

April 26, 2006

Members of the Legislative Audit Committee:

The Texas Medical Board (Board) has most of the internal controls necessary to provide reasonable assurance that its expenditures are properly authorized, reasonable, and processed correctly and in a timely manner. Although all of the expenditures that auditors tested were appropriate and reasonable, opportunities exist for the Board to strengthen the processes related to its payroll function, professional service fees expenditures, and travel advance fund. In addition, the Board did not have an internal audit function, as required, for a portion of the audit period.

Expenditure categories tested included salaries and wages, professional service fees, and travel. These categories represented 69.1 percent of the Board's total expenditures during the audit period (see text box). Although the expenditures tested came from selected categories, the internal controls in place are the same for all types of expenditures. Any system of internal controls has inherent limitations and can provide only reasonable assurance of achieving the control objective, regardless of how well it is designed and operated. Internal controls cannot provide absolute assurance that errors or irregularities would be prevented or detected.

Salaries and Wages (Payroll Process)

All 40 of the salary and wage expenditures tested, totaling \$137,156, were appropriate and reasonable, but auditors identified opportunities for the Board to strengthen its internal controls over the payroll process. For example, the Board has granted one employee the authority to both enter and release payroll data in the Uniform Statewide Payroll/Personnel System. In addition, the Board's documented payroll procedures do not address key situations, such as procedures to follow when payroll processing employees are unavailable to perform payroll functions.

One employee entered and released 4 of the 31 payrolls processed during the audit period. This lack of segregation of duties presents a risk that inappropriate payroll transactions could be set up and released without proper approval. Board records contained no evidence of other controls to mitigate that risk. Basic accounting principles require an organization to plan and provide for appropriate separation of functional responsibilities. For example, the person responsible for creating an accounting transaction for payment should not be the same person who approves or authorizes the payment.

Texas Medical Board Expenditures

The table below contains the amounts the Board expended, by category, for the audit period of fiscal year 2005 and fiscal year 2006 through November 30, 2005.

Texas Medical Board's Expenditures September 1, 2004, through November 30, 2005		
Category	Amount Expended	Percentage of Total Expenditures
Salaries and Wages	\$6,363,830.00	52.97%
Professional Service Fees	1,618,442.15	13.47%
Travel	319,599.46	2.66%
All Others	\$3,711,670.41	30.90%
Total Expenditures	\$12,013,542.02	100%

Source: Uniform Statewide Accounting System (USAS) and Uniform Statewide Payroll/Personnel System (USPS)

SAO Report No. 06-033

The Board's documented payroll policies and procedures do not include backup procedures that would provide for adequate controls in the payroll process when key employees are unavailable. The policies and procedures also do not address reliable methods for verifying employees' prior state service when the Board's initial request to another state agency for this information is not answered. Twenty-five percent of the sampled records did not contain adequate documentation for prior state service. The Office of the Comptroller of Public Accounts reported in its fiscal year 2003 post-payment audit that there were instances in which the Board incorrectly calculated employee longevity pay, resulting in both overpayments and underpayments.

Recommendations:

The Board should:

- Document and implement procedures to ensure that separation of duties exists for payroll processing or that mitigating controls are in place if separation of duties is not practical.
- Consider using alternative methods for verifying employees' prior state service when the information is not confirmed after an initial request to the other agency.

Professional Service Fee Expenditures

The Board pays professional service fees to consultants who work on investigation cases. All 35 of the expenditures for professional services fees that auditors tested, totaling \$126,837, were appropriate and reasonable. The Board is unable to determine whether invoices for professional services fees are being paid within 30 days, as required by Texas Government Code, Section 2251.021. This is because Board staff are not stamping the invoices with the date they are received as required by the Board's policies and procedures. The Board calculates the 30 days from the time the invoices are approved by the investigation department manager, instead of from the time they are actually received.

The Board also has not documented several procedures that its investigations department currently performs. These procedures include updating the case investigations database when invoices are received, reviewing invoices, and matching invoices to their corresponding case files. Without documented procedures, there is an increased risk that steps may be performed incorrectly or overlooked, particularly when key employees are unavailable.

Recommendations:

The Board should ensure that its investigation department:

- Strengthens internal controls by complying with the existing policy to date stamp all mail when it is received in the mail room.
- Revises its documented procedures to include all procedures performed.

Travel Expenditures

All 35 of the travel expenditures tested, totaling \$8,606, were appropriate and reasonable. Auditors found no errors related to the processing of travel expenditures, but we identified two internal control weaknesses related to the Board's \$2,000 travel advance fund:

- The Board has not provided for adequate segregation of duties over this fund. The same person who issues the checks from the fund also reconciles the account associated with it, and there is no independent review and approval of that reconciliation. This presents a risk that errors and misuse of state funds could go undetected.
- The Board does not comply with its policy requiring employees to submit travel vouchers for past travel advances before they can obtain additional travel advances. Of 19 travel advance vouchers tested, one employee had not submitted vouchers for past travel advances but continued to receive three additional advances totaling \$712.

Recommendation:

If the Board continues to have a travel advance fund, it should strengthen the controls over the use of this fund. The Board may want to evaluate the need to maintain a travel advance fund, taking into consideration the cost of additional controls. Other options available to the Board are to require employees who must travel to use the direct billing option or the state credit card available to them for travel expenditures.

Internal Auditor

The Board did not have an internal audit function during fiscal year 2004 and did not submit its required annual internal audit reports to the State Auditor's Office (Office) for fiscal years 2003 and 2004. The Board did not execute a contract for an internal auditor's services for fiscal year 2005 until August 12, 2005 (the last month of fiscal year 2005), and it does not currently have a contract in place for an internal audit function for fiscal year 2006. According to the Board, it removed the expenditure for the internal audit function from its budget for the 2004-2005 biennium in an effort to achieve a 12.5 percent budget reduction.

Texas Government Code, Chapter 2102, requires certain state agencies (including the Board) to have an internal audit function that includes preparation of an annual audit plan and periodic audits of major systems and controls. The statute also requires state agencies to submit an annual audit report to the Governor, Legislative Budget Board, Sunset Advisory Commission, and State Auditor. Without an internal audit function, the Board did not comply with this statute and it also did not have an independent and objective party to perform assurance and consulting services. Having an internal audit function helps an organization accomplish its objectives by providing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes.

Recommendation:

The Board should comply with all applicable terms of Texas Government Code, Chapter 2102, including maintaining an internal audit function and completing and submitting all required reports to the Governor, Legislative Budget Board, Sunset Advisory Commission, and State Auditor, as appropriate.

The Board generally agrees with our recommendations, and its responses are included in the attachment to this letter.

We appreciate the Board's cooperation during this audit. If you have any questions, please contact Susan Riley, Assistant State Auditor, or me at (512) 936-9500.

Sincerely,

John Keel, CPA
State Auditor

Attachment

cc: President and Members of the Texas Medical Board
Dr. Donald W. Patrick, J.D., Executive Director, Texas Medical Board



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Attachment

Objective, Scope, and Methodology

The audit objective was to determine whether expenditures for goods and services at the Texas Medical Board (Board) are properly authorized, processed correctly and in a timely manner, and reasonable for the performance of Board functions.

The audit scope included expenditures made during fiscal year 2005 and September through November 2005.

The audit methodology included interviewing personnel, performing analyses of the accounts, and reviewing original documentation. This audit was conducted in accordance with generally accepted government auditing standards.

Audit fieldwork was conducted from December 2005 through February 2006. The following members of the State Auditor's staff performed the audit work:

- Robert G. Kiker, CGAP (Project Manager)
- Margaret Nicklas, CGAP, CIA (Assistant Project Manager)
- Bev Bavousett, CPA (Team Leader)
- Pamela A. Bradley, CPA
- Anca Pinchas, MPA
- Karen Smith
- Leslie Ashton, CPA (Quality Control Reviewer)
- Susan Riley, CPA (Assistant State Auditor)



Texas Medical Board

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Management Responses to SAO Audit Conducted December 2005-February 2006

Payroll Process:

Recommendations:

The Board should:

- Document and implement procedures to ensure that separation of duties exists for payroll processing or that mitigating controls are in place if separation of duties is not practical.
- Consider using alternative methods for verifying employees' prior state service when the information is not confirmed after an initial request to the other agency.

Response:

The Board agrees with this recommendation. Finance staff will immediately implement new procedures to ensure separation of duties and controls exists for payroll processing. A new payroll reconciliation spreadsheet will be created and used for monthly payrolls. Management will approve the spreadsheet before final payroll is completed for each pay period.

Human Resources staff will be responsible for initiating the initial request to other agencies to verify employees' prior state service. HR will also be responsible for conducting a follow-up request, either through fax or email, if there has been no response from the initial request within 10 days. The initial request and follow-up request will be filed in the employee's personnel file, if applicable.

These procedures will be written and retained in agency operating procedures.

Professional Service Fee Expenditures:

Recommendations:

The Board should ensure that its investigation department:

- Strengthens internal controls by complying with the existing policy to date stamp all mail when it is received in the mailroom.
- Revises its documented procedures to include all procedures performed.

Response:

The Board agrees with this recommendation. However, the Board would like to take the opportunity to clarify the policy for date stamping mail. All mail is date stamped when it is received in the Agency mailroom. Invoices for professional services were not date stamped in the mailroom, but were forwarded to Investigations where the professional consultant report and invoice could be verified and approved by Investigation staff prior to payment. The group of professional consultant invoices is somewhat different from other invoices received in the Agency, due to the large volume received and the verification and approval process required. All other invoices are date stamped in the mailroom and are forwarded to Accounts Payable staff. Effective April 3, 2006, mailroom staff will be responsible for date stamping all incoming professional service invoices upon receipt in the Agency mailroom before being forwarded to the Investigations Department.

Staff of the Investigations Department will be responsible for revising its documented procedures to include all procedures performed within the professional services scope.

These procedures will be written and retained in agency operating procedures.

Travel Expenditures:

Recommendation:

If the Board continues to have a travel advance fund, it should strengthen the controls over the use of this fund. The Board may want to evaluate the need to maintain a travel advance fund, taking into consideration the cost of additional controls. Other options available to the Board are to require employees who must travel to use the direct billing option or the state credit card available to them for travel expenditures.

Response:

The Board agrees with this recommendation. The Board will eliminate the travel advance fund effective April 2006. The efforts needed to assure ongoing compliance with the requirements of the fund are out of proportion to the value received. The Board will inform employees about other travel options, including direct billing of travel expenditures and the state travel card by April 21, 2006.

Internal Auditor:

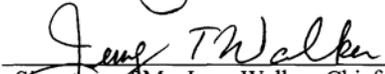
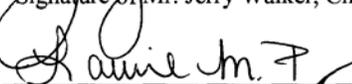
Recommendation:

The Board should comply with all applicable terms of Texas Government Code, Chapter 2102, including maintaining an internal audit function and completing and submitting all required reports to the Governor, Legislative Budget Board, Sunset Advisory Commission, and the State Auditor, as appropriate.

Response:

The Board agrees with the SAO recommendation and will comply fully with the Texas Internal Auditing Act as well as the SAO Guidelines for the Internal Audit Annual Report. TMB met the statutory requirement regarding submission of the FY 2005 internal audit. The agency was not aware of a statutory deadline for executing a contract for audit consulting services. TMB staff have completed a risk assessment as the first step in its internal audit for FY 2006 and is preparing the RFP for audit services. Risk assessment training for agency staff was conducted by the SAO in January 2006. It seemed appropriate for agency staff to complete training and conduct a thorough risk assessment prior to determining the focus of the audit contract. Since it is our understanding that neither the Act nor the SAO guidelines specifies deadlines or timetables for which internal audit contracts must be in place, the TMB would request SAO guidance for best practices to use when establishing a timeline to complete an internal audit that requires an external contract.

The Board would like to take this opportunity to comment on the applicability of both the statute and the guidelines to an agency of our size. While the TMB does just meet the statutory threshold requirements for FTEs (100) and annual operating budget (in excess of \$10 million), it does not have the resources available to have its own internal audit department as is commonly found in larger agencies. Consequently, internal audit activities must be performed under contract with external vendors. Given the limited financial and staff resources of an agency our size, an annual audit is a burden. We hope that SAO and the Legislature will consider a biennial audit requirement for some category of agencies slightly larger than those currently exempted. In addition, certain sections of the SAO Guidelines appear most applicable to state agencies that have their own internal audit departments. TMB will continue to clarify in its annual reports how the use of external vendors and other agency audit-related processes were used to meet the guidelines.

 _____ Signature of Dr. Donald W. Patrick, Executive Director	<u>4/11/06</u> Date
 _____ Signature of Mr. Jerry Walker, Chief Audit Executive	<u>4/11/06</u> Date
 _____ Signature of Ms. Laurie M. Perez, Director, Finance Division	<u>4/11/06</u> Date