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## Texas Natural Resource Conservation Commission Effectiveness of Internal Audit Engagement June 1997

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# Texas Natural Resource Conservation Commission

## Detailed Issues and Recommendations

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### Overall Conclusion

The Internal Audit Division (Internal Audit) at the Texas Natural Resource Conservation Commission (Commission) is effective:

- Commissioners and executive management state that the internal audit function is effective because it provides accurate findings, valuable recommendations, clear and timely audit reports, and professional service.
- Internal Audit is credited by management with alerting the Commission before potential problems occur and effectively communicating with the Commission's executive management.
- Internal Audit assists members of the organization in the effective discharge of their responsibilities.
- Internal Audit furnishes independent analyses, appraisals, and recommendations about the adequacy and effectiveness of the Commission's major systems and controls.
- Internal Audit's resources are used to perform audits in high-risk areas of the Commission.
- Internal Audit met all eight effectiveness criteria developed from the Texas Internal Auditing Act.

Internal Audit employs five professional staff members and one administrative assistant to provide audit coverage for the activities of the Commission. The Commission is responsible for an operating budget of \$335 million, with more than \$94.7 million in contract expenditures, providing about \$282 million in revenues, and employing more than 2,900 employees.

### The Internal Audit Division is Effective in All Eight Effectiveness Criteria

- **Assessing Entity Risks** - Internal Audit bases audit planning on a biennial risk assessment. The risk assessment addresses the goals, strategies, and objectives of the Commission. It includes the major control systems, information systems, and programs. Input about the various Commission operations is obtained from managers. The risk assessment is documented and adequately supported. The risk assessment ranks the various auditable areas by risk factors in descending order.
- **Preparation of the Audit Plan** - Internal Audit is effective in preparing audit plans. The audit plan is based upon the risk assessment and approved by the Commissioners. The areas identified as the highest risk are selected and presented to executive management and the Commissioners for discussion of potential projects. Based upon these discussions, the audit projects are selected for inclusion in the audit plan. The planning process is coordinated with other internal evaluation groups and external auditors.

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Approximately 78 percent of the audit plans for fiscal years 1994 and 1995 were completed.

- **Organizing and Managing the Internal Audit Function** - Internal Audit's staff has the necessary skills, educational backgrounds, professional certifications, and experience to carry out its applicable audit responsibilities. Each position has a job description that is current and appropriate for the various audit staff levels. The job descriptions also list education and experience criteria. All current Internal Audit staff members meet or exceed the criteria. Internal Audit has a training program and a training record tracking system.
- **Planning and Conducting Audits** - Internal Audit properly plans and performs audit work according to the Institute of Internal Auditors and Government Auditing Standards. The extent of the work is adequate to meet the stated scope and objectives of its audits. The audit program steps are properly carried out; revisions to audit programs are proper and timely; and working papers adequately support auditors' findings, conclusions, and recommendations.
- **Communicating Audit Results** - Internal Audit appropriately communicates the results of its audits in written form to the proper level of management for corrective action. The reports are addressed to the Commissioners and executive management and signed by the Internal Audit Director. The audit reports contain the scope, purpose, objectives, executive summary, overall opinion, appropriate references, and responses from management. The findings and recommendations are clear, complete, factual, and objective.
- **Ensuring Compliance With Audit Standards** - Internal Audit has a quality assurance policy for internal and external reviews. The program includes policies for adequate audit supervision to ensure conformance with internal auditing standards, policies, and audit programs. Internal Audit review processes ensure all audit work conforms to audit standards.
- **Management Involvement in the Internal Audit Program** - Commissioners and executive management are actively involved with the internal audit function. The Commissioners approve the appointment of the Internal Audit Director and the audit plan. A Commissioner performs the annual performance evaluation of the Internal Audit Director. The Commissioners approve any deviations from the audit plan. The Commission Chair requested that follow-ups on all recommendations be completed every six months. Internal Audit allocates time for special projects requested by the Commission and executive management, which does not affect the completion of the overall audit plan.

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- **Follow-Up on Audit Recommendations** - Internal Audit follows up on recommendations twice each fiscal year. To fulfill the task, Internal Audit sends out audit recommendation status reports to all directors who have had audits and have not implemented all recommendations to date. The directors review and update the recommendations to reflect any changes made in the last six months. In addition, the directors document actions taken to address audit recommendations. Directors continue to receive the status reports until all of the recommended actions have been implemented or resolved.

### Management's Comment

*The Texas Natural Resource Conservation Commission (TNRCC) recognizes the value which an effective internal audit function can provide to agency management. TNRCC Internal Audit has worked to provide excellent service to the agency commissioners, management, and staff. As such, they have recommended many changes which have helped the agency to improve its operations. We believe that this partnership between our auditors and staff has fostered a positive approach to change.*

*We appreciate your efforts in reviewing the performance of our Office of Internal Audit and look forward to achieving further success.*

Appendix

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## Objectives, Scope, and Methodology

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### Objective

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 agency 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, procedures, manuals, reports, memoranda and other written communications
  - Internal audit reports

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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 basic 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 was 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.

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### 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:

- Scotty Killingsworth, CIA (Team Leader)
- Arthur Arispe
- Michelle Duncan
- Terry Holderman, MBA
- Larry Vinyard, CPA, CIA (Project Manager)
- Linda Lansdowne, CPA (Quality Control Reviewer)
- Charlie Hrcir, CPA (Audit Manager)
- Deborah Kerr, Ph.D. (Audit Director)