

Key Points Of Report

Texas Education Agency 1994 Statewide Financial and Compliance Audit

March 1995

Overall Conclusion

The Texas Education Agency is not adequately protecting its automated information. The Internal Audit Department did not base its audit plan on a current risk assessment and has never received a peer review.

The Agency is in compliance with most federal regulations related to the \$1.5 billion of federal funds disbursed in fiscal year 1994.

The accounts in the Agency's 1994 Annual Financial Report that were tested as part of the statewide financial audit are materially accurate and properly reported. These accounts included Investments, \$8.5 billion; Purchases of Investments, \$1 billion; Sales of Investments, \$613 million; Education Expenditures, \$7.6 billion; Transfers In, \$6.8 billion; and Revenues from Licenses, Permits and Fees, \$336 million.

Key Findings

- Policies and procedures over security for over access to the Agency's automated information resources are incomplete. In addition, adequate resources have not been dedicated to monitor controls that safeguard information resources.
- The Agency's Internal Audit Department did not perform a current risk assessment to identify issues for its fiscal year 1994 and 1995 audit plans and has never received an internal audit peer review.
- The Agency's time reports used for allocating administrative expenditures between state and federal programs were not accurate. Three of five divisions tested did not submit accurate June 1994 time reports due to mathematical errors and an incorrect time charge. In addition, supervisor review and approval, which is required by the operating procedures, was not performed by three of the five divisions. This issue has been identified in prior audits.
- The Agency did not conduct timely reviews of all subrecipient audit reports. Seven of 45 audit reports tested were not reviewed timely. The reports were reviewed six months past the report receipt date.
- By not using estimates, the Agency materially understated the amount of federal funds passed through to school districts on the Schedule of Federal Financial Assistance in the Annual Financial Report by \$52.9 million. This misstatement occurred because the Agency did not record all federal expenditures by the school districts as of August 31, 1994.

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Other Related Reports

The State Auditor's Office has verified that \$140,364.00 in adjustments have been made as required by the U.S. Department of Health and Human Services' letter of resolution. These adjustments resulted from the November 1993 report on the State Legalization Impact Assistance Grant (CFDA 93.565) issued by the Department's Office of Inspector General. The report related to the Texas Education Agency and other state agencies.

Internal Control Issues

Internal Control Issue 1:

Develop And Administer Information Security Policies And Procedures

Policies and procedures over access security for the Texas Education Agency's automated information resources are incomplete. In addition, adequate resources have not been dedicated to monitor controls that safeguard information resources. Without the development and enforcement of security policies and procedures, automated information becomes more susceptible to improper modifications or deletions by unauthorized personnel. Weaknesses in security over federal program information resources which result from the lack of policy and procedure enforcement include:

- Programmers have access to the Financial Management System programs.
- Some programmers have access to data for the Federal Funding Program and Compensatory/Bilingual/Migratory systems.
- Computer operators are using the same user identification.
- Procedures to change user access in response to employee termination or change in job duties are not consistently performed.

These automated systems processed \$1.5 billion of federal funds in fiscal year 1994.

Department of Information Resources' (DIR) standards, adopted by the *Texas Administrative Code* [1 TAC §201.13(b)], require that by September 1, 1993, agencies are to have written internal policies and procedures for the protection of information resources.

Recommendation: The Agency should assign responsibility to develop and implement security policies and procedures over access to automated resources to help ensure the adequate protection of its State-owned information. DIR's standards and guidelines can assist the Agency in the development of policies and procedures which would also address the weaknesses cited above.

Management's Response: The agency agrees with this finding. The Agency's Department of Information Systems will take corrective action according to the following 1995 timetable:

<i>March</i>	<i>Assign responsibility to develop and implement security policies and procedures over access to automated resources.</i>
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<i>March-May</i>	<i>Develop security policies and procedures consistent with DIR standards and guidelines.</i>
<i>June</i>	<i>Acquire Agency approval for the newly developed security policies and procedures.</i>
<i>June-September</i>	<i>Implement the approved security policies and procedures.</i>
<i>September</i>	<i>Request follow up audit of agency security policies and procedures.</i>

Internal Control Issue 2:

Plan Annual Audits Based On A Current Risk Assessment

The Texas Education Agency's Internal Audit Division (Division) did not perform a current risk assessment to identify issues for its fiscal year 1994 or 1995 audit plans and has never received an internal audit peer review. An annual assessment should be performed to identify significant issues currently affecting the Agency. The 1995 audit plan contains limited financial and electronic data processing (EDP) audits even though these areas could significantly impact the Agency.

The internal audit function provides a mechanism for quality control that helps ensure that the entity is accomplishing its goals efficiently and that appropriate internal controls are operating. A peer review provides management with feedback on the Division's compliance with Internal Auditing Standards and identifies areas for improvement within the internal audit function.

Recommendation: We recommend that the Division perform and use an annual risk assessment of significant issues as a basis for the annual audit plan. Financial and EDP control issues should be considered in both the risk assessment and the formation of the audit plan. The Division should also participate in an internal audit peer review.

Management's Response: The Agency concurs with this finding. The 1994-95 internal audit plan was developed based on a risk assessment instrument; however, that instrument has not been formally revised on an annual basis. The risk assessment instrument was developed several years ago in order to create a five-year audit plan as recommended by the State Auditor's Office at that time. Areas that were initially identified as high risk, plus those areas specifically brought forward to the Internal Audit Division as needing immediate attention, are taken into consideration in developing the internal audit plan each year. Internal Audit adjusts for any changes that have taken place in the Agency's organization and believes that the results of the initial risk assessment remain valid. Those areas rated as the highest risk are being included in the internal audit plan. Although the 1995 audit plan appears to contain limited financial and EDP audits, this may not be entirely accurate. Internal audit is heavily involved in the development of new systems, including a new financial management system, and modifications of existing systems at the Agency. In addition, EDP systems existing within an audited division are examined as part of the audit.

The Internal Audit Division is currently working on revising its risk assessment instrument. The internal audit plan for fiscal year 1995-96 will be based on this revision. The Division will re-evaluate the risk assessment annually. The Internal Audit Division will undergo a peer review by August 31, 1995.

Federal Compliance Issues

Recommendations addressed in other sections of this report *could* impact controls over federal funds, especially for the Agency's most significant federal programs administered by the U.S. Department of Education.

Federal Compliance Issue 1:

Ensure Accuracy Of Time Reports

(Prior Audit Issue)

Time reports used for allocating administrative expenditures between state and federal programs were not accurate. Three of five divisions tested did not submit accurate June 1994 time reports due to mathematical errors and an incorrect time charge.¹ In addition, supervisory review and approval, which is required by the operating procedures, was not performed by three of the five divisions.

As a result, allocations of expenditure variances between programs were not accurate. State funds are unnecessarily *used* when federal programs are undercharged. If the federal funds are overcharged, then the State must repay the Federal Government.

The *allocation* system identifies variances between budgeted and actual expenditures. The system processes approximately \$2.2 million of administrative expenditures annually.

The *time* report errors were caused by a lack of proper review and verification of the reports before submission and a lack of adherence to Agency operating procedures.

Recommendation: We recommend that Agency employees adhere to operating procedures on time reports and that these reports be reviewed by management before submission. In addition, the Agency's Internal Auditor should perform an audit of one month of time reports for each division to verify their accuracy and ensure adherence to operating procedures.

Management's Response: *TEA implemented its new automated time and effort reporting system. During August 1994, all employees who were subject to time and effort reporting procedures received instructions on how to use the new system along with a brief exam testing their knowledge about those procedures. The system is currently in use for recording of all work subject to time and effort. Use of this system will eliminate routine math errors. The agency's Technology Support Division will add to its curriculum a course on the new automated system for future instruction.*

¹ The three divisions were Technology Services, Office of Education of Special Population and Adults, and Accreditation.

Operating procedures were put into place to explain all responsibilities of management and each employee. The problems in lack of proper review and verification have been addressed in the new system that spells out an approval sequence for each division to follow, including required electronic approval by a division manager. Failure to complete the approval process in the proper order within established time deadlines will trigger non-compliance reports alerting management of delinquent divisions.

Management will review the possibility of periodic training updates to agency personnel to eliminate incorrect time charges. The Internal Audit Division will study the feasibility of performing annual audits of one month of time reports for each division. Changes to the Internal Audit Plan are subject to management and Board priority. It should also be noted that because fiscal year 1995 is already in progress, the time needed to complete audits of each division may not be available.

Federal Compliance Issue 2:

Conduct Timely Reviews For All Subrecipient Audit Reports

(Prior Audit Issue)

Although the Texas Education Agency has made substantial improvements in the report resolution process, it does not conduct timely reviews of all subrecipient audit reports. As a result, the Agency cannot *ensure* that all subrecipient audit findings are resolved within the required time. Delayed reviews could result in the Agency being unaware of noncompliance by subrecipients.

Seven of 45 *audit* reports tested were not reviewed in a timely manner. The reports were reviewed six months past the report receipt date. *The Office of Management and Budget Circular A-128* requires the Agency to review audit reports for adequacy and determine whether subrecipients have taken corrective action on audit findings within six months after report receipt.

The *subrecipients* receive federal funding from the following federal programs: *School Breakfast (CFDA 10.553), National School Lunch (CFDA 10.555), Chapter 1 - Local Education Agencies, Migrant Education - Basic State Formula (CFDA 84.011), Special Education State Grants (CFDA 84.027), Vocational Education - Basic Grants to States (CFDA 84.048), Improving Schools (CFDA 84.151), and Drug-Free Schools and Communities (CFDA 84.186).*

Recommendation: We recommend that the Agency continue its efforts to conduct timely reviews for all subrecipient audit reports.

Management's Response: *The School Financial Audits Division has continued to make modifications to the procedures implemented last year to the audit review process. These modifications call for the review of all audit reports within three months of receipt, thereby leaving three months for follow-up of instances of subrecipient non-compliance. We anticipate this year, barring unforeseen circumstances, being in full compliance with The Office of Management and Budget Circular A-128 requirements.*

Federal Compliance Issue 3:

Improve Procedures For Reporting *Federal* Pass-through Funds

The Agency materially understated the amount of federal funds passed through to school districts on the Schedule of Federal Financial Assistance in the 1994 Annual Financial Report by \$52.9 million. This misstatement occurred because the Agency did not record all federal expenditures by the school districts as of August 31, 1994.

The Comptroller's Reporting Guidelines require all federal program funds expended by subrecipients during the state fiscal year to be reported as pass-throughs by the granting state agency. This includes the costs incurred by subrecipients which are not yet recorded by the state agency as of the end of the fiscal year.

Recommendation: We recommend that the Agency's Accounting Division improve its procedures for determining school district federal *expenditures* as of August 31. This will help ensure that federal pass-throughs are accurately reported. Because of the difficulty in receiving expenditure reports from school districts within the time frames necessary to prepare the annual financial report, the Agency should consider using estimates based on budgeted amounts.

Management's Response: *The Agency Accounting Division must rely on the program divisions for school districts' expenditure reports which are received and reviewed by TEA program divisions before being recorded in the accounting system.*

The problem is that all final expenditure reports are due to TEA on August 15 or later, and all divisions involved do not have enough time during August and September to process all final expenditure reports, settle payments, calculate the carryover amounts for all new projects, and also begin flowing funds to school districts in September.

We will follow the State Auditor's recommendation that future reports be prepared using estimates based on budgeted amounts.

Audit Scope

The primary focus of our audit was the Agency's financial and administrative controls over the nine major federal programs which disbursed \$1.5 billion in fiscal year 1994. We gained an understanding of the internal control structure, including the general control environment and tested controls related to the federal programs. Specific procedures were used to test compliance with the major federal program requirements.

Financial accounts significant to the statewide financial statements were also tested. These accounts include Investments, \$8.5 billion; Purchases of Investments, \$1 billion; Sales of Investments, \$613 million; Education Expenditures, \$7.6 billion; Transfers In, \$6.8 billion; and Revenues from Licenses, Permits and Fees, \$336 million.