

TEXAS HIGHER EDUCATION COORDINATING BOARD

INTERNAL AUDIT ANNUAL REPORT



FOR

FISCAL YEAR 2018

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Compliance with Texas Government Code, Section 2102.015

Texas Government Code, Section 2102.015 requires state agencies to post on the agency's Internet Web site its internal audit plan, internal audit annual report, and any weaknesses or concerns resulting from the audit plan or annual report. Please see the [Coordinating Board internet web site](#) and the "Internal Audit and Compliance Monitoring" tab under 'About Us' for this required information. The 2018 Internal Audit Annual Report will be posted following its presentation to the board in October, 2018.

The screenshot shows a web browser window displaying the THECB website. The address bar shows the URL: <http://www.thecb.state.tx.us/index.cfm?objectid=C22D5880-1738-11E8-A6640050560100A9>. The browser has several tabs open, including 'CBNet', 'For Internal Audi...', 'Texas State Audit...', and 'THECB - Inter...'. The website's navigation bar includes links for 'Plan, Pay, & Complete College', 'Institutional Resources & Programs', 'Data & Reports', 'Legislative & Media Resources', and 'About Us'. A search bar is located on the right side of the navigation bar. The main content area is titled 'Internal Audit & Compliance Monitoring' and contains the following sections:

- Internal Audit Charter**
The Internal Audit Charter defines Internal Audit's purpose, authority, and responsibility as approved by the agency's governing board.
- Report Fraud**
The Texas Higher Education Coordinating Board along with its Stakeholders, are responsible for protecting the assets and resources of the agency, and its programs. To accomplish this, Stakeholders are encouraged to report factual information suggestive of dishonest or illegal activities involving the agency and its programs.
- Annual Internal Audit and Compliance Monitoring Plans**
The Annual Internal Audit Plan and Annual Compliance Monitoring Plan are reports of scheduled audits by process or location that are developed each year based on a comprehensive risk assessment. These plans are approved annually by the agency's governing board.
- Annual Internal Audit Reports**
The Texas Internal Auditing Act requires certain state agencies and higher education institutions to submit an internal audit annual report each year to the Governor, the Legislative Budget Board, the Sunset Advisory Commission, the State Auditor's Office (SAO), and the entities' governing boards and chief executives.
- Internal Audit Reports**
An Internal Audit report is a formal document where Internal Audit summarizes audit results and reports its findings and recommendations based on that work.
- Compliance Monitoring Reports**
A Compliance Monitoring audit report is a formal document where Compliance Monitoring summarizes audit or desk review results and reports its findings and recommendations based on that work.

Inquiries should be directed to Mark.Poehl@thecb.state.tx.us.

Internal Audit Plan for Fiscal Year 2018

Explanatory Information - The table below indicates the status of FY 17 planned audits, as shown on the approved audit plan, versus those accomplished during the year.

Board-Approved FY 18 Audit Plan	Status of Audit at 8/31/18
Follow Up Audits	(1) Follow Up Audit of Data Administration and Governance: Planned to start in Fiscal Year 2019. (2) Follow Up Audit of Contract Management: Planned to start in Fiscal Year 2019. (3) Follow Up Audit of Texas Educational Opportunity Grant (TEOG) Administration: Planned to start in Fiscal Year 2019.
Self-Assessment of Work Quality, Internal Audit	Self-Assessment of Work Quality THECB-IA-WP-18-199 Report date September 12, 2017.
An Audit of Formula Funding	An Audit of Formula Funding THECB-IA-WP-18-201 Report date June 19, 2018.
Review of the Physician Education Loan Repayment Program	Review of Physician Education Loan Repayment Program THECB-IA-WP-18-204 Report date August 21, 2018.
Review of Contract Management Administration	Review of Contract Management Administration Planned to start in Fiscal Year 2019.

Consulting Engagements and Non-Audit Services Completed

The Texas Higher Education Coordinating Board internal audit function did not perform consulting or non-audit services in fiscal year 2018.

External Quality Assurance Review (Peer Review)

G Shemo Consulting Inc.
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REPORT ON THE EXTERNAL QUALITY ASSESSMENT OF

**TEXAS HIGHER EDUCATION
COORDINATING BOARD**

INTERNAL AUDIT and COMPLIANCE DEPARTMENT

September 28, 2016

Overall Opinions on Conformance

September 20, 2016

Under a contractual agreement with the Texas Higher Education Coordinating Board (THECB), G Shemo Consulting Inc. (GSC) has conducted an independent External Quality Assessment (EQA) of the THECB Internal Audit activity (IA activity) in the Internal Audit and Compliance Department (IACD).

The review was conducted during the period of September 12, 2016 to September 20, 2016 at the offices of THECB in Austin, Texas. This EQA was conducted as required by the Institute of Internal Auditors' (IIA) *Standard 1312*, in accordance with the approach and procedures contained in the IIA "Quality Assessment Manual" (Issued August 1, 2013). Further, this EQA included a Peer Review of IA activity conformance with applicable GAO Standards, and was conducted according to the requirements contained in GAO Standards 3.96 to 3.107. Finally, this EQA included an assessment of IA activity compliance with the requirements of the Texas Internal Auditing Act.

GSC attests that it is fully qualified to conduct this EQA of the IA activity, and that GSC is independent in all respects to THECB and the IACD. Based on the results of this EQA, GSC has reached the following conclusions:

In regard to the IIA Standards:

It is our overall opinion that, as of September 15, 2016, the THECB IA activity "Generally Conforms" to the IIA *Standards*, the Code of Ethics, and Definition of Internal Auditing. "Generally Conforms" is the top rating provided within IIA QA guidance, with the others being "Partially Conforms" and "Does Not Conform". For a detailed list of conformance to individual IIA *Standards*, please see Attachment A. The QA team has identified opportunities for further enhancing the IA activity, details of which are provided in this report.

In regard to the GAO Standards:

It is our overall opinion that the THECB IA activity's QAIP was suitably designed and complied with, for the year ended August 31, 2016, in order to provide reasonable assurance of performing and reporting in conformity with applicable GAO standards in all material respects. Accordingly, in our opinion, the appropriate Peer Review Rating for the IA activity is "Pass". This rating is the highest of the three ratings provided within GAO Standards, with the other ratings being "Pass With Deficiencies", and "Fail". For a detailed list of conformance to individual GAO *Standards*, please see Attachment B.

In regard to the Texas Internal Auditing Act:

It is our overall opinion that, as of September 15, 2016, the IA activity conforms to all the requirements contained within the Texas Internal Auditing Act.



George J Shemo, CPA, CGMA
 President, G Shemo Consulting Inc.

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Executive Summary

Purpose

As requested by the Director, Internal Audit and Compliance (DIAC), G Shemo Consulting conducted an external EQA of the IA activity of THECB. The principal objectives of the EQA were to:

- Assess IA activity conformance to the IIA “Definition of Internal Auditing”, the *International Standards for the Professional Practice of Internal Auditing (Standards)*, and the Code of Ethics;
- Assess IA activity conformance to applicable GAO Standards;
- Assess IA activity compliance with the Texas Internal Auditing Act;
- Evaluate IA activity effectiveness in carrying out its mission, as set forth in its charter and expressed in the expectations of the THECB Agency Operations Committee (AOC) and senior management;
- Identify opportunities to enhance IA activity management and work processes, as well as its ability to add value to THECB.

Scope and Methodology

Prior to GSC arriving onsite at THECB to conduct the EQA, the DIAC provided advance preparation documents, which contained detailed information about the IA activity and THECB. Additionally, GSC conducted a preliminary meeting with the DIAC in order to gather additional background information, select executives and operating managers for interviews during our onsite field work, and to finalize planning and administrative arrangements for the EQA. Onsite fieldwork commenced on September 12, 2016 and concluded on September 20, 2016.

During the onsite fieldwork we conducted interviews with the Chair of the AOC, members of senior management, selected operating managers, a representative of the external CPA firm, and all members of the IA activity staff. We also evaluated the IA activity risk assessment and audit planning processes, audit tools and methodologies, engagement and staff management processes, and a representative sample of the IA activity work papers and reports.

We conducted the QA according to the IIA and GAO guidelines and procedures that were necessary to evaluate the following components of the IA activity:

- Director Reporting Lines and Quality Assurance
- Organization of the Audit Activity
- Communications with the AOC and Senior Management
- Risk Assessment and Engagement Planning
- Staff Professional Proficiency
- Information Technology Capabilities
- Productivity and Value Added to THECB
- Audit Engagement Work Papers and Reports
- Audit Tools and Methodologies
- Engagement and Staff Management Processes

Executive Summary

Summary of Recommendations for Conformance

Based on the results of this EQA, no issues affecting conformance, with either the IIA or GAO Standards, or compliance with the Texas Internal Auditing Act were found, and therefore, no recommendations are provided.

Summary of Recommendations for Enhancement

The following recommendations are identified as potential opportunities to enhance the IA activity ability to add value to THECB:

1. Broaden senior management's expectations for IA activity services
2. Increase AOC involvement in evaluating performance of the DIAC
3. Expand the Quality Assurance and Improvement Program (QAIP)
4. Enhance the IA activity Annual Planning Process

Commendations

During our review, we observed the IA activity environment to be well-structured and progressive; that the IIA Standards, the GAO Standards, and the requirements of the Texas Internal Auditing Act are appropriately understood; and IA activity management is endeavoring to provide useful audit tools and implement appropriate practices in order to add value to the operations of THECB. It is appropriate to commend the IA activity for the following:

- Results of this EQA are well above average relative to other EQAs performed throughout the profession
- Excellent relationship with and strong support from the AOC and executive management
- DIAC is recognized for leadership, experience, integrity, guidance, and emphasis on continuous improvement
- Staff is viewed positively for their professionalism, knowledge, demeanor, willingness to listen, and well written reports; and
- Competent and experienced staff with 12 professional certifications and five graduate degrees
- IA and Compliance viewed as adding value to THECB on a collaborative basis
- Annual visitation with key stakeholders soliciting input and ideas for the annual risk assessment
- IA and Compliance is instrumental in THECB risk management
- Embedding audit steps and procedures within the TeamMate audit software program
- IA activity maintains a publicly accessible website providing relevant information which promotes transparency

Recommendations for Enhancement

- 1. Consider broadening senior management's expectations for IA activity services and expand the scope of those services to increase focus on THECB governance and business processes**

**Implementing Stakeholders: Senior Management
Agency Operations Committee
IA activity**

Associated Stakeholder: Operating Management

Successful Practice

Related Practice Advisories: 2110-1, 2110-2, 2110-3

This EQA has determined that the DIAC has implemented a program of internal auditing that fully meets the AOC and senior managements' formally established expectations in a highly effective manner. Currently, those expectations focus on assurance services related to the control environment and compliance with the policies and procedures of THECB. As a result of the discussions with senior and operating management during the EQA interviews, there appears to be considerable interest in having the IA activity increase services that are more focused on process improvement. While current IA activity services do provide some elements of process improvement, the formal scope of services would need to be expanded to meet increased expectations.

Accordingly, senior management, the Agency Operations Committee, and the DIAC could consider the opportunity to formally increase expectations of expanded IA activity services. Such consideration would need to be viewed in light of recommendation #4 regarding a more in depth evaluation of Internal Audit resource requirements. Some elements of an expanded scope of services could include:

- The economic and efficient use of resources
- Performance measurement
- Business process improvement
- Administrative process improvement
- THECB governance processes

Recommendations for Enhancement

2. Increase AOC involvement in evaluating performance of the DIAC

Implementing Stakeholders: Senior Management

Agency Operations Committee

Associated Stakeholder: DIAC

Reference: Practice Advisory 1110-1

The structure of the functional and administrative reporting relationships of the IA activity within THECB is entirely appropriate, and achieves complete independence for the IA activity. It establishes the proper environment to allow the IA activity to effectively support THECB in fulfilling its mission and achieving its goals and objectives, in line with senior management's expectations. As a result of this EQA, there appears to be an opportunity to further enhance IA activity independence by increasing the responsibilities of the AOC in regard to the functional reporting relationship. The AOC could consider revising its Charter to include the following responsibilities:

- Approving all decisions regarding the performance evaluation, appointment, or removal of the DIAC.
- Approving the annual compensation and salary adjustment of the DIAC.

3. Expand the Quality Assurance and Improvement Program (QAIP)

Implementing Stakeholder: IA activity

Associated Stakeholders: Agency Operations Committee
Senior Management
Operating Management

Practice Advisories: 1311-1 and 1320-1

The DIAC has designed and implemented a fully functional QAIP which appropriately monitors and assesses IA activity performance, and its conformance with the IIA and GAO Standards, as well as the Texas Internal Auditing Act. The DIAC could increase the effectiveness of the QAIP even further by considering the following:

- Expanding the scope of periodic self-assessments to ensure that every IIA and GAO Standard is assessed at least once during a three year cycle;

Recommendations for Enhancement

3. Expand the Quality Assurance and Improvement Program (QAIP) (Cont.)

- Including the results of external assessments, internal self-assessments, and ongoing monitoring activities, as well as the resulting IA activity plans for continuous improvement, in periodic status reports to senior management and the AOC.

4. Enhance the IA activity Annual Planning Process

Implementing Stakeholder: IA activity

Associated Stakeholders: Agency Operations Committee
Senior Management
Operating Management

Practice Advisory: 2020-1

The annual planning process developed by the DIAC provides the AOC and senior management with a risk based plan that appropriately determines the priorities of the IA activity consistent with THECB's goals. The plan, as presented to senior management for their review, and for the approval of the AOC, properly communicates IA planned activities and the resource requirements needed to accomplish them. There are opportunities to further enhance annual planning by providing additional information which will provide the basis to better quantify IA resource requirements that are needed to meet the needs of THECB. For example, the DIAC could consider the following:

- Reviewing the detailed audit universe with the AOC and senior management to agree on the entities within the universe that need to be reviewed by IA at some point, over a period of time, in the future (the auditable segment), and those that do not need to be reviewed by IA at any point in the future (the non-auditable segment). Separation of the audit universe should be based upon an assessment of the THECB's need for support, not on the amount of current IA activity resources. Reviewing the audit universe in this manner needs to occur each year, as part of the annual planning process in order to determine if there is a need to shift entities between segments.
- Assessing risk of the entities within the auditable segment, and ranking the segment in risk rating order.
- Grouping the entities according to risk ratings. Establish groups consistent with AOC and senior management expectations. For instance, four groups could be established for

Recommendations for Enhancement

4. Enhance the IA activity Annual Planning Process (Cont.)

extremely high, high, moderate, and low risks. Assigning entities to the groups should be done with the agreement of the AOC and senior management.

- Establishing frequency guides for each risk group. For example: extremely high risk entities audited annually; high risk entities audited over two years; moderate risk entities over four years; and low risk entities over five years. The frequency guides should be established with the agreement of the AOC and senior management.
- Preparing an annual plan in a multi-year format. The number of years presented would be equal to the frequency guide established for the lowest risk group. It is important to note that the plan includes all entities assigned to the auditable segment of the audit universe, regardless of its risk group. The DIAC would prepare preliminary scope descriptions and resource estimates for the entities identified for audit in the upcoming year. Remaining entities would show an indication of the future year in which it is to be audited. In the example above, the upcoming year would include all extremely high risk, one-half of high risk, one-fourth of moderate risk, and one-fifth of low risk entities.

Following this approach will provide a result that specifically quantifies the IA activity resource requirements to service the needs of THECB in the upcoming year. It can serve as the basis for the AOC and senior management to make informed decisions on the quantity of IA activity resources to be provided, and the impact that any resource shortages will have on the multi-year plan.

Director Response

I have read this report in its entirety, and acknowledge responsibility for communicating it to the appropriate members of the Agency Operations Committee and senior management. I accept the "Recommendations for Enhancement" as advisory, and understand they are provided for consideration as potential opportunities to increase the value the IA activity adds to THECB. In consultation with the Agency Operations Committee and senior management, I will develop action plans as appropriate, and will share these plans with the Agency Operations Committee and senior management.



Mark Poehl

Director, Internal Audit and Compliance

THECB

Attachment A

IIA Standards

		GC	PC	DNC
OVERALL EVALUATION		x		
ATTRIBUTE STANDARDS		x		
1000	Purpose, Authority, and Responsibility	x		
1010	Recognition of the Definition of Internal Auditing	x		
1100	Independence and Objectivity	x		
1110	Organizational Independence	x		
1111	Direct Interaction with the Board	x		
1120	Individual Objectivity	x		
1130	Impairments to Independence or Objectivity	x		
1200	Proficiency and Due Professional Care	x		
1210	Proficiency	x		
1220	Due Professional care	x		
1230	Continuing Professional Development	x		
1300	Quality Assurance and Improvement Program	x		
1310	Requirements of the Quality Assurance and Improvement Program	x		
1311	Internal Assessments	x		
1312	External Assessments	x		
1320	Reporting on the Quality Assurance and Improvement Program	x		
1321	Use of "Conforms with the <i>International Standards for the Professional Practice of Internal Auditing</i> "	x		
1322	Disclosure of Noncompliance	x		
PERFORMANCE STANDARDS		x		
2000	Managing the Internal Audit Activity	x		
2010	Planning	x		
2020	Communication and Approval	x		
2030	Resource Management	x		
2040	Policies and Procedures	x		

Attachment A

IIA STANDARDS

2050	Coordination	x		
2060	Reporting to Senior Management and the Board	x		
2070	External Service Provider and Organizational Responsibility for Internal Auditing	NA		
2100	Nature of Work	x		
2110	Governance	x		
2120	Risk Management	x		
2130	Control	x		
2200	Engagement Planning	x		
2201	Planning Considerations	x		
2210	Engagement Objectives	x		
2220	Engagement Scope	x		
2230	Engagement Resource Allocation	x		
2240	Engagement Work Program	x		
2300	Performing the Engagement	x		
2310	Identifying Information	x		
2320	Analysis and Evaluation	x		
2330	Documenting Information	x		
2340	Engagement Supervision	x		
2400	Communicating Results	x		
2410	Criteria for Communicating	x		
2420	Quality of Communications	x		
2421	Errors and Omissions	x		
2430	Use of "Conducted in conformance with the International Standards for the Professional Practice of Internal Auditing"	x		
2431	Engagement Disclosure of Nonconformance	NA		
2440	Disseminating Results	x		
2450	Overall Opinions	x		
2500	Monitoring Progress	x		
2600	Management's Acceptance of Risks	x		
	IIA Code of Ethics	x		

Attachment B

GAO STANDARDS

	PASS	FAIL
GENERAL (107)	X	
Independence (59)	x	
Professional Judgment (9)	x	
Competence (13)	x	
Quality Control & Assurance (26)	x	
PERFORMANCE (85)	X	
Planning (52)	x	
Supervision (3)	x	
Evidence (23)	x	
Documentation (7)	x	
REPORTING (44)	X	

Internal Audit Plan for Fiscal Year 2019

TEXAS HIGHER EDUCATION COORDINATING BOARD

INTERNAL AUDIT & COMPLIANCE MONITORING

Internal Audit Plan

Fiscal Year 2019

The Texas Internal Auditing Act requires state agency Internal Auditors to conduct a program of auditing that includes an annual audit plan, is prepared using risk assessment techniques, and identifies the individual audits to be conducted during the year. The following proposed plan meets the requirements of the Texas Internal Auditing Act.

Specific risk factors were considered as they apply to the agency's significant operational activities. These risk factors included:

- Financial significance
- Reputational significance and visibility
- Complexity; inherent risk; and the potential for abuse
- Prior audit and compliance monitoring results as an indicator of control effectiveness
- Audit recency – internal audit, compliance monitoring (as applicable), KPMG, SAO, and/or Federal auditors
- Changes in mission or key management

A risk-ranked listing of significant operational activities became the basis for the audits proposed for consideration herein.

A. Required Audits

	<u>Estimated Hours Required</u>
1. Follow Up of Prior Internal Audits <i>Assess the implementation status of previously reported internal audit findings in the areas of Texas Educational Opportunity Grant, Data Administration and Governance, Formula Funding, Physician Education Loan Repayment Program, and Contract Management.</i>	460
2. Self-Assessment of Work Quality, Internal Audit <i>Perform a self-assessment of internal audit work quality, in accordance with the requirements of professional auditing standards.</i>	210
3. Investigations	355

Texas Government Code Chapter 321.022, Coordination of Investigations, requires the coordination of investigations between the agency and the Texas State Auditor's Office. If the administrative head of an agency that is subject to audit by the state auditor has reasonable cause to believe that money received from the state by the agency or by a client/department of the agency may have been lost, misappropriated, or misused, or that other fraudulent or unlawful conduct has occurred in relation to the operation of the agency, the administrative head shall report the reason and basis for the belief to the state auditor. The state auditor may investigate the report or may monitor any investigation conducted by the agency.

4. Provide Assistance--External Audit of Agency Financial Statements 50
Internal Audit provides 50 hours of audit support to reduce external audit fees and to increase the level of knowledge of external auditors' assessment of the agency's financial statements and associated risks.
5. Ongoing Status Assessment of Corrective Action Plan Implementation to Address 470
NTT Texas Cyber Security Assessment Report
Perform an ongoing status assessment to assess the implementation status of the corrective action plan prepared to address recommendations from the 2017 NTT Texas Cyber Security Assessment Report.¹

B. Risk-Based Audits

6. Review of Formula Funding (Community College "Ten Pay" Payment System) 440
Review of internal administrative activities associated with the community college "ten pay" payment system. The appropriation for FY 2018 was \$900 million.
7. Review of Selected Academic Grant Programs 625
Review the internal administrative activities of selected academic grant programs for compliance effectiveness and efficiency. Academic grant program appropriations for FY 2018 were approximately \$216 million.
8. Review of Scholarship Programs 640
Review of scholarship programs for compliance, effectiveness, and efficiency. Scholarship program appropriations for FY 2018 were approximately \$3 million.
9. Review of Contract Management Administration 415
Review of agency contract administration processes for compliance with laws, regulations, policies, and procedures.

¹ Texas Administrative Code (TAC) 202 requires an independent review of the state agency's information security program.

External Audit Services Procured in Fiscal Year 2018

The agency contracted with KPMG, LLP, to perform an independent audit of the agency's Fiscal Year 2017 Financial Statements. As part of the agreement, the agency provided 50 hours of internal audit staff support to KPMG, LLP.

Reporting Suspected Fraud and Abuse

Actions taken by the agency to address the requirements of Section 7.10.Fraud Reporting, General Appropriations Act (82nd Legislature), Article IX and Government Code, Section 321.022.Coordination of Investigations, include:

- 1) Established a fraud prevention policy and posted the policy on the agency intranet for the employees. The policy encourages reporting of suspected violations to the State Auditor's Office Fraud Hotline.
- 2) Established a link to the State Auditor's Office Fraud Hotline on the agency's home page to enable the general public or employees to report suspected fraud or misconduct directly to the State Auditor's Office.
- 3) Coordinated with the Special Investigations Unit of the State Auditor's Office to investigate suspected fraud.
- 4) Provided ethics-related information to all new employees as part of the orientation process.