

Audit Trails and Source Documents Supporting Automated Databases and Financial Statements: So What?

Do you know where your marriage license is? Did you know your marriage license is a source document? It proves you are married. Will you be ready when the Internal Revenue Service calls? Taxpayers are responsible for maintaining source documents to support transactions on their tax returns that have an impact on their income, deductions, and tax liability, and to prove ownership, prove citizenship, enable us to obtain a driver's license, and a myriad of other things.

In the same way, government agencies including the Department of Defense (DoD) are responsible for maintaining proper records that can serve as source documents and as part of an audit trail during an audit of financial and/or other automated information systems, such as those used to manage human capital.

In our private lives, source documents that serve as an audit trail can include deeds of trust; purchase invoices; inventory receiving documents; receipts for charitable donations; birth certificates; grocery store, gasoline, and restaurant receipts; and an electronic copy or hard copy of a check for a mortgage payment. Did you ever stop to think that, every day, people like you and me collect source documents and maintain audit trails?

As demonstrated by the examples above, we all need source documents to manage our affairs. In addition to its fleet and bases and support materiel, the DoD must properly keep track, through a variety of methods including electronic databases, of its human capital – the personnel who are the DoD's soldiers, sailors, airmen, and civilian support employees – and critical information about them. Without them DoD cannot operate, and without proper records the Services cannot keep track of their human capital to determine if it is being used to the greatest benefit to DoD and the nation.

Source documents and audit trails help us provide reasonable assurance that:

- 1. We own assets;*
- 2. A transaction occurred;*
- 3. We are liable for the charges;*
- 4. The charges are accurate; and*
- 5. Payment was made to the intended party.*

Source documents and audit trails also give us the ability to reconstruct transactions or events.

“In the midst of war and transformation, a constant remains – accountability,” wrote Gordon England, Assistant Secretary of Defense-nominee and Secretary of the Navy, in the cover letter of the Department of the Navy's 2003 Annual Financial Report. “...Efficient and effective management of financial resources enhances our enduring roles of assurance and deterrence, command of the seas, power projection, and homeland security.”

Accurate, timely, and reliable financial and other management information affirmed by favorable audit opinions is a key financial management goal. DoD has been working for more than a decade to obtain favorable opinions of its financial statements. This is not merely a “good business” practice by the DoD, but a requirement of the Chief Financial Officers Act of 1990. A key obstacle to obtaining favorable opinions has been the Department’s inability to support the information in its statements with adequate source documentation.

For example, managers can rely on audit trails to trace any change to data processed and stored by information systems. Much financial and management data, such as personnel assignments, training, travel orders, payroll, health records, etc., still exists on paper at some time during its life.

In the same manner that taxpayers must have source documents to support their tax returns, DoD managers must have source documents to support their entries on financial statements and in feeder systems that house financial and other data, such as human capital data.

Increasingly, however, data enters our information systems from other electronic sources. These paper records or electronic data can form the foundation of the audit trail.

For many years, the DoD audit community showed that the lack of audit trails and source documents have directly contributed to auditors reporting numerous material weaknesses, and that continues to be a problem today. Among these material weaknesses is a lack of source documents and audit trails that cause auditors’ inability to render favorable audit opinions. A key to achieving a favorable audit opinion is assuring that information affecting the financial statement has an audit trail sufficient to enable anyone to clearly trace the information to a source document.

So what are Audit Trails and Source Documents?

Audit Trails

A good audit trail should be able to answer the “who,” “what,” “when,” “where,” “why,” and “how” questions. There are various existing Government-wide regulatory requirements associated with audit trails. Figure 1 provides the applicable policy guidance regarding the requirements for maintaining and retaining audit trails.

An audit trail comprises all of the records, either paper or electronic, that enable someone to reconstruct a transaction. Audit trails should allow for a transaction to be traced from initiation through processing to final reports.

Figure 1. Policy Guidance for Audit Trails

GUIDANCE	REQUIREMENT
DoD Regulation 7000.14-R, Volume 1, Chapter 3	A key test of the adequacy of an audit trail is whether tracing the transaction forward from the source or back from the result will permit verification of the amount recorded or reported.
DoD Regulation 7000.14-R, Volume 6, Chapter 2	DoD Components shall ensure that audit trails are maintained in sufficient detail to permit tracing of transactions from sources to their transmission to the Defense Finance and Accounting Service.
Defense Finance and Accounting System, “A Guide to Federal Requirements for Financial Management Systems,” Chapter 14	Audit trails (documentation of transactions from their inception to final disposition and reporting in the books or original entry) are critical to providing support for transactions and accounts. All transactions, including computer-generated computations, must be traceable to individual source records. Step 14.01.07 states that a system must provide the capability to retain archived data and system records in accordance with Federal regulations established by the National Archives and Records Administration (NARA).
National Archives and Records Administration, General Records Schedule 7	Requires that general accounting ledgers be maintained for 6 years and 3 months.
Joint Financial Management Improvement Program, “Core Financial System Requirements”	Requires core systems to: (1) retain archived data and system records in accordance with Federal regulations established by NARA, the General Accounting Office, and the National Institute of Standards and Technology; and (2) provide the ability to selectively retrieve archived data based on user-defined criteria such as date, account period, or vendor.

Source Documents

Before we talk some more about source documents, let’s briefly describe the term “evidence.” Evidence is information obtained and used by managers, auditors, or team members to arrive at a conclusion or support an opinion. Evidence is comprised of source documents and accounting records, and corroborating information from other sources.

Source documents are the evidence of initial input into the accounting process and serve as objective evidence of a transaction. They serve as part of the audit trail should an activity or organization need to prove that a transaction occurred. For example, the source document captures the key data of the transaction when a business event, such as a receipt of revenue, personnel reassignment, or receipt of inventory, occurs. The source document describes the basic facts of the transaction such as **who** authorized it, **what** was the event, **when** did it occur (the date), **where** did it occur,

Source documents and audit trails also provide managers with a means of monitoring and measuring the effectiveness of controls over day-to-day operations, identifying the sources of automated system errors, and the effectiveness of programs.

why did the event occur (the purpose), and *how much* was spent (the amount). Source documents may be created in either paper or electronic format. Figure 2 provides some examples of both paper and electronic source documents.

Figure 2. Examples of Source Documents

- Cash Receipt**
- Cancelled Check**
- Invoice Sent or Received**
- Time Sheet**
- Travel Order**
- Military Interdepartmental Purchase Request (DD Form 448)**
- Order for Work and Service/Direct Citation (NAVCOMT 2276)**
- Schedule of Cost Accrual**
- Contracts**
- Amendment of Socialization/Modification of Contract (Standard Form 30)**
- Fund Rates Calculation**
- Order for Supplies or Services (DD Form 1155)**
- Research Grant Letter**
- Interagency agreement or Project Agreement**
- Solicitation/Contract/Order for Commercial Items (Standard Form 1449)**
- Request for contractual Procurement**

Source documents are often followed by the creation of many additional records, which do not qualify as initial recordings. Auditors often find that many personnel have a misunderstanding of what constitutes a source document. They believe that paper or electronic sources such as computer printouts, onscreen images, or even some form such as a Standard Form (SF) 1080 “Voucher for Transfers Between Appropriation and/or Fund” are valid source documents. However, computer printouts or onscreen images are usually just the representation of electronic information in a requested format. The electronic format may not always provide indication of the origin, authorization, or integrity of the data therein. Computer printouts can be part of an audit trail but are not usually source documents in and of themselves. For example, the Standard Form 1080 is not considered a sufficient source document because it summarizes multiple transactions for various cost elements such as labor, travel, and payroll. In this case, the individual supporting travel vouchers with appropriate receipts supporting employee travel costs, and timesheets with signatures to verify employee payroll and labor costs, would be the appropriate source documentation.

Internal Controls

Internal controls are processes that management establishes within a business or government agency that are intended to ensure accuracy, timeliness, and completeness of information, as well as compliance with policies and regulations. As part of a sound internal control program, managers need to rely on audit trails and source documents to form the basis for effective and efficient business operations. To illustrate, source documents provide managers information required to analyze and classify a transaction and to create the journal entries about that transaction. A key enabler to achieving the goal of a favorable audit opinion on financial statements is that information affecting the statement, as well as the effectiveness of internal controls, should have a sufficient audit trail to enable anyone to clearly trace the information to a source document.

Consequently, individuals involved in the financial statement and internal control processes should recognize the importance of maintaining an audit trail and producing adequate source documentation.

Nearly all business processes, such as acquisition, financial activities, contracting, and logistics, have many internal controls. Determining the risks that may occur in a business process requires examination of the overall control environment related to the business process. Maintenance of a good audit trail and adequate source documents are an example of sound internal controls. Documents of original entry and records upon which transactions are entered are important elements of internal controls. The ability to trace transactions to source documents provides managers reasonable assurance that all assets are properly controlled and all transactions are correctly recorded. For example, information on a receiving report can be compared to a purchase order or an invoice to verify that the quantity and type of goods ordered has been received before a payment to the vendor is processed.

Information in source documents such as this will help DoD better manage its business operations, obtain favorable opinions on its financial statements, and know that the information upon which it is basing its management decisions, such as in the human capital area, is accurate and reliable.

As for you, have you found your marriage license yet? If not, ***good luck with the IRS!***