

**REPORT ON THE
EXTERNAL QUALITY ASSURANCE REVIEW
OF THE
TEXAS COUNCIL FOR DEVELOPMENTAL DISABILITIES
INTERNAL AUDIT FUNCTION**

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PERFORMED BY

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Performed in accordance with the
Texas State Agency Internal Audit Forum
Peer Review Policies and Procedures

OVERALL OPINION

Based on the information received and evaluated during this external quality assurance review, it is my opinion that the Texas Council for Developmental Disabilities Internal Audit function “**fully complies**” with:

- the Institute of Internal Auditors (IIA) *International Professional Practices Framework* including the *International Standards for the Professional Practice of Internal Auditing*, the *Definition of Internal Auditing*, and the *Code of Ethics*,
- the United States Government Accountability Office (GAO) *Government Auditing Standards*, and
- the Texas Internal Auditing Act (*Texas Government Code*, Chapter 2102).

This opinion means that there are relevant structures, policies, procedures, and processes in place that comply with the requirements of both the IIA and GAO standards, and the Texas Internal Auditing Act in all material respects. Any deviations found between the professional standards and the TCDD policies, procedures, and practices, or the work performed by the contractor, were judged to be insignificant.

I found that the Internal Audit function is independent, objective, and able to render impartial and unbiased judgments on the audit work performed. The Internal Auditor is qualified, proficient, and knowledgeable in the areas she audits. Individual audit projects are planned using risk assessment techniques; audit conclusions are supported in the working papers; and findings and recommendations are communicated clearly and concisely.

Interviews conducted during the peer review indicate that TCDD management and the Council consider Internal Audit a useful part of the overall operations and find that the audit process and report recommendations add value and help improve the organization.

ACKNOWLEDGEMENTS

I appreciate the courtesy and cooperation extended to me by the TCDD and especially those persons who participated in the interview process: the TCDD Chair (who recently served as the Audit Committee Chair), the Executive Director, the Operations Director, the Grants Management Director, the Operations Coordinator, and the Internal Auditor. The feedback from the interviews and the comprehensive self assessment provided valuable information regarding the operations of the Internal Audit function and its relationship with TCDD management, the Audit Committee, and the Council.

David J. MacCabe, CIA, CGAP, MPA
Peer Reviewer

Date

BACKGROUND

The Texas Council for Developmental Disabilities (TCDD) is a 27-member board dedicated to ensuring that all Texans with developmental disabilities, about 437,885 individuals, have the opportunity to be independent, productive and valued members of their communities. Using a variety of methods, the Council works to:

- Ensure that the service delivery system provides comprehensive services and supports that meet people's needs, are easy to access and are cost effective
- Improve people's understanding of disability issues

Texas state government internal audit functions are required to obtain external quality assurance reviews to appraise the quality of their operations and to assess compliance based on the following requirements:

- the Institute of Internal Auditors (IIA) *International Professional Practices Framework* including the *International Standards for the Professional Practice of Internal Auditing*, the *Definition of Internal Auditing*, and the *Code of Ethics*,
- the United States Government Accountability Office (GAO) *Government Auditing Standards*, and
- the Texas Internal Auditing Act as codified in the *Texas Government Code*, Chapter 2102.

The TCDD has contracted with the firm of Rupert and Associates, P. C., Certified Public Accountants (the Contractor) to conduct internal audit projects for the past seven years. Ms. Jaye Stepp, a Certified Public Accountant and Certified Government Auditing Professional with the accounting firm, has the primary responsibility for planning and performing Internal Audit work.

A periodic external quality assurance review, or peer review, of the internal audit function is an essential component of a comprehensive quality assurance and improvement program. The *Government Auditing Standards* require external peer reviews be conducted at least every three years. This quality assurance review project was performed in accordance with guidelines published by the Texas State Agency Internal Audit Forum (SAIAF).

A previous peer review for the TCDD Internal Audit function was completed in June 2006 by a nationally-recognized Internal Audit consultant using SAIAF guidelines. The TCDD successfully implemented the three recommendations made in the report of the previous quality assurance review.

This external review was performed during the period July 15-22, 2009 by an Internal Audit consultant who is a Certified Internal Auditor, previously served as a Chief Audit Executive for 27 years, and obtained the IIA's Certification in Internal Quality Assessment/ Validation.

The IIA has defined a five-level “Path to Quality” that illustrates that Internal Audit quality is achieved over time. The IIA believes that achieving quality requires the understanding not only by those performing internal auditing but also by audit customers and those responsible for Internal Audit oversight.

The quality model provides a framework for the Internal Auditor to assess the current state, target an appropriate level of quality capability for the future, and lay out the steps along a path to reach the function’s quality capability target. Additional information on this quality model for internal auditing may be found at: <http://www.theiaa.org/guidance/quality/the-external-quality-assessment-process/path-to-quality/>

OBJECTIVES, SCOPE, AND METHODOLOGY

The primary objective of the quality assurance review was to evaluate the agency Internal Audit function’s compliance with auditing standards and the *Texas Internal Auditing Act*. Additional objectives of the review included identifying leading practices as well as areas where improvement may be needed.

The review focused on Internal Audit work activities performed during the period July 2007 through June 2009.

The quality assurance review methodology included:

- Review of the June 2006 quality assurance peer review conducted by a nationally-recognized internal audit consultant using SAIAF criteria,
- Review, verification, and evaluation of the self-assessment documentation prepared by the Internal Auditor according to SAIAF guidelines,
- Interviews with the TCDD Chair (and former Audit Committee Chair), the Executive Director, the Operations Director, the Operations Coordinator, the Grants Management Director, and the Internal Auditor,
- Review and evaluation of the FY 2008 Internal Audit project working papers, and
- Review of the TCDD annual risk assessment, the *FY 2009 Audit Plan*, the *FY 2008 Annual Internal Audit Report*, the *Rupert & Associates Internal Audit Procedures Manual*, and other relevant documents.

DETAILED RESULTS

The results of the quality assurance review for the TCDD Internal Audit function are presented in the order listed in the IIA's *International Standards for the Professional Practice of Internal Auditing*.

No significant weaknesses were identified during the review that would prevent the TCDD Internal Auditor from fulfilling her responsibilities. The detailed results include identification of leading practices as well as some opportunities for improvement that the Internal Audit function may wish to consider.

IIA Code of Ethics

Internal Audit demonstrates its commitment to the IIA *Code of Ethics* by including it in the Rupert and Associates *Internal Audit Procedures Manual*, attending periodic ethics training classes, and practicing ethical behavior in the course of audit work. In addition, the Council's *Conflict of Interest Disclosure Policy* provides an indication of an organization-wide commitment to accountability, integrity, and good governance.

Standard 1000: Purpose, Authority, and Responsibility

The purpose, authority, and responsibility of Internal Audit have been defined in a charter that is generally consistent with internal auditing standards. The charter defines the purpose, authority and responsibility for Internal Audit services and grants unrestricted access to agency records, property, and personnel. The current charter was signed by the TCDD Audit Committee Chair, the Executive Director, and the Internal Auditor in October 2007.

A draft revision to the charter incorporating recent changes to the *IIA Standards* has been developed and will be considered at the August 2009 Audit Committee meeting. During the course of this engagement, the peer reviewer has provided some informal suggestions to the Internal Auditor for consideration in the charter revision.

Among the suggestions were the inclusion of (1) Definition of Internal Auditing, (2) information on assurance and consulting services, and (3) the Council Chair's approval signature on the Internal Audit Charter signifying approval and support by the full Council. The Internal Auditor was receptive to the suggestions and these changes were included in the proposed revision to the Internal Audit Charter.

Section VII. D. of the TCDD Policies describes Audit Committee Duties related to the Internal Audit Charter, the Annual Audit Plan, audit reports, and special audits. The IIA Model Audit Committee Charter includes additional responsibilities that are typically included in such charters.

Opportunity for Improvement 1 – Consider the Revision of the Audit Committee Charter to Include Other Typical Responsibilities

It is suggested the Audit Committee and the Council consider the following responsibilities that are typically assigned to Audit Committees and include those that are appropriate to the TCDD in the Audit Committee Charter:

- Assist the Council in fulfilling its oversight responsibilities for the financial reporting process, the system of internal control, the audit process, and the Council's process for monitoring compliance with laws, regulations, TCDD policies such as the Conflict of Interest Disclosure Policy
- Provide recommendations to the Council on securing or renegotiating contract internal audit services.
- At least once per year, review the effectiveness of the contract internal audit function, including compliance with The Institute of Internal Auditors' *International Professional Practices Framework for Internal Auditing* consisting of the *Definition of Internal Auditing*, the *Code of Ethics* and the *Standards*.
- Review with management and the auditors all matters required to be communicated to the Committee under generally accepted auditing *Standards*.
- Understand the scope of internal and external auditors' review of internal control over financial reporting, and obtain reports on significant findings and recommendations, together with management's responses.
- Understand how management develops interim financial information, and the nature and extent of internal and external auditor involvement.

Internal Audit Response:

The Audit Committee and the Council approved suggested revisions to the TCDD Internal Audit Charter at their meetings held August 7th and 8th, 2009. As noted, Section VII.D. of the TCDD Policies specify the responsibilities of the Audit Committee. The Audit Committee will review proposed revisions to that section of Policies at its next meeting, including the suggestions noted above.

Standard 1100: Independence and Objectivity

The Internal Audit function is independent both in terms of the Council's organizational structure and Internal Audit practices. The Internal Auditor reports directly to the TCDD Audit Committee which provides sufficient authority to promote independence and to ensure adequate consideration of audit reports and appropriate action on audit issues and recommendations.

The Internal Audit Charter helps ensure continued independence by specifying that internal auditors must remain free of operational and management responsibilities that could impair their ability to make independent reviews of all areas of the agency's operations. The Internal Auditor is an independent contractor and has had no prior responsibilities for any areas that the function audits. In addition, the Internal Auditor is required to sign Independence and Objectivity Statements for each audit performed.

Standard 1200: Proficiency and Due Professional Care

The Internal Auditor possesses the knowledge, skills, and abilities to perform assigned responsibilities. She is a Certified Public Accountant (CPA) and Certified Government Auditing Professional (CGAP). She enhances her knowledge, skills, and abilities by obtaining at least 40 hours of continuing professional education each year. At least two other members of the Rupert & Associates firm could serve as backups to the Internal Auditor if deemed necessary.

Standard 1300: Quality Assurance and Improvement Program

The Internal Auditor has implemented a quality assurance and improvement program to help ensure that Internal Audit adds value and improves the agency's operations and to provide assurance that the Department complies with *Standards* and the *IIA Code of Ethics*. The quality assurance program involves managing partner review of draft audit products and periodic external peer reviews, the results of which are communicated to the Audit Committee and the Council and subsequently made available to oversight agencies. Internal Audit is considering the use of business partner surveys after each audit. Audit reports include an appropriate reference that audit work was performed in accordance with the *Standards*.

Standard 2000: Managing the Internal Audit Activity

The Internal Auditor conducts an annual risk assessment that forms the basis for the Annual Audit Plan, which is reviewed and approved by the Audit Committee and the Council. Internal Audit reports address risk and control issues within the agency. The Internal Auditor has developed policies and procedures to guide the audit activity. The Auditor reports the Internal Audit function's performance relative to the Annual Audit Plan in the *Annual Internal Audit Report* submitted to Council members, the TCDD Executive Director, the Governor's Office, the Legislative Budget Board, and the State Auditor.

The following audit assurance projects have been completed during the past two fiscal years:

- Grantee Audit Desk Review Process (2008)
- Internal Controls over Financial Reporting to the Council (2008)
- Grantee Records Management Process (2008)
- Grantee Monitoring Onsite Review Process (2007)
- Internal Administrative Operating Procedures (2007)
- Grantee Reporting Database Development-DDS Suite (2007)

Standard 2100: Nature of Work

Internal Audit evaluates risks related to financial and operating information as well as the effectiveness and efficiency of operations, safeguarding of assets, and compliance with laws and regulations. The function also evaluates the extent to which operating and program objectives have been achieved.

The Internal Auditor contributes to the organization's governance, risk management and control processes by providing information and assistance to Executive Management and the Council about how the accomplishment of goals are monitored and how accountability is ensured. This was done in the past year primarily through the Internal Auditor's application of Control Self Assessment (CSA) techniques in the audit risk assessment activities that were the basis for the FY 2009 Internal Audit Plan.

IIA Standard 2110 pertaining to governance states “The internal audit activity must assess and make appropriate recommendations for improving the governance process in its accomplishment of the following objectives:

- Promoting appropriate ethics and values within the organization;
- Ensuring effective organizational performance management and accountability;
- Communicating risk and control information to appropriate areas of the organization; and
- Coordinating the activities of and communicating information among the board, external and internal auditors, and management.”

IIA Standard 2110A.1 further requires that “The internal audit activity must evaluate the design, implementation, and effectiveness of the organization’s ethics-related objectives, programs, and activities.”

Projects undertaken by other Internal Audit activities to meet this requirement include

- Conducting an employee ethics survey
- Review of employee and Council/Board member filing of required declarations regarding awareness of ethics policy and requirements for advising of actual or potential conflicts of interest
- Reviewing Board/Council member compliance with Texas Ethics Commission filing requirements.
- Assisting in designing and/or delivering ethics training sessions for staff and Council/Board members
- Review of human resource policies pertaining to reference and background checks as part of the hiring procedures.

Opportunity for Improvement 2 – Plan Future Internal Audit Projects Evaluating Organizational Governance

The Internal Auditor should incorporate the evaluation of ethics and governance into future audit projects.

Internal Audit Response:

The Internal Auditor agrees with this suggestion and will incorporate the evaluation of ethics and governance into future audit projects as appropriate. TCDD executive staff have also embraced the importance of ethics and fraud prevention by incorporating appropriate guidance in appropriate staff operating procedures including TCDD OP 02-02: TCDD Standards of Conduct and Conflicts of Interest and TCDD OP 02-04: TCDD Fraud Prevention Policy. The auditor reviewed and provided input to TCDD while those items were under development.

Standard 2200: Engagement Planning

During planning, the Internal Auditor considers the objectives of the activity being reviewed and the related risks and controls. Resources needed for each audit are adequately considered during planning. Project risk assessments are used to develop the objectives of each audit. Interviews conducted during the quality assurance review indicated that the objectives of audits are clearly communicated to business partners. An Audit Program is developed and documented for each audit. The scope of audits is adequately planned and documented in planning documents and audit reports.

Standard 2300: Performing the Engagement

The Internal Auditor evaluates and documents sufficient, reliable, and relevant information to achieve their audit objectives. Results and conclusions are based on analysis. The Rupert & Associates *Internal Audit Procedures Manual* contains excellent guidance on the planning, field work, working paper standards, reporting, and wrap-up phases of an audit project.

Audits are planned and conducted by the Internal Auditor and audit work is overseen by a senior partner at Rupert & Associates. The Internal Auditor conducts planning meetings, prepares appropriate control documents, and documents interviews, observations, and record reviews in the working papers to ensure the sufficiency of evidence and compliance with *Standards*.

Some minor improvements in workpaper techniques would be beneficial to more fully comply with this standard and the *Internal Audit Procedures Manual*. Specific examples were provided to the Internal Auditor including consistency in labeling workpapers and double checking to ensure all necessary documents are included.

Standard 2400: Communicating Results

Audit results are communicated in a timely manner. Potential findings are communicated during the audits thus providing management the opportunity to provide additional information and/or to initiate corrective action. Audit results are presented to management before they are finalized in a report helping to ensure there is agreement about the areas for improvement and the recommended solutions.

Audit reports contain the audit objectives, results, conclusions, recommendations, and management's responses and action plans. TCDD management and the Council Chair indicated in interviews with the peer reviewer that Internal Audit reports are accurate, objective, clear, concise, and complete. The Internal Auditor distributes reports to the Audit Committee and to management. Internal Audit reports are shared with oversight agencies after review by the Council.

Standard 2500: Monitoring Progress

TCDD developed a more complete system for monitoring the disposition of Internal Audit issues and recommendations in response to the 2006 peer review. The status of management's progress in implementing audit recommendations is periodically reported to the Audit Committee and the Council and provided to management.

IIA Standards require that the Internal Auditor "must establish a follow-up process to monitor and ensure that management actions have been effectively implemented or that senior management has accepted the risk of not taking action." The Internal Auditor is planning to conduct a follow-up project this fiscal year to determine the status of outstanding audit recommendations and report to management and the Audit Committee.

Standard 2600: Management's Acceptance of Risks

During the quality assurance review, no instances were identified of management accepting an inappropriate level of risk that would require the Auditor to notify the Audit Committee and Council.

COUNCIL MEMBER AND MANAGEMENT COMMENTS

The Council Chair, the Executive Director, and three other TCDD staff members interviewed were very complimentary of the internal audit services provided by Rupert and Associates through Ms. Jaye Stepp, the Internal Auditor. The following are representative comments from the persons interviewed:

“Jaye has very good communication skills and is direct, clear, and honest. She is clearly a 10 out of 10 point scale in professionalism.”

“The internal auditor is competent, capable, and knowledgeable about Council activities. I am comfortable with the quality of work and independence demonstrated by the auditor”

“I have a high comfort level with the Rupert accounting firm and Jaye as our auditor. I do have some concerns about an extended relationship with any given audit firm. There may be value in changing auditors periodically from the standpoint of prudence.”

“Our meetings with Jaye on risk assessment are beneficial and usually cause good discussion and some modifications. We consider risk probabilities, impacts and worse case scenarios in deciding future audit projects.”

“Jaye reports directly to the Council and the Audit Committee but is someone we can meet with and discuss problems while she maintains her independence from management.”

“The auditor has gone through the entire operation with a fine tooth comb including the complexities associated with our payment methodology with TEA as the designated state agency.”

“We are up for Sunset Commission review in 2013 and Internal Audit helps us prepare by showing us where there may be shortcomings.”

“Jaye is responsive – when we write, call, or send an email message we get a fairly responsive answer on a timely basis.”

LEADING PRACTICES

The Internal Audit function is dedicated to continuous improvement. During the quality assurance review, I observed a number of practices that demonstrate outstanding commitment and professionalism. These leading practices include the following:

- The TCDD management team is very knowledgeable and supportive of the role of Internal Audit in helping ensure an appropriate control environment.
- The Rupert & Associates firm and the Internal Auditor are very knowledgeable about the Council authority, responsibilities, and personnel and have assisted the organization in considering governance, risk management, and control issues and concerns. More specifically, the Internal Auditor made recommendations that led to management implementing some procedures relating to grantee audits and risk assessments that strengthened accountability and oversight.
- Internal Audit details its audit engagement planning process in a comprehensive manner to include the identification of potential risks, testing methodology, preliminary interviews, and audit objectives and scope.
- The Internal Auditor through Rupert & Associates has developed the *Internal Audit Procedures Manual*, an excellent guide that helps the current and future auditors comply with *Standards* and results in more consistent audit practices.
- The Internal Auditor is professional and proficient. Jaye is a Certified Internal Auditor and a Certified Government Auditing Professional. Managers stated in interviews that the Internal Auditor is a competent professional who understands and is committed to the Council's mission.
- The Internal Auditor has obtained more than the mandated 80 hours of continuing professional education for a two-year period provided by local professional auditing organizations including the State Auditor's Office (SAO), the IIA Austin Chapter, the Texas Society of Certified Public Accountants (TSCPA), and the Texas State Agency Business Administrators Association (TSABAA).
- The Internal Auditor is active and well respected in local professional organizations including the SAIAF and the IIA Austin Chapter.

REPORT DISTRIBUTION

Ms. Brenda Coleman-Beattie, Chair, Texas Council for Developmental Disabilities

Ms. Mary Durham, Chair, Audit Committee

Mr. Roger Webb, Executive Director

Mr. Carl Risinger, Operations Director

Ms. Patrice LeBlanc, Grants Management Director

Ms. Martha Cantu, Operations Coordinator

Ms. Jaye Stepp, CPA, CGAP, Internal Auditor (Rupert & Associates)