Texas Water Development Board

Internal Audit Annual Report

Fiscal Year 2014

TABLE OF CONTENTS

I. Compliance with House Bill 16 (Texas Government Code, Section 2102.015): Posting the Internal Audit Plan, Internal Audit Annual Report, and Other Audit information on Internet Web site 3

II. Planned Work Related to the Proportionality of Higher Education Benefits 3

III. Internal Audit Plan for Fiscal Year 2014 3

IV. Consulting Services and Nonaudit Services Completed 4

V. External Quality Assurance Review (Peer Review) 5

VI. Internal Audit Plan for Fiscal Year 2015 7

VII. External Audit Services Procured in Fiscal Year 2014 8

VIII. Reporting Suspected Fraud, Waste and Abuse 9

I. Compliance with House Bill 16 (Texas Government Code, Section 2102.015): Posting the Internal Audit Plan, Internal Audit Annual Report, and Other Audit information on Internet Web site

The Texas Water Development Board (TWDB) has fully complied with HB 16 by posting (on its Internet website) the agency's approved annual audit plans, annual internal audit reports, individual audit reports and audit implementation status reports issued in the last several years.

The individual audit reports provide information on audit findings, recommendations and management's responses while the audit implementation status reports provide a summary update of the action taken by management in addressing the audit issues. The latest status audit implementation report (issued on September 19, 2014) indicates that management has ***fully implemented*** (2 of 2) the recommendations from the SAO's State of Texas Compliance with Federal Requirements for Selected Major Programs (A-133) audit for fiscal year ended August 31, 2013. In addition, the report found internal audit recommendations to have been ***substantially implemented***, with the outstanding ones being on schedule to be implemented by their due date.

II. Planned Work Related to the Proportionality of Higher Education Benefits

This section is not applicable. The agency is not a higher education institution.

III. Internal Audit Plan for Fiscal Year 2014

Internal Audit changed its fiscal year end to August 31, to coincide with the state and agency fiscal year ends. This has resulted in the 2014 report being for a period of ten months rather than a year. The audits completed in the ten months ended August 31, 2014 are shown in the table below. The Review of Economically Distressed Areas Program (Project # 20140401) was completed in August and the report was issued in September 2014.

List of Completed Projects

Project Name	Current Status
20130203: Review of Revenue Management	Brought forward from FY 2013 Issued: February 2014
20130801: Review of the Drinking Water State Revolving Fund (DWSRF)	Brought forward from FY 2013 Issued: February 2014
20140101: Review of Debt Portfolio Management	Issued: April 2014
20140103: Review of Compliance with PFIA	Issued: April 2014
20130901: Review of Research & Planning	Brought forward from FY 2013 Issued: August 2014
20140102: Review of Loan Recipient Monitoring	Issued: August 2014

List of Carry-over Audits

Project Name	Current Status
20140401 Review of the Economically Distressed Areas Program (EDAP)	Report issued: September 2014

IV. Consulting Services and Nonaudit Services Completed

Internal Audit did not perform any consulting or nonaudit services in the ten months ended August 31, 2014.

V. External Quality Assurance Review (Peer Review)

Richard Tarr, CIA, CISA
3035 Dawley Ave.
Orlando, FL 32806
May 2014

The Institute of Internal Auditors' *International Standards for the Professional Practice of Internal Auditing (IIA Standards)*, the U.S. Government Accountability Office (GAO) *Government Auditing Standards*, and the Texas Internal Auditing Act (TIAA) require that internal audit functions obtain external or self-assessment quality assurance reviews to assess compliance with auditing standards, the TIAA, and to appraise the quality of their operations. The Director of Internal Audit conducted a self-assessment quality assurance review of the internal audit (IA) activity at the Texas Water Development (TWDB) during April 2014.

The primary objective of an independent validation is to provide an objective opinion as to whether or not the assertions made in the Quality Assurance Self-assessment Report can be relied upon. Another objective is to provide any additional recommendations that the reviewer deems may be of value to the IA activity. Other matters that might have been included in the scope of a full independent assessment, such as an in-depth analysis of successful practices, governance, consulting services, and use of advanced technology, were excluded from the scope of this independent validation.

In acting as validator, I am fully independent of the TWDB and have the necessary knowledge and skills to undertake this engagement. The validation, conducted during the period April 30 through May 2, 2014, consisted primarily of a review and testing of the procedures and documented results of the self-assessment. This included a review of a limited sample of the department's workpapers as well as conducting interviews with the TWDB's three Board Directors, the Executive Administrator, and the Director of Internal Audit. The review was conducted in accordance with a recommended methodology published by the State Agency Internal Audit Forum (SAIAF).

Based upon my interviews, the workpaper reviews, and a review of the work conducted by the Director of Internal Audit, I concur with her conclusion that the internal audit activity at the TWDB **generally conforms** to applicable internal auditing standards and the TIAA. A review of the workpapers documenting the review she performed showed that the results, including the opinion, were appropriately documented and they appear to have been objectively developed.

While I concur with the conclusion in the Self-assessment Report the following recommendations are intended to build on the foundation that is already in place with the objective of further improving the value, efficiency and efficacy of the audit work being performed at TWDB.

Recommendations

- Update the Internal Audit Charter to include a requirement that the Board annually and formally review the performance and compensation of the Director of Internal Audit.
- The Board should annually and formally review and set the budget and staffing resources for the internal auditing activity to ensure that the risks identified in the annual risk assessment are being adequately covered within a reasonable time frame, as required by the TIAA Sec. 2102.006 (d).
- The Director of Internal Audit should develop a new risk assessment model and from that model a new annual audit plan (reflecting risk perceptions of the new Board and senior management).
- Ensure that future plans give adequate attention to Information Technology (IT) risks.
- Consider implementing IDEA or ACL, for more efficient data analysis.
- The Chairman of the Board should consider being the administrative point person for the internal audit activity at TWDB.

Richard H. Tarr, CIA, CISA

VI. Internal Audit Plan for Fiscal Year 2015 (Board Approved: August 7, 2014)

Project Name	Hours
Review of the Flood Mitigation Assistance Program	600
Review of the Clean Water State Revolving Fund (CWSRF)	700
Review of Financial Reporting	800
Review of Contract Management	Reserve Project

Audits included in the 2015 Plan were primarily identified through a risk assessment process, in collaboration with Board members, the Executive Administrator, Deputy Executive Administrators, Division Managers, and staff. Risk assessment is a systematic process for assessing and integrating professional judgments about probable adverse conditions and events. The IIA defines risk as "the possibility of an event occurring that will have an impact on the achievement of objectives." The audit planning process considered both the impact and likelihood of such events occurring. The TWDB's auditable activities include both organizational units and Agency-wide processes, each of which was risk-ranked using specific elements including relative size of the unit, potential impact on operations, regulatory compliance, public exposure, work complexity, audit history, and other factors deemed relevant by Internal Audit and Executive Management.

The audit, Review of Contract Management, serves as a reserve project. It will be performed in the event that the hours put aside for contingencies i.e. fraud, waste and abuse investigations and special projects are not fully expended.

The specific scope of each audit in the plan will be determined once the audit team has completed its audit planning process.

Additional High Risks Not Included in the FY 2015 Audit Plan:

An additional several processes/programs were ranked as "high risk" during the annual risk assessment due to their impact on the agency's mission. An explanation for their exclusion is shown in the table below.

Project Name	Reason Project Was Excluded From The FY 2015 Plan
Debt Portfolio Management	Audited in FY 2014. The report was issued in April, 2014.
Investment Portfolio Management	SWIFT/SWIRFT processes are still under development.
IT - Governance & Operations	IT Division is undergoing significant changes in management and operations/procedures.
IT - Information Security	IT management is in the process of implementing recommendations from the recent Gartner Information Security Review.
SWIRFT Program	Program rules, policies and procedures are still under development.
Rules & Policy Development	Management is in the process of inventorying agency policies for Board consideration.

VII. External Audit Services Procured in Fiscal Year 2014

During Fiscal Year 2014, Internal Audit did not have any ongoing external audit services, nor were any services procured for the time period.

VIII. Reporting Suspected Fraud, Waste and Abuse

The agency has several mechanisms for reporting fraud to the State Auditor's Office (SAO). These mechanisms satisfy the requirements of Article IX, Section 7.09, the General Appropriations Act (83rd Legislature, Conference Committee Report), and the Texas Government Code, Section 321.022.

Fraud Reporting per Article IX, Section 7.09, the General Appropriations Act (83rd Legislature, Conference Committee Report)

TWDB has a link for reporting fraud, waste and abuse on the agency's website at http://www.twdb.texas.gov/home/fraud.asp. The link provides information on how to report suspected fraud, waste and abuse involving state resources. The link also includes information on SAO's fraud hotline and a further link to SAO's fraud, waste and abuse webpage.

Compliance with Texas Government Code, Section 321.022

The agency's Fraud, Waste and Abuse policy defines fraud, waste and abuse and provides staff with guidance on how to report fraud and/or suspected fraud. The policy assigns Internal Audit the primary responsibility for the investigation of all suspected fraudulent acts and for coordinating investigative activities along with the Human Resources Division, and Legal Services. The policy also requires the Executive Administrator to report suspected fraud or unlawful conduct to the State Auditor's Office.

The agency provides Ethics training to all employees periodically. The most recent agency-wide Ethics training was provided over three sessions in April and May 2014.