



**United States
Department of
Agriculture**

**Food Safety
and Inspection
Service**

**FSIS Directive
1090.2**

Audits of Management Controls

AUDITS OF MANAGEMENT CONTROLS

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UNITED STATES DEPARTMENT OF AGRICULTURE
FOOD SAFETY AND INSPECTION SERVICE
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AUDITS OF MANAGEMENT CONTROLS

PART ONE – GENERAL

I. PURPOSE

This directive describes the methodology that Office of Program Evaluation, Enforcement and Review (OPEER) auditors follow when planning and conducting audits of Agency management controls. The methodology meets the audit requirements of the Office of Management and Budget (OMB). OPEER conducts audits of FSIS management controls to ensure:

A. Programs achieve the Agency’s food safety and food defense mission in compliance with applicable laws and regulations.

B. Programs and use of resources comply with procedures to avoid waste, fraud, abuse, and mismanagement.

C. Reliable and timely information (**examples:** financial, managerial, and operational) is obtained, reported, and used for decisionmaking.

D. Controls are designed to prevent or promptly detect unauthorized acquisition, use, or disposition of assets.

E. Program risks are appropriately identified and managed through only management controls or management controls and performance measures.

II. (RESERVED)

III. (RESERVED)

IV. REFERENCES

9 CFR Part 500, Rules of Practice
Chief Financial Officer’s Act of 1990, as amended

DISTRIBUTION:
All Offices

OPI:
OPEER – Management Controls Branch

Clinger-Cohen Act of 1996 (formerly known as the Information Technology Management Reform Act)

Egg Products Inspection Act

Federal Financial Management Improvement Act of 1996

Federal Information Security Management Act of 2002

Federal Managers' Financial Integrity Act of 1982

Federal Meat Inspection Act

Government Performance and Results Act of 1993

Humane Methods of Slaughter Act

Improper Payments Information Act of 2002

Inspector General Act of 1978, as amended

Poultry Products Inspection Act

OMB Circular A-50, Audit Follow-up

OMB Circular A-123, Management's Responsibility for Internal Control

OMB Circular A-127, Management of Financial Management Systems

OMB Circular A-130, Management of Federal Information Resources

OMB Circular A-133, Single Audit Act of 1984

FSIS Directive 1090.1, Management Controls

FSIS Comprehensive Management Control System

USDA, Departmental Manual 1110-002, Management Control Manual

Committee of Sponsoring Organizations (of the Treadway Commission) {COSO} Internal Control – Integrated Framework, dated September 2007

U.S. Government Accountability Office, Government Auditing Standards

U.S. Government Accountability Office, Standards for Internal Control in the Federal Government

V. **ABBREVIATIONS AND FORMS**

The following appear in their shortened form in this directive:

AA	Assistant Administrator
COSO	Committee of Sponsoring Organizations (of the Treadway Commission)
FMFIA	Federal Managers' Financial Integrity Act of 1982
GAAP	Generally Accepted Accounting Principles
GAO	Government Accountability Office
ICS	Internal Control Staff, OPEER
LEARN	Laboratory Electronic Application for Results Notification
MCS	Management Control System
OIG	Office of the Inspector General
OMB	Office of Management and Budget
OPEER	Office of Program Evaluation, Enforcement and Review

VI. POLICY

It is FSIS policy that:

- A. Audits of management controls are conducted in accordance with the references in Part One, subparagraph IV.
- B. OPEER auditors with proper authorization and security clearances have full and unrestricted access to all personnel, facilities, records, reports, databases, documents, or other FSIS information and materials for accomplishing announced and unannounced management control audits.
- C. Indications of misconduct, fraud, or other criminal acts discovered during the management control audit process are referred to an appropriate investigative organization.
- D. Immediate notification will be given to senior program officials if OPEER auditors observe or have evidence that a condition indicating continued production and shipment of a product can pose an imminent threat to public health. (See the Federal Meat Inspection Act, the Poultry Products Inspection Act, the Egg Products Inspection Act, and the Rules of Practice (9 CFR Part 500).)

VII. DEFINITIONS

- A. **AssuranceNet.** A web-based application that supports the monitoring, analysis, and reporting of the Agency's MCS. The application allows supervisors and senior managers to identify where organizational performance is not meeting established performance measures, or where performance indicates a vulnerability to failure in achieving Agency objectives and mandates.
- B. **Audit.** An examination of an organization, system, or project to ascertain the validity and reliability of information to provide an assessment of a system's management controls.
- C. **Audit Plan.** A document that identifies the reasons for the audit, the audit objectives, methodology, and milestones.
- D. **Audit Findings.** The results of the auditors' data collection and analysis. Audit findings are linked to audit objectives and are developed in accordance with Government Auditing Standards. Negative findings may be linked to a recommendation to address the cause of a deficiency. Audit findings are classified as Green, Yellow, or Red using a system similar to that of the OMB, President's Management Agenda scorecard:
 - 1. Green – Program area has adequate documentation verifying that management controls and performance measures have been established, implemented and are adequate or effective.

2. Yellow – Program area has incomplete documentation verifying that management controls and performance measures have been established and implemented; or program area has documentation verifying that management controls and performance measures have been established and implemented, but documentation does not completely verify adequacy or effectiveness.

3. Red – Program area does not have documentation verifying that management controls and performance measures have been established and implemented, or the program area documentation cannot be tested to determine adequacy or effectiveness.

E. **Compliance Testing.** Testing that determines the extent to which staff follow prescribed policies and procedures in actual practice, comparing procedures as executed against required or expected procedures. Such testing provides objective evidence on how well controls are executed.

F. **Control Deficiency.** A condition in which the design or operation of a control does not allow management or employees, in the course of performing their assigned functions, to prevent, detect, or correct deviations from design expectations in a timely manner.

G. **COSO.** A private sector organization dedicated to guiding organizations toward the establishment of more effective, efficient, and ethical operations. COSO has established a definition of management controls and standards, and has set criteria against which companies and organizations can assess their control systems.

H. **Effectiveness of Systems of Control.** A control evaluation designed to manage risk to a reasonable level, rather than eliminate all risk of failure to achieve policies, goals, and objectives. Therefore, it can only provide reasonable and not absolute assurance of effectiveness (**example:** compliance testing).

I. **External Audits.** Audits conducted by independent auditors not affiliated with FSIS (**examples:** OIG and GAO).

J. **Internal Audits.** Audits conducted by independent auditors affiliated with, but separate from, the program area being audited.

K. **Management Controls.** The organization, policies, and procedures used to ensure that business is conducted as expected; programs achieve their intended results; resources are used consistent with Agency mission; programs and resources are protected from waste, fraud, and mismanagement; laws and regulations are followed; and reliable and timely information is obtained, maintained, reported, and used for decisionmaking.

L. **Material Weakness or System Nonconformance.** A major deficiency in Agency management controls when:

1. There is not reasonable assurance that management controls are achieving their objectives (see FMFIA, Section 2).
2. Management controls do not comply with financial systems requirements (see FMFIA, Section 4).

M. **Performance Measures.** A management tool for enhancing decisionmaking and accountability that is in addition to management controls. Performance measures consist of ways to objectively assess or measure the degree of success an organization has had in achieving its strategic objectives, goals, and planned program activities.

N. **Program Area Management Control Liaison.** A representative who facilitates the communication of the program area's management control activities, oversees the monitoring function from the program area's perspective, and keeps program area management current on all Agency management control issues.

O. **Reasonable Assurance.** A management concept whereby managers rely on operational information and experience to know whether risks are acceptable or effectively managed. Reasonable assurance recognizes that no system of management control is perfect and any efforts to reduce risk must be tempered by the cost of a control not exceeding the benefit derived.

P. **Significant Control Deficiency.** A control deficiency that has a moderate or high inherent risk which is not mitigated by adequate controls, warrants reporting to the next level of management, and merits the attention of the Secretary of Agriculture.

VIII. **BACKGROUND**

A. **FSIS MCS.**

1. Early in fiscal year 2005, the FSIS Administrator directed the Agency to design and implement a comprehensive MCS to support Agency programs and interdependencies.

2. The FSIS MCS complies with requirements in USDA Management Control Manual, DM 1110-002; OMB revised Circular A-123, Management's Responsibility for Internal Control; and the FMFIA, Title 31, U.S.C. 3512, which require agencies to establish and maintain management controls, conduct ongoing audits and evaluations, and report the adequacy of internal accounting and administrative control systems.

3. Management controls, also known as internal controls, include processes for planning, organizing, directing, and controlling Agency operations and resources. The controls should include systems for measuring, reporting, and monitoring performance.

B. FMFIA and the Chief Financial Officer’s Act.

1. The FMFIA is the central authority for establishing and maintaining Agency controls. It requires the head of each agency to establish and maintain management controls for all Agency programs, organizations, and functions. The Act also stipulates that accounting systems should conform to Federal accounting standards and related requirements.

2. The Chief Financial Officer’s Act of 1990 (Public Law 101-576) identifies management control-related activities as a primary responsibility of the Department’s Chief Financial Officer (CFO). The FSIS CFO has primary responsibility for Agency financial and accounting management control reviews.

C. COSO.

FSIS has adopted COSO components in auditing Agency management controls. The five components are control environment, risk assessment, control activity, information and communication, and monitoring (see Attachment 1-1, Auditing Internal Controls: COSO-Based Approach).

IX. ROLES AND RESPONSIBILITIES

The following describes the roles and responsibilities of key personnel during audits of management controls:

A. Office of the Administrator and the FSIS Management Council.

1. Provide leadership in the implementation of management controls in all FSIS programs to achieve the Agency’s mission effectively and efficiently.

2. Ensure that management controls are an integral part of the Agency’s entire cycle of planning, budgeting, program delivery and operations, accounting, and auditing processes.

3. Ensure program monitoring, ongoing audits, and corrective actions in implementing appropriate and cost-effective management controls for all processes that support the delivery of Agency programs and operations.

B. AAs and Division and Staff Directors.

1. Ensure the availability of program information and cooperation of program personnel during audits of management controls.

2. Ensure that management controls are implemented, maintained, and monitored within each program or functional area.

C. OPEER AA.

1. Provides Agencywide leadership and guidance related to the management control program and related audit activities.

2. Provides periodic updates to the FSIS Management Council regarding new requirements and management control audit findings.

D. ICS Director (or designee).

1. Ensures planning and implementation of the Agencywide management control audit program.

2. Ensures that audit teams are properly staffed and trained to conduct audits of management controls.

3. Ensures that management control audits are planned and performed in accordance with this directive and related standards, guidelines, and procedures.

4. Ensures the quality control of the final audit reports and transmittal to OPEER and program area AAs.

E. Audit Team Leader.

1. Ensures that management control audits are planned and performed in accordance with this directive and related standards, guidelines, and procedures.

2. Provides first-level review in directing management control audit planning, monitoring onsite activities, and reviewing work papers, tentative findings, and report preparation.

3. Serves as the primary point of contact during the management control audit.

4. Ensures that the management control audit reports are reviewed, finalized, and transmitted to the appropriate ICS Branch Chief (or designee).

F. Audit Team.

1. Performs management control audits in accordance with this directive and related standards, guidelines, and procedures.

2. Prepares the audit plan under the team leader's direction to include defined scope, staff requirements, milestones, and audit steps.

3. Performs all management control audit fieldwork needed to gather relevant evidence for measurement and evaluation.
4. Develops findings and recommendations from evidence collected.
5. Develops the management control audit report for submission to the audit team leader.

AUDITING INTERNAL CONTROLS: COSO-BASED APPROACH

All FSIS programs should utilize the five integrated components of COSO in establishing and implementing their MCSs. Each component is described below and includes criteria for how auditors may assess whether a program is addressing the components.

- **Control Environment.** The foundation for all other components of management controls. Auditors assess through interviews, questionnaires, and documentation whether:
 - The program area has a mission statement.
 - Managers and employees possess integrity, ethical values, and competence.
 - The nature of management's philosophy and operating style is appropriate.
 - There is proper assignment of authority, responsibility, and separation of duties.
 - There is proper organization of available resources and sufficient resources.
 - There is proper training and development of people.
 - The program area promotes efficiency, reduces risk of loss, and ensures compliance with applicable laws and regulations.
 - There is proper attention and direction from management.
- **Risk Assessment.** The identification, analysis, and management of risks. Auditors assess through interviews, questionnaires, and documentation whether:
 - Management has established a set of objectives that integrates all of the organization's resources.
 - Management identifies, analyzes, and manages the risks and obstacles involved in the successful achievement of objectives.
- **Control Activity.** Policies and procedures to ensure management directives are carried out and necessary actions are taken. Auditors assess through interviews, questionnaires, and documentation whether management has established and executed policies and procedures to ensure the effective implementation of actions to address risks and to achieve objectives.

- **Information and Communication.** For this component, internal and external information is identified, recorded, and communicated in a manner that enables Agency personnel to carry out responsibilities. Auditors assess through interviews, questionnaires, and documentation whether:

- Pertinent information is identified, captured, and communicated in a form that enables people to effectively carry out responsibilities.
- Communication flows in all directions throughout the organization.
- Management has made it clear to all employees that control responsibilities are to be taken seriously.
- Employees understand their own roles in the internal control system, as well as how individual activities relate to the work of others.
- All employees have the means to communicate significant information upstream.
- There is effective communication with external parties.

- **Monitoring.** Encompasses Agency activities that evaluate the quality and effectiveness of management controls while ensuring that all findings are resolved promptly. Auditors evaluate the implementation and effectiveness of an MCS which also can include resolving previous findings and reporting new findings. Auditors assess through testing whether:

- The entire MCS is monitored to assess the quality of the system's performance over time.
- There is ongoing monitoring in the normal course of doing business. Such monitoring can be regular supervisory and management activities, and the actions employees take in performing normal duties.
- Internal deficiencies are reported upstream, with serious matters reported directly to top management.
- Evaluations of the internal control system are independent.

PART TWO – CONDUCTING AUDITS OF MANAGEMENT CONTROLS

I. INTRODUCTION

Part Two provides the methodology for conducting audits of management controls.

A. Scope.

The scope of the management control audit is to verify the most recent management controls and performance measures developed and implemented by the program area being audited. The audit team determines whether FSIS program areas being audited require updated management controls, if prior audit recommendations have been addressed (for both internal and external audits), and if previous Agency corrective actions are effective in mitigating risk. These issues are discussed and the scope (of the management control audit) is agreed upon with the program area being audited prior to the initiation of the audit.

B. Objectives.

1. All management control audits verify:
 - a. Development and implementation of management controls within the FSIS program area.
 - b. Establishment of performance measures for management controls.
2. Additionally, audits may verify the effectiveness of management controls in achieving program objectives.

II. PERFORMING MANAGEMENT CONTROL AUDITS

A. The following provides a brief overview of the auditor's role during an audit. For all management control audits, auditors:

1. Review the program area's basic requirements (**examples:** regulations, policies, procedures, manuals, directives, and organizational structure).
2. Collect and review evidence relating to the implementation of the basic requirements and identify the scope of the review.
3. Review prior audit findings and recommendations.
4. Review prior corrective actions.
5. Conduct interviews and data analysis.

6. Compare the basic requirements to the evidence collected.
7. Develop findings and recommendations based on the analysis of the evidence against the basic requirements.
8. Develop conclusions based on the facts, observations, and findings.
9. Document final results.
10. Discuss with management as needed.

B. Additionally, auditors may determine the adequacy and effectiveness of management controls and performance measures.

C. When auditing management controls, OPEER auditors must follow an audit process that includes three phases: Planning, Testing and Analysis, and Reporting. Refer to Attachment 2-1, Management Controls Audit Process, and Attachment 2-2, Management Controls Audit Process Flowchart, for more specific information regarding the audit steps that occur under each phase.

III. **MONITORING CORRECTIVE ACTIONS**

Corrective actions are voluntary management decisions to address reported audit findings and recommendations, as warranted, based on acceptable operational risk levels. After an audit report is complete, the program area monitors corrective actions as part of the FMFIA process through their annual assurance statement. It is management's ultimate responsibility to ensure that the program area meets its mission objectives and goals. Program managers are also responsible to the FSIS Administrator and Management Council for systems of management controls and risk management.

IV. **ICS RECORDKEEPING AND FOLLOW-UP**

After the final audit report is issued, the audit team leader is responsible for organizing and storing all audit evidence, documentation, findings outlines, and final reports. Audit information can be stored in either electronic or paper form. The audit report and supporting documentation must be available in accordance with the criteria outlined in the ICS records management plan.

V. **DATA ANALYSIS**

OPEER analyzes the data compiled during the management control audit to identify lessons learned to improve communications and enhance operational efficiency and effectiveness throughout FSIS. The data analysis determines significant findings, trends, cross-cutting issues, and other pertinent information related to the Agency's mission of public health and food safety.

VI. **ADDITIONAL CONTACT INFORMATION**

For additional information, contact the Branch Chief, Management Controls Branch, ICS, OPEER at (202) 720-5959.

A handwritten signature in black ink, appearing to read "William P. Milroy". The signature is written in a cursive style with a large, sweeping initial "W".

Assistant Administrator
Office of Management

MANAGEMENT CONTROL AUDIT PROCESS

When auditing management controls, OPEER auditors must follow an audit process that includes three phases: Planning, Testing and Analysis, and Reporting. Each phase contains specific audit steps. Although the audit steps are described sequentially, some aspects may occur concurrently. (Refer to Attachment 2-2, Management Controls Audit Process Flowchart, for further information.)

• **PLANNING PHASE**

Detailed planning is required to ensure that a management control audit is thorough, unbiased, efficient, and effective. Proper planning reduces audit risk so auditors can have reasonable assurance that evidence gathered is sufficient and appropriate to support audit findings and recommendations. During the planning phase, the audit team is formed and develops the audit plan. The following activities occur during all management control audits:

- Assemble the audit team ensuring that it is qualified, trained, and understands its roles and responsibilities.
- Gather data and background information to obtain a thorough knowledge of the program area. Identify issues to audit from sources such as Congressional inquiries, OIG reports, incident reporting, media, or Departmentwide vulnerabilities. Identify data and information that is assessed for the application and relevance to the audit subject area in accordance with COSO to complete the audit plan. The data and information is obtained by the auditors from, but not limited to, the following sources:
 - Agency information systems or databases (**examples:** AssuranceNet, Performance Based Inspection System (PBIS), Electronic Animal Disposition Reporting System (eADRS), Automated Import Information System (AIIS), Inspection Appeals Tracking System (IATS), LEARN, ProClarity, Bovine Spongiform Encephalopathy (BSE) Surveillance Information System, Non-Routine Incident Management System (NRIMS)).
 - Regulations, statutes, directives, notices, implementing instructions, standard operating procedures, special studies, internal reports, and other relevant documentation.
 - Past audits and recommendations, FMFIA self-assessment reports, open audit recommendations from OIG and GAO reports, corrective action plans, and other evaluations.
 - Documents explicitly describing program-specific management controls such as management control worksheets, performance measures, and management controls in AssuranceNet.

- AgLearn and training materials.
 - Outline the proposed program-specific audit objectives to assess whether programs have established and implemented management controls to achieve desired mission objectives and program performance. The audit determines whether management controls are functioning as intended.
 - Conduct preliminary review and analysis of the relevant information using COSO to identify issues, noncompliance, and probable high-risk activities.
 - Finalize the audit objectives and scope after researching and analyzing data.
 - Notify the program AA in writing of an impending audit, stating the objectives and scope, date of the planned audit, request for a point of contact, and any additional information. The notification letter can identify what information should be available to the auditor during the onsite audit, and other support assistance.
 - Prepare an audit plan that includes the audit objectives, scope, milestones, audit team members, audit sample, methodology (**examples**: methods for assessing risks, testing management controls, and reporting material or significance findings), relevant criteria for assessing performance, applicable laws and regulations, relevant coordination with others, timeline, and report template.
 - Identify and contact program areas that may be impacted.
 - Arrange and hold the entrance conference to discuss the objectives, scope, and milestones of the audit.
 - Obtain work schedules for operating personnel and critical activities to plan and minimize the disruption of ongoing work operations.
 - Prepare internal and external communications plans.

- **TESTING AND ANALYSIS PHASE**

- Auditors test and analyze the implementation and effectiveness of management controls and performance measures to determine whether the controls are functioning as intended. For all management control audits, auditors test management controls and performance measures by comparing them to relevant regulations, standards, and expected results from the program area. When differences are noted, auditors ensure that all relevant evidence is collected, documented, and verified to support findings and recommendations. Auditors analyze and document evidence to substantiate the basis for identifying trends, reaching judgments, and drawing conclusions. Analysis can consist of comparison, observation, verification, actual performance, and retesting. Trends, judgments, and conclusions obtained through analysis must be supported by evidence that is sufficient and valid to develop findings and recommendations. All evidence and analysis will be documented in the auditor's work papers.

- During an audit, auditors will also authenticate the presence, quality, or relevance of management controls and evaluate the accuracy and quality of documentation for performance measure data.
- Auditors will take the following steps for all management control audits:
 - Discuss the planned audit methodology with program personnel and collect additional evidence (**examples**: data and information).
 - Verify that management controls and performance measures have been implemented and reviewed, as documented. This step assesses the following issues:
 - Are program objectives clear and linked to controls?
 - Are performance measures adequately measured?
 - Are results used as intended?
 - Do performance measure results agree with supporting records?
 - Are performance measures integrated into decisionmaking?
 - Verify that the program area's MCS or similar procedures clearly define the responsibilities of all key personnel.
 - Evaluate how key personnel's responsibilities compare to responsibilities found in the MCS.
 - Determine if the test results analyzed are sufficient, competent, and relevant to develop findings and recommendations.
 - Ensure that findings and recommendations are in compliance with the U.S. GAO, Government Auditing Standards, July 2007 Revision.
 - Ensure that audit findings address the audit objectives and include the condition, criteria, cause, effect, and possible recommendations.
 - Ensure that the auditor's judgments and conclusions are supported by audit documentation analysis.
 - Notify the program area AA immediately if a finding leads to a material weakness or evidence of a condition posing an imminent threat to public health. This requirement is to be implemented during any phase of the management control audit.

- Continually anticipate, evaluate, and report any potential significant roadblocks, audit plan changes, outcomes, and audit deadlines with program area management and OPEER management when appropriate to resolve potential problems.
- Arrange the exit conference with the program area within 2 weeks of completion of onsite work to discuss audit findings. Discuss the information collected from the program area and confirm that no additional information is required. Discussions with the program area on the factual accuracy of audit findings can occur before the exit conference.
- Auditors may also take the following steps during an audit:
 - Evaluate the critical activities for management controls to confirm that they are effective and appropriate to a program area's mission.
 - Evaluate the critical activities for performance measures to confirm that they are effective and appropriate to a program area's mission.

- **REPORTING PHASE**

- The reporting phase consists of documenting and presenting the audit findings and recommendations. The audit report should include a detailed explanation of whether the audit objectives were met by tying the evidence (**examples**: testing and analysis results) to the objective. The auditors take the following steps:
 - Prepare a draft audit report within 30 days of the completion of fieldwork, as stated in the audit plan for review by ICS management.
 - Ensure the draft report concurs with the stated scope and objectives of the audit and includes an assessment of the program area's management controls and performance measures in accordance with COSO.
 - Ensure that documentation supports all information contained in the draft audit report.
 - Ensure that all findings are documented and any recommendations are supported with evidence collected during the testing and analysis phase.
 - Send the draft report to the program area's management for comments and corrective action response.
 - Allow the program area 30 days from receipt of the draft report to review and provide final comments and possibly, a corrective action plan, as stated in the audit plan.
 - Incorporate program area management comments and corrective actions into the draft report. Once this is done, submit the report to the appropriate ICS Branch Chief (or designee) for review and concurrence.

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- The appropriate ICS Branch Chief (or designee) will submit the report to the ICS Director.

- The ICS Director will submit the final report to the OPEER AA for transmittal to the program area AA.

Management Control Audit Process Flowchart

