoring analytic techniques and related technical assistance. For example, an analysis could include audit and oversight findings from reviews, single audits, and audits conducted by IGs and internal auditors for the fiscal year just ended or, depending upon the breadth of the project, multiple years. **Appendix 4** of the *CAROI Guide* displays a matrix that can be used in organizing audit findings.

If the project focuses on numerous findings, automation may help with the analysis. Data analytics may be useful in this process (**see sidebar**, A Promising Practice: *Data Analytics*). Data analytics can be especially helpful in sharing information among CAROI participants, and in analyzing trends across a specific grant program or the extended federal enterprise. It may help reveal a systematic breakdown resulting in findings across programs.

One promising practice has been the use of the federal government's MAX.gov site, which is a portal offering shared services as common solutions. Federal agencies are now able to invite non-federal entities to participate in MAX.gov, which offers tools to help with budget performance integration, data collection and tracking, document production, knowledge management and analytics (See **Appendix B**).

To conduct the analysis, determine whether there are: recurring findings; the same findings occurring in multiple agencies or levels of government; pervasive oversight findings with program performance; or protracted negotiations in which litigation has been initiated. Pay special attention to internal control weaknesses and the nature of any identified improper payments.

There will be a difference between initial follow-up on single audits versus other audits, such as federal reviews and federal audits. In the case of single audits, and perhaps IG audits, the auditee and appropriate federal agencies should conduct a preliminary analysis of audit findings to help determine the appropriate course of action. All parties should read through the audit, determine the nature and scope of the findings, and then determine whether a CART is needed. For federal program reviews and audits, the preliminary analysis may already have been completed.

A Promising Practice: *Data Analytics*

Using information from Form SF-SAC (Data Collection Form for Reporting on Audits of States, Local Governments and Nonprofit Organizations), the Federal Audit Clearing House (FAC) collects and disseminates information on single audits and selected associated audit reports. The FAC offers the ability to proactively identify high-risk recipients, as well as areas of emerging risk, thereby enhancing government planning and resource management. In relatively fast order, data analytics enables management to glance at data to determine high-risk recipients by:

- discerning common root causes for single audit findings;
- conducting trend analysis of these causes to identify distinct patterns; and
- developing with a certain degree of accuracy, a predictive capability to identify emerging risk.

The use of powerful data analytics techniques to uncover hidden patterns in large data sets will play an important role in reducing improper payments, and identifying and eliminating fraud, waste and abuse. Sharing data, knowledge and analytic tools can help governments identify the high-risk recipients of funds.

Data analytics can be especially valuable when CAROI teams are working with more than one audit or review. If, for example, the team is using information about several programs covered by multiple single audits, an inspector general's audit and a legislative auditor's office, data analytics could organize the findings into manageable categories across programs. Categories could include documentation errors, cash management problems, questionable wire transfers or unsupported journal entries. Each category could be assigned to a specific team for resolution, making data that was collected in each category valuable in analyzing trends across programs.

Determine the CAROI Approach that Is Most Appropriate

Determine whether simple CAROI, complex CAROI or self-initiated CAROI — as previously explained — is the right process for a given situation.

Establish the Cooperative Audit Resolution Team (CART), if Needed

Every audit and oversight initiative is different. The need for a CART — and its composition — depends on issues identified during audit or oversight, along with the abilities and needs of the recipient organization. A CART should include anyone from the awarding agency and the award recipient entity — who has a stake in the program(s) involved. Members of the CART should be at a level that enables them to speak for the agency. It is important to include representatives from all relevant disciplines, including program staff, the office of the general counsel, the independent auditor (auditor or inspector general) and the office of the chief financial officer. Also, make sure to specify CART members' responsibilities.

Remember that auditors can be an especially valuable resource to management in the audit resolution process. The *CAROI Guide* includes a section addressing the kinds of non-audit services that do not impair auditor independence.[18]

In some cases, findings can be successfully resolved if the recipient entity's management and staff simply adhere to existing policies and procedures. Simple CAROI may work fine without a CART. Complex cooperative audit resolution almost certainly needs a CART. A self-initiated CAROI project is also likely to need a CART, though it may not include as many members as for a complex CAROI approach.

CART activities are likely to include — but may not be limited to — developing and signing the scope and resolution agreements. Finally, a CART should conduct regularly-scheduled calls or meetings and develop a means for its members to communicate.

Formalize the Scope Agreement

The scope agreement covers issues that will be addressed during the CAROI process. It is a blueprint for the resolution of findings and a commitment on the part of all participants. If a CART has been established, the scope agreement should be signed by the CART members, otherwise it should be signed by the individual stakeholders involved in the CAROI process.

The scope agreement establishes the issues to be resolved, timeframes, the parties involved and their roles throughout the process.[19]

Execute the CAROI Process

This play involves bringing together individuals or the CART, depending upon the complexity of the situation. The goal of this play is to understand the findings, determine their underlying causes and agree on what should be done to address them.

Findings may be broken into categories, based on complexity or commonality, and workgroups may be established to deal with specific issues. It is entirely possible that initial expectations, as expressed in the scope agreement, may need to be modified as more is learned about the findings. This is likely to be one of the most challenging and time-consuming plays undertaken as part of the CAROI process. Collaboration among individual stakeholders on the CART is critical, and it is important for participants to begin with the end in mind: to realize that the goals of the process are to improve programs and reduce improper payments going forward.

During the execution process, it is important to determine the root causes of the performance-limiting factors or internal control weaknesses found during the audit or oversight process. Audit and oversight reports often address what was not done, but do not always explain performance-limiting factors that resulted in the finding. In carrying out the CAROI process, these questions should be asked:

- Were compliance requirements understood?
- Were policies, procedures and controls well-written?
- Were policies, procedures and controls circumvented, ignored or not understood?
- Is there a systemic problem, or was the problem caused by one individual or control weakness?
- What tone did management set regarding the importance of internal controls and other issues?
- Was personnel turnover a contributing factor?
- Was there intentional wrongdoing?
- Did federal, state or local oversight, or lack thereof, contribute to findings?
- Was there an opportunity to identify and fix the issue earlier?
- Would full disclosure of the issue, as soon as it was identified, have mitigated the extent or gravity of the issue?

Answering these questions will help identify and address the root causes of the findings, reduce the risk of findings being repeated, and mitigate or prevent improper payments.

Formalize Resolution Agreement

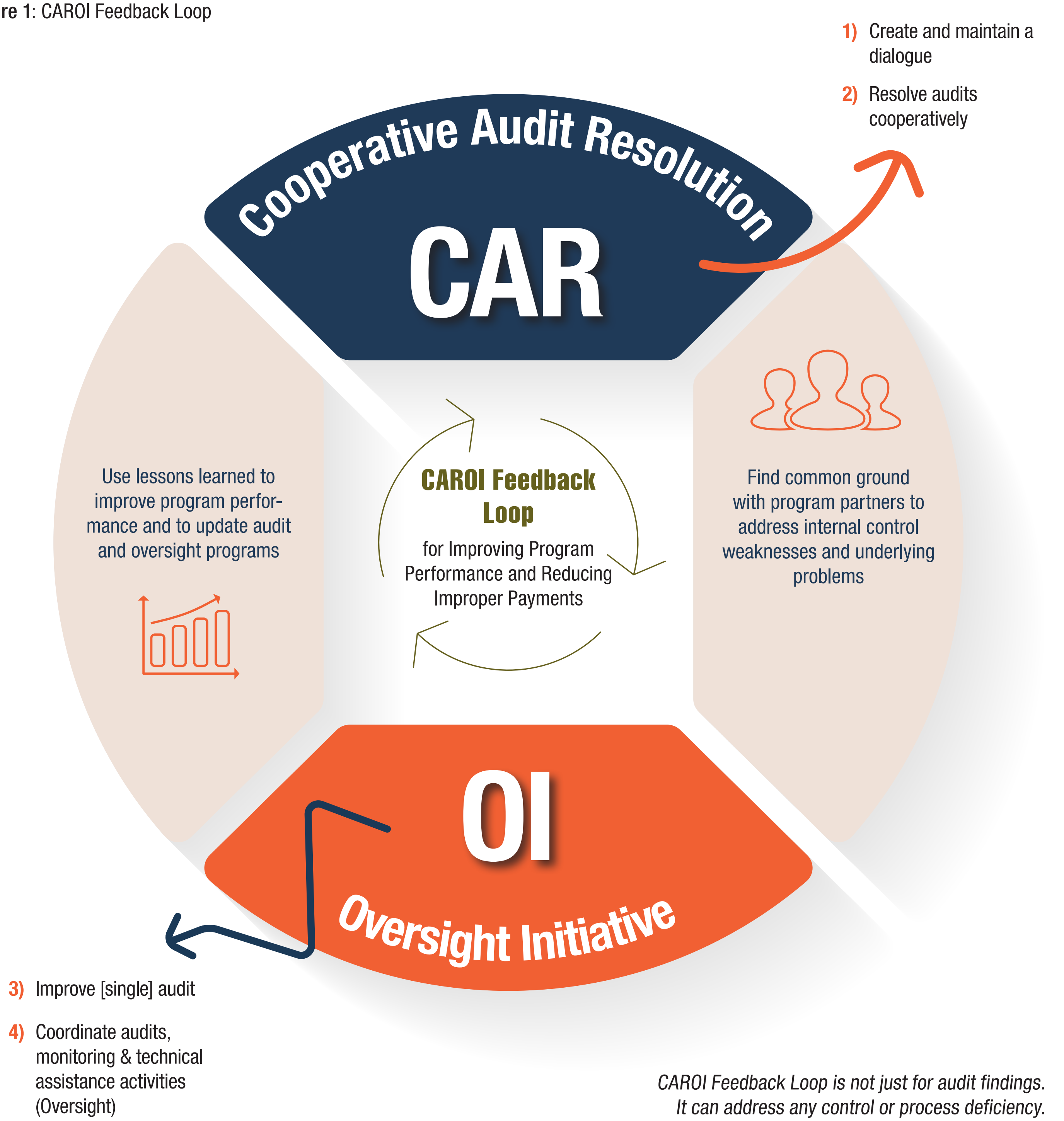
Like scope agreements, resolution agreements are a commitment on the part of all participants. They are developed based on lessons learned during the execution process, and outline how audit and oversight findings will be resolved. They are likely to address specific corrective actions that will be implemented, whether funds will be recovered, how follow-up will occur, how accountability is going to be measured and which personnel are going to be involved in the process. The agreement will also detail and discuss any finding that is no longer applicable, and explain why. In keeping with the definition of cooperative audit resolution in the *Uniform Guidance*, the agreement could also establish appropriate relief for past noncompliance when subsequent audits or reviews that prompt, corrective action has occurred or specify sanctions that will result if agreed-upon corrective action is not appropriately carried out.

As with the scope agreement, the cooperative audit resolution agreement should be signed by the appropriate, authorized officials.[20]

Establish a Continuous Feedback Loop for Program Improvement

It is important to use the audit and oversight process to establish a feedback loop (see **Figure 1**) for continuous program improvement. This involves:

Figure 1: CAROI Feedback Loop



CAROI Feedback Loop is not just for audit findings. It can address any control or process deficiency.

Following Up and Learning from Agreed-upon Corrective Actions

- Engage early (don't wait a year) in follow-up to verify corrections are being implemented as agreed upon in the resolution agreement.
- Assess the effectiveness of corrective actions early. The agreed-upon approach to resolving findings may have seemed like the correct one when signing the resolution agreement; however, actual practice may reveal weaknesses or limitations in the corrective actions that require

a course correction. It is best to learn early, rather than late, that controls are not working as intended so adjustments can be made.

- Report back on progress in strengthening internal controls and reducing improper payments. The entity or entities receiving funds could use a collaborative portal, like MAX.gov, to explain how new procedures or controls help avoid certain findings; or, they could post the next audit or review, explaining how findings have been corrected. Having this type of background information available can be valuable to future decision-makers, and can help avoid situations where new managers reverse previous corrective actions because they were unaware of the reasons for adopting corrective procedures or controls.

- Determine how to engage auditors or reviewers in the continuous improvement process. This might involve reviewing and testing the approved resolution agreement during subsequent audits or reviews to ensure implementation of planned internal control systems. This process could also provide more information to auditors and reviewers about both the receiving and awarding entities' expectations; and it could be part of tests already being conducted to follow up on prior years' findings.[21]

Updating Internal Control Plans and ERM Processes

Based on lessons learned during the resolution process, improper payments can likely be reduced if recipient entities update their internal control plans to reflect actions agreed upon in the resolution agreement. Internal control improvement should be shared with awarding entities.

Updating the Compliance Supplements

OMB and federal agencies can use audit resolution data to better target the compliance supplement. Section 200.513 of the *Uniform Guidance* specifically requires federal awarding agencies to provide OMB with annual updates to the compliance supplement. These updates to the compliance supplement should help focus auditor testing on requirements most likely to cause improper payments, fraud, waste or abuse. Continuous feedback means the supplement can be modified to address weaknesses or audit problems sooner than they may otherwise have been identified.

CONCLUSION

The *Uniform Guidance* provides a foundation for using cooperative audit resolution to improve program performance and reduce improper payments. This playbook connects the dots among various provisions within the *Uniform Guidance*. It focuses on how cooperative audit resolution offers a foundation for expanding the dialogue among those who award grants and those who receive them as a means of improving program outcomes and integrity.

This playbook is intended for those who obligate and oversee government funds. It was developed to provide a hands-on guide for leveraging the *Uniform Guidance* to create a continuous feedback loop for program improvement, not just for the federal government, but also for those who comprise the extended federal enterprise.

RESOURCES FOR LEVERAGING THE *UNIFORM GUIDANCE*

There are a number of resources to further leverage the *Uniform Guidance's* provisions related to internal control, cooperative audit resolution and improper payments, including:

Guide to Improving Program Performance and Accountability through Cooperative Audit Resolution and Oversight, AGA, Intergovernmental Partnership, May 2010

We Are Here to Help: External Auditor's Role, *Journal of Government Financial Management*, Geoffrey Frank and Rich Rasa, Summer 2014, AGA, p. 32.

Standards for Internal Control in the Federal Government, known as the Green Book, Government Accountability Office, GAO-14-704G, Sept. 10, 2014

Cooperative Audit Resolution and Oversight Initiative Pilot Program: Results in Brief, United States Equal Employment Opportunity Commission, Office of the Inspector General, Sept. 23, 2014

A Framework for Managing Fraud Risks in Federal Programs, Government Accountability Office, GAO-15-593SP, July 28, 2015

Fraud Prevention Toolkit, AGA, online tool

OMB Circular No. A-123, Management's Responsibility for Internal Control

APPENDIX A

Section 200.25 Cooperative audit resolution.

Cooperative audit resolution means the use of audit follow-up techniques that promote prompt corrective action by improving communication, fostering collaboration, promoting trust, and developing an understanding between the federal agency and the non-federal entity. This approach is based upon:

a) a strong commitment by federal agency and non-federal entity leadership to program integrity;

b) federal agencies strengthening partnerships and working cooperatively with non-federal entities and their auditors; and non-federal entities and their auditors working cooperatively with federal agencies;

c) a focus on current conditions and corrective action going forward;

d) federal agencies offering appropriate relief for past noncompliance when audits show prompt corrective action has occurred; and

e) federal agency leadership sending a clear message that continued failure to correct conditions identified by audits which are likely to cause improper payments, fraud, waste or abuse is unacceptable and will result in sanctions.

Section 200.26 Corrective action.

Corrective action means action taken by the auditee that:

a) corrects identified deficiencies;

b) produces recommended improvements; or

c) demonstrates that audit findings are either invalid or do not warrant auditee action.

Section 200.513 Responsibilities.

c) Federal awarding agency responsibilities. The federal awarding agency must perform the following for the federal awards it makes (See also the requirements of §200.210, “Information contained in a federal award”):

3) Follow-up on audit findings to ensure the recipient takes appropriate and timely corrective action. As part of audit follow-up, the federal awarding agency must:

(iii) Use cooperative audit resolution mechanisms (see §200.25 cooperative audit resolution) to improve federal program outcomes through better audit resolution, follow-up, and corrective action;

6) Provide OMB with the name of a key management single audit liaison who must:

(iv) Promote the federal awarding agency’s use of cooperative audit resolution mechanisms.

APPENDIX B

A Promising Practice: *Facilitating Communication and Collaboration Using MAX.gov*

MAX.gov is relevant to this playbook because it is already being used to promote key CAROI principles by managing communication and collaboration among federal and non-federal partners involved in the resolution of audit and oversight findings. Specifically, it is being used in an ambitious effort to resolve findings for state, local government and tribal federally funded programs.

MAX.gov offers an innovative suite of collaboration and knowledge-management tools that are connecting the federal government. With more than 165,000 users across all federal agencies, MAX.gov is a powerful and secure cloud-based platform used by federal agencies to collaborate and manage content and knowledge for thousands of projects.

Federal agencies are now sponsoring non-federal partners to assist with information collection and management, collaboration on programs and projects, paperless performance and financial reporting and more. MAX.gov promotes collaboration and accountability by providing a forum for all stakeholders to discuss and document follow-up on findings, including related follow-up work, and decisions on corrective actions and questioned costs, in a transparent environment.

Audit resolution for tribal governments is proving to be an area where such a collaborative tool can be very helpful. Tribes are relatively small governments, with small program, administrative and oversight staffs, with many varied and often complex federal programs. Tribal audits can contain cross-cutting findings that identify internal control weaknesses and compliance issues that potentially impact multiple federal programs across numerous agencies.

MAX.gov provides a forum for the cognizant, oversight or awarding agency to document and coordinate other audits and reviews by or for federal agencies with the single audit in an effort to avoid duplication of audits. It can be used for communication among tribal and federal officials, including management, auditors, reviewers, program officials and others with a stake in the programs being reviewed — all in one place, at one time, thus reducing the burden on the non-federal entity. With proper documentation of the audit resolution in MAX.gov, all participating federal agencies can rely on the cognizant or oversight agency, or perhaps one or more involved agencies, to resolve cross-cutting and agency-specific findings alike, thus allowing the federal government to make best use of limited resources.

The actual single audit findings, including criteria, conditions, causes, effects, questioned costs, other pertinent information, and auditor recommendations, can be included on a tribe's MAX.gov site to provide a starting point to:

- help determine existing performance-limiting factors (turnover, insufficient training, inadequate policies and procedures, weak controls, etc.)
- develop workable solutions to overcome the performance-limiting factors and achieve compliance (changes in hiring policies, develop or obtain training, review and update policies and procedures, etc.), and
- create and enact effective internal controls to provide internal as well as external assurances that, once gained, compliance can be sustained and program performance improved.

Once the resolution process is agreed to, MAX.gov can be used to demonstrate actual implementation of corrective action plans. For instance, where costs were questioned due to inadequate competition, MAX.gov processes and dashboards can be set up to ensure that the proper procurement steps are taken and documented. Further, MAX.gov pages can be restricted on a "need-to-know" basis for audit follow up, both internal and external to the non-federal entity. MAX.gov also functions as a dynamically-updated distribution list that is self-administered and managed.

MAX.gov has helped instill trust among the tribal CAROI partners, because it facilitates ongoing, non-intrusive oversight and communication. It also promotes transparency in a manner that permits the tribes to control the content on their page and use tools to manage their programs better.

Interactions among state, local, tribal, territorial, international and other non-government partners occurs within secure groups. MAX.gov is agile and cost-effective because it relies on reusable modular web services, open source, open standards and publicly-released, web-oriented applications that can automatically talk to each other. Tribes and others might find MAX to be useful in ongoing monitoring of their federally funded programs, even after findings are resolved.

Any federal agency interested in learning more about MAX.gov capabilities and pricing, including using MAX.gov to support their cooperative audit resolution process, can find more information by visiting MAX.gov or contacting MAX.gov support at MAXSupport@omb.eop.gov.

ENDNOTES

1. Paymentsaccuracy.gov.
2. Medicaid.gov and the Kaiser Family Foundation, Medicaid Financing: An Overview of the Federal Medicaid Matching Rate (FMAP), Sept. 30, 2012, available at http://kff.org/health-reform/issue-brief/medicaid-financing-an-overview-of-the-federal.
3. Paymentaccuracy.gov.
4. Uniform Guidance, Section 200.513 (c)(3)(iii).
5. *Uniform Guidance*, Section 200.513 (c)(5)(i).
6. *Uniform Guidance*, Section 200.303, Internal Controls.
7. *Uniform Guidance*, Section 200.25.
8. *Uniform Guidance*, Section 200.25 (d).
9. *Uniform Guidance*, Section 200.25.
10. *Uniform Guidance,* Section 200.25 (e).
11. Paymentsaccuracy.gov
12. *Uniform Guidance*, Section 200.61, Internal Controls.
13. The Value Agenda, Institute of Internal Auditors – UK and Ireland and Deloitte & Touche 2003
14. ERM is now addressed specifically in OMB Circular No. A-11 Preparation, Submission and Execution of the Budget and Circular No. A-123 Management's Responsibility for Internal Control. Since risk management practices should be taken into account when designing internal controls and assessing their effectiveness, ERM is key to implementing the internal control provisions of the *Uniform Guidance*.
15. Draft version, OMB Circular No. A-123, Management's Responsibility for Internal Control, p. 9.
16. *Leveraging COSO Across the Three Lines of Defense*; Douglas J. Anderson and Gina Eubanks; 2015
17. The role of Inspectors General can vary. However, for this specific discussion on the third line of defense, the Inspector General is viewed as being an internal auditor
18. See AGA's *CAROI Guide*, "The Role of the Independent Auditor in the CAROI Process," p. 9.
19. See pages 9 and 18 of AGA's *CAROI Guide*, which includes recommended provisions and a sample agreement.
20. More detail on resolution agreements is available in the *CAROI Guide* on pages 9 and 19.
21. The potential role for external auditors was addressed in an article on page 32 of the summer 2014 edition AGA's *Journal of Government Financial Management*, which focused on improper payments.

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