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Texas Department of Human Services Effectiveness of Internal Audit Engagement June 1997

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Overall Conclusion

The Internal Audit Department (Internal Audit) of the Texas Department of Human Services (Department) is effective:

- Internal Audit assists members of the organization in the discharge of their responsibilities.
- Internal Audit provides analyses of the adequacy and effectiveness of internal control systems, policies, procedures, and departmental performance.
- Auditees perceive Internal Audit staff to be qualified professionals, providing logical, understandable, useful recommendations.
- Internal Audit meets all eight of the effectiveness criteria developed from the Texas Internal Auditing Act.

Internal Audit employs seven auditors to provide audit coverage for the activities of the Department. The Department is responsible for an operating budget of \$ 3.2 billion, which includes more than \$ 2.8 billion in contract expenditures, providing about \$2.8 billion in revenues, and employing more than 18,100 employees.

Section 1:

The Internal Audit Department Is Effective in all Eight Key Criteria



Assessing Entity Risks - Internal Audit prepares a comprehensive risk assessment which appropriately identifies and ranks agency auditable areas. Management input is obtained when identifying and ranking these areas. The assessment is well-documented and linked to the annual audit plan and the Department's strategic plan.



Preparation of the Audit Plan - The audit plan reflects the high-risk areas of the Department. Internal Audit uses input from many sources to determine these areas. Internal Audit expends its resources on these high-risk areas.

Organizing and Managing the Internal Audit Function - Internal Audit's staff has the necessary skills, educational backgrounds, professional certifications, training, and experience to carry out audit responsibilities. Internal Audit uses monthly status reports to keep executive management and the Texas Board of Human Services (Board) informed of activities and progress.

Planning and Conducting Audits - Internal Audit plans and conducts audits according to the Institute of Internal Auditing standards.

Communicating Audit Results - Audit reports contain the scope, purpose, objectives, executive summary, overall opinion, appropriate references, and responses from management and auditees. Internal Audit sends the reports to the Commissioner and

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all Board members, which helps to ensure auditees will take corrective action. The findings and recommendations are clear, concise, and objective.

Ensuring Compliance With Audit Standards - Internal Audit is in compliance with requirements of the Texas Internal Auditing Act, the Institute of Internal Auditing Standards, and government auditing standards. Internal Audit is also in compliance with the Institute of Internal Auditing's *Code of Ethics*.

Management Involvement in the Internal Audit Program - Executive management and the Board approved the Internal Audit Department charter, annual audit plan, and departmental budget. Additionally, Internal Audit discusses all audit reports with executive management and Board members.

Following-Up on Audit Recommendations - Internal Audit performs timely follow-ups on all audit recommendations. Follow-up review procedures are outlined in Internal Audit's handbook.

Section 2:

Office of Inspector General Compliance Audit Function Merged With Internal Audit Department

Subsequent to the end of our fieldwork, the Office of Inspector General compliance audit function was merged with the Internal Audit Department. Obligating Internal Audit with certain compliance responsibilities is not consistent with internal auditing standards requiring the internal audit function to be free of all operational responsibilities.

The effect is that the Department of Human Services has reduced the ability of Internal Audit to independently evaluate the compliance function.

Recommendation:

We recommend that the Department develop a plan to independently evaluate the compliance function periodically as long as it remains a part of Internal Audit.

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Management's Response:

The Department plans to contract with an independent auditor to evaluate the compliance function as long as it remains a part of the internal audit department. The evaluations will be performed periodically, scheduled at least as frequently as peer reviews are currently required by the Texas Internal Auditing Act, once every three years. The independent auditor selected will be either a private sector firm or a public sector entity, such as the State Auditor's Office.

Objectives, Scope, and Methodology

Objectives

The objectives of Evaluating the Effectiveness of Internal Audit were to:

- Evaluate the effectiveness of the State's internal audit departments.
- Determine whether internal audit departments meet the key objectives of internal auditing and assist agency administrators in carrying out their assigned responsibilities.

Scope

The scope of the audit included:

- Evaluating the effectiveness of 12 of the larger state agencies' internal audit departments
- Surveying the board chairs, elected officials, audit committee chairs, and internal audit department directors of the 79 agencies and universities with internal audit departments to obtain their opinions and comments on the effectiveness of internal auditing; and compiling the results of the survey.

Methodology

The methodology used on this engagement consisted of developing criteria, obtaining information on each of the 12 agencies selected for review, analyzing the information, and evaluating the information against the criteria.

Information collected to accomplish the audit objective included the following:

- Interviews with management of oversight agencies
- Interviews with management and staff of individual agencies
- Documentary evidence, including:
 - State statutes
 - Internal auditing standards
 - Government Auditing Standards
 - Agency documents including plans, policies, manuals, reports, memoranda, and other written communications
 - Internal audit reports

Objectives, Scope, and Methodology

Procedures and tests conducted:

Internal audit function information collected in the current fiscal year and the last two completed fiscal years was evaluated against criteria developed from the Texas Internal Auditing Act.

Criteria used:

- Criteria developed from the Texas Internal Auditing Act

The following are the eight effectiveness criteria and a brief definition of each:

- **Board/Management Involvement in Internal Audit Function** - The agency's board or elected official and executive management are adequately involved in the internal audit function and in completing their responsibilities under the Texas Internal Auditing Act.
- **Organizing and Managing the Internal Audit Function** - The internal audit director is effective in managing and organizing the internal audit department.
- **Assessing Entity Risks** - A risk assessment is used in the audit planning process and all agency risks are identified and appropriately ranked.
- **Preparation of the Audit Plan** - The audit plan includes those areas identified as high risk, and resources are available to complete the plan.
- **Planning and Conducting Audits** - Audit projects are properly planned, and due professional care is used in performing the audits.
- **Communicating Audit Results** - The results of audits are appropriately communicated in written format to the proper level to ensure corrective action is taken.
- **Ensuring Compliance With Audit Standards** - The internal audit department takes steps to ensure work conforms to audit standards
- **Follow-Up on Audit Recommendations** - The internal audit department follows-up recommendations in audit reports from prior periods.

Objectives, Scope, and Methodology

Other Information

Fieldwork was conducted from April to September 1996. The audit was conducted in accordance with applicable professional standards, including:

- Generally Accepted Government Auditing Standards
- Generally Accepted Auditing Standards

The audit work was performed by the following members of the State Auditor's staff:

- Terry Holderman, MBA (Team Leader)
- Kim Builta, CPA
- Tom McGaha
- Larry Vinyard, CPA, CIA (Project Manager)
- Linda Lansdowne, CPA (Quality Control Reviewer)
- Charlie Hrcir, CPA (Audit Manager)
- Deborah Kerr, Ph.D. (Audit Director)