Report to Management

Audit of the Budget and Financial Analysis Process

April 14, 2010

Texas Water Development Board

Gilbert W. Mokry, Jr., CPA, CFE

Lawrence C. Gambone, CPA

Shari Daffern, CPA, CIA, CFE
KEY POINTS OF INTEREST

Overall Conclusion

The budget process has improved since the previous audit and generally works well. Communication between the Budget Office and the Executive Administrator, Deputy Executive Administrators, and Division Directors has been enhanced; monthly budget reports are provided by Budget Analysts; monthly meetings are conducted within the agency areas; and the most recent budget reports are now available to all employees electronically on the IWEB.

Nevertheless, the Budget Office has an opportunity to improve the budget development and monitoring processes.

Written procedures that detail the entire budget process would add transparency and assist management’s understanding.

Additional reports and analyses from Budget Analysts may assist management in monitoring their budgets and ensure the accomplishment of TWDB spending goals.

Training for agency staff and new management would enhance their understanding of the budget process.

Since the ultimate responsibility for each office’s budget rests with the DEA, agency management should be more involved in its development and notified of major revisions.

Key Facts and Observations

Detailed written procedures would assist in understanding the budget process.

The budget monitoring process ensures the accomplishment of TWDB’s spending goals. However, additional reports and analyses from the Budget Office would be helpful.

State Revolving Fund justification memoranda are reviewed by the Policy Integration and Federal Coordination Division.

Training for agency personnel would enhance their understanding of the budget process.

Budget preparation and maintenance is a complex process that would benefit from the increased involvement of agency management.
TABLE OF CONTENTS

A. Management Summary

1. Purpose ............................................................................................................................................. 1
2. Background ......................................................................................................................................... 1
3. Scope and Objectives .......................................................................................................................... 2
4. Conclusion ......................................................................................................................................... 2
5. Action Plans ....................................................................................................................................... 3

B. Detailed Observations, Recommended Action Plans, and Management Responses

1. Detailed Written Procedures Would Assist in Clarifying the Budget Process ......................................................... 4
2. Budget Monitoring Process Ensures Accomplishment of TWDB Spending Goals; However Additional Reports/Analyses from Budget Would Enhance Management Planning ................................................................. 5
3. State Revolving Fund Justification Memoranda are Reviewed by the Policy Integration and Federal Coordination Division ........................................................................................................ 6
4. Training for Agency Personnel Would Enhance Understanding of the Budget Process ......................................................... 6
5. Budget Preparation and Maintenance is a Complex Process that Would Benefit from Increased Involvement of Management ........................................................................................................ 7
Texas Water Development Board
Audit of the Budget and Financial Analysis Process

A. Management Summary

1. Purpose

The purpose of this report is to present the conclusion, observations, recommended action plans, and management responses from the audit of the Budget and Financial Analysis Process. This audit was conducted in accordance with the International Standards for the Professional Practice of Internal Auditing and Generally Accepted Government Auditing Standards.

The government standards require the audit to be planned and performed to obtain sufficient, appropriate evidence to provide a reasonable basis for observations and conclusions based on the selected audit objectives. The evidence obtained provides a reasonable basis for the observations and conclusions based on these objectives.

2. Background

The Budget Office is located within Finance and is comprised of the Budget Director and four of the five (4 of 5) budget analysts or officers (BAs) who perform budget analyses for the various TWDB Offices. The BAs for the Executive Administration Office, Finance, Water Resources Planning and Information (WRPI), Project Finance (PF), Construction Assistance (CA), and Operations and Administration (OA) report directly to the Budget Director and are part of the Finance Office. The BA for Water Science and Conservation (WSC) reports directly to the WSC Deputy Executive Administrator (DEA), but also has dotted line reporting responsibilities to the Budget Director. Two of the BAs have been performing budgeting functions for the agency for fewer than 15 months.

The mission of the Budget Office is to establish the Operating Budget and provide accurate monitoring, technical assistance, and reporting through its duration. This mission, which entails providing service to both external and internal customers, requires effective communications within all levels of TWDB.

The key initiatives of the budget team are to provide: (1) fiscal prudence through accuracy, accountability, analysis, and automation; (2) customer service through timely responses, open communication, integrity, and trust; and (3) an innovative environment through cross-training, succession planning, and best practices.

Fieldwork was conducted from March 1 through March 30, 2010. It involved a review of selected documents and interviews with the Chief Financial Officer (CFO), the Budget Director, and the five BAs. The Executive Administrator (EA), five (5) DEAs and seven (7) Division Directors were also interviewed. For purposes of this audit report, the EA, DEAs and Division Directors interviewed will be referred to collectively as management.

A prior internal audit of the Budget and Financial Analysis Process was performed in Fiscal Year 2007. The report for that audit was issued on February 26, 2007.
3. **Scope and Objectives**

The scope of this audit focused on the budget process and was not designed to make a determination on the budget itself. It encompassed the examination and evaluation of the adequacy and effectiveness of the internal controls and quality of performance in carrying out assigned responsibilities in relation to establishing the budget. The scope included specific program steps designed to assess:

- Effectiveness and efficiency of operations, and
- Reliability and integrity of information.

The objectives included the following determinations:

- Budget process works effectively and is formally documented;
- Budget monitoring process ensures the accomplishment of TWDB spending goals;
- TWDB is maximizing the availability and use of Clean Water and Drinking Water State Revolving Fund administrative funds;
- Adequate training in the budget process is provided to Budget Office staff and agency management;
- Budget Office provides management with sufficient information to develop and monitor their budgets.

4. **Conclusion**

The budget process has improved since the previous audit and generally works well. Communication between the Budget Office and the Executive Administrator, Deputy Executive Administrators, and Division Directors has been enhanced; monthly budget reports are provided by Budget Analysts; monthly meetings are conducted within the agency areas; and the most recent budget reports are now available to all employees electronically on the IWEB.

Nevertheless, the Budget Office has an opportunity to improve the budget development and monitoring processes.

Written procedures that detail the entire budget process would add transparency and assist management’s understanding.

Additional reports and analyses from budget analysts may assist management in monitoring their budgets and ensure the accomplishment of TWDB spending goals.

Training for agency staff and new management would enhance their understanding of the budget process.

Since the ultimate responsibility for each office’s budget rests with the DEA, agency management should be more involved in its development and notified of major revisions.
5. **Action Plans**

The following steps are recommended:

- The development of internal procedures for the Budget Office should be given a high priority. Equally important is written documentation of the budget process on an agency level. Establishing the parameters and directions for budget development can enhance control of the process, reduce the communication difficulties, firmly establish timelines and milestones, and provide an established reference for new BAs, managers, Directors, and DEAs.

- The Budget Office should consider providing management with a menu of optional, proactive reports and analyses in addition to the standard reporting package. The menu should contain a brief description of each tool’s function.

- The Budget Office should prepare a detailed budget process training session that could be presented to interested agency personnel on a recurring basis. At a minimum, the training would provide approximate timelines of the budget process, responsibilities of all respective parties (both the Budget Office and the separate areas of TWDB), explanations of terms and acronyms, reports that are available, and the preparation and monitoring steps required during the budget process.

- The Chief Financial Officer should consider establishing a forum for enhanced communication with management regarding budget target development. Communication with management at this stage of the process would be a positive step towards solving the perceived “transparency” problem. It would also accomplish several things: 1) garner early leadership buy-in of the budget process; 2) mitigate problems that may occur later, since management may have already addressed areas of concern during the initial target process, and 3) increase the feeling of management ownership of the budget.

- A policy regarding major changes to the operating budget should be included in the written procedures recommended in Action Plan Number 1 of this report. The procedures should state that management of the affected area should be notified of major changes to their budget. This would give the affected management an opportunity to receive an explanation of the change and, possibly, recommend a more effective course of action. It would also enhance management’s “ownership” of the budget and strengthen management’s resolve to adhere to the budget.
B. Detailed Observations

1. Detailed Written Procedures Would Assist in Clarifying the Budget Process

Overall, the budget process works well. The general consensus among management is that both the budget process and communication with Budget Office staff have improved since the previous audit. Monthly reports are provided by the Budget Office and the most recent version of the budget is available to management electronically on the IWEB. Most of the management interviewed stated that they have a good working relationship with their budget analysts (BAs).

Nevertheless, there are opportunities for improvement. Aside from the general budget instructions, there are no written policies and procedures that document in detail the entire budget process on an agency level. Based upon interviews with management and Budget Office employees, the creation of, and adherence to, detailed procedures would help to make the process more “transparent” and would clarify the roles and duties of all participants.

Management recognizes the necessity and inevitability of budget revisions to accommodate limited or decreased funding and unexpected expenditures. However, since no documented procedures exist, it is the formal change-making process that is not clearly defined.

The requirement for documented procedures was noted in the prior audit of the budget process, which stated in part:

*The processes for developing and monitoring the Operating Budget should be better documented . . .*

The Budget Director has recognized the need for comprehensive internal procedures and has tasked one of the BAs to develop them.

**Recommended Action Plan 1:**
The development of internal procedures for the Budget Office should be given a high priority. Equally important is written documentation of the budget process on an agency level. Establishing the parameters and directions for budget development can enhance control of the process, reduce the communication difficulties, firmly establish timelines and milestones, and provide an established reference for new BAs, managers, Directors, and DEAs.

**Management Response 1:**
The CFO and Budget Director recognize the importance of written procedures; as a result the development of desk procedures is included in all performance plans. One of the Senior Budget Analysts has already been tasked with coordinating the development of comprehensive written procedures for Budget processes.
2. **Budget Monitoring Process Ensures Accomplishment of TWDB’s Spending Goals; However, Additional Reports/Analyses from Budget Would Enhance Management Planning**

For the most part, management was satisfied with the budget monitoring and reporting process. DEAs and Directors receive monthly reports from their respective BAs and most DEAs hold monthly meetings to discuss the budget status. Nevertheless, most management interviewed agreed that enhanced, proactive analyses from the Budget Office would help them with future decision making.

Management relies on the knowledge and analytical skills of their BAs to provide them with status reports, warnings about potential issues, and “goal-seeking” and “what if” analyses to help them with their budget decisions. In this respect, several members of management explained that they receive some proactive “reports and analyses” (tools) from their BAs. Conversely, other managers stated that they are currently tracking and analyzing their budgets on Excel spreadsheets and/or Access databases because specific monitoring and analyses from the Budget Office are not provided.

A lack of analyses was noted in the prior audit of the budget process, which stated in part:

> . . . possibilities for automation should be explored to ensure accuracy and expediency. With automated tools, forecasting models could be created that would allow TWDB to maximize the use of agency funds.

**Recommended Action Plan 2:**
The Budget Office should consider providing management with a menu of optional, proactive reports and analyses in addition to the standard reporting package. The menu should contain a brief description of each tool’s function.

**Management Response 2:**
As part of the presentation of the approved operating budget to agency management in September 2010 budget staff will provide a menu of specialized reports that can be
request from the budget officer. In addition this menu of reports will be available on the iWeb for all staff to view.

**Responsible parties:** Budget Director and staff  
**Estimated completion date:** September 2010

3. **State Revolving Fund Justification Memoranda are Reviewed by the Policy Integration and Federal Coordination Division**

   Justification memoranda are prepared annually by management to substantiate TWDB’s usage and maximization of Clean Water and Drinking Water State Revolving Fund administrative funds. Beginning last year, responsibility for the memoranda was transferred from the Budget Office to the Policy Integration and Federal Coordination Division.

   The justification memoranda for FY 2010 were properly reviewed. Individual Directors were consulted, as part of the review process, to clarify any questions or discrepancies noted. The reviews were adequately documented.

   The Policy Integration and Federal Coordination Division has prepared new instructions, including a template for Directors to use, for the preparation of next fiscal year’s memoranda.

   **Recommended Action Plan 3:** None deemed necessary.

4. **Enhanced Training for Agency Personnel Would Expand Understanding of the Budget Process**

   No formal training program for new BAs has been established to familiarize them with their assigned areas. Further, the training provided for newly appointed DEAs and Directors may not be sufficient to adequately prepare them for the budget process.

   Our interviews with BAs revealed that training for the budget and budget process is generally via a “hands on” approach. New BAs generally rely on their more experienced counterparts to teach them the process. The new BAs indicated that the analysts work well as a team, and that the experienced members were helpful to the newer personnel.

   Several newly appointed Directors expressed concerns about their lack of knowledge and experience in the budget process. The Budget Office presents a slide-show to management at the beginning of each fiscal year. The presentation, which is available on the IWEB, includes a brief description of budget policies, timelines, some definitions of terms and acronyms, and a review of the monitoring process. Other than this presentation, no formal training program has been established; nor are there formal budget procedures to reference other than the initial budget instructions.

   The prior audit of the budget process noted a lack of available training. The finding stated:
Training for developing and maintaining the Operating Budget should be developed and made available to the appropriate responsible staff at the various staffing levels.

**Recommended Action Plan 4:**
The Budget Office should prepare a detailed budget process training session that could be presented to interested agency personnel on a recurring basis. At a minimum, the training would provide approximate timelines of the budget process, responsibilities of all respective parties (both the Budget Office and the separate areas of TWDB), explanations of terms and acronyms, reports that are available, and the preparation and monitoring steps required during the budget process.

**Management Response 4:**
Budget staff have scheduled a Budget Kickoff for April which will include detail on the budget process as well as identification of roles and responsibilities. Based on feedback from this presentation, budget staff will develop an ongoing training session for interested agency personnel. A slide show will be developed which will be added to the iWeb.

**Responsible parties: CFO and Budget staff**
**Estimated completion date: November 2010**

5. **Budget Preparation and Maintenance is a Complex Process that Would Benefit from Increased Involvement of Management**

The annual budget process begins when the budget instructions are forwarded to the DEAs in April. The instructions provide general information and guidelines for estimating and developing areas of the budget.

DEAs receive their budget “targets” from the Budget Office with the budget instructions. The targets, which are generally based upon the prior year’s budget, are developed by the CFO and Budget Director and then presented to the Executive Administrator for approval. Once approved, they are given to the DEAs.

Ultimately, each office’s management is responsible for the development and implementation of their budget; and the prescribed budget process should reflect this responsibility. However, management lacks a clear understanding of the decisions and methodologies that enter into target development. In essence, though the DEAs realize targets are not arbitrarily determined, as the ultimate owners of their budgets, they expressed concern because target decisions are made without their input.

Similarly, the majority of management interviewed stated they have experienced major changes to their budget without notifications and/or satisfactory explanations from the Budget Office or their assigned BAs. Upon reviewing their monthly budget reports, they would discover that a budget category was reduced or (on rare occasions) increased,
without explanation or prior notification. In many cases, the budget “owners” had plans for the funds that no longer existed.

Management requested that the Budget Office communicate the details of the budget and budget process to its “customers.” The DEAs interviewed also requested that they be given an opportunity for input into the development of the agency’s targets.

The prior audit of the budget process noted this lack of communication. The finding stated in part:

Changes in the budget totals by [the Budget] Office should be documented and communicated to the executive team and to key budget staff . . . as to who made the decision, why, and what long range impact the changes may have.

Recommended Action Plan 5:  
The Chief Financial Officer should consider establishing a forum for enhanced communication with management regarding budget target development. Communication with management at this stage of the process would be a positive step towards solving the perceived “transparency” problem. It would also accomplish several things: 1) garner early leadership buy-in of the budget process; 2) mitigate problems that may occur later, since management may have already addressed areas of concern during the initial target process, and 3) increase the feeling of management ownership of the budget.

A policy regarding major changes to the operating budget should be included in the written procedures recommended in Action Plan Number 1 of this report. The procedures should state that management of the affected area should be notified of major changes to their budget. This would give the affected management an opportunity to receive an explanation of the change and, possibly, recommend a more effective course of action. It would also enhance management’s “ownership” of the budget and strengthen management’s resolve to adhere to the budget.

Management Response 5:  
After approval by the Executive Administrator, the CFO presented 2011 and 2012-13 budget targets and instructions during a leadership meeting. In addition, the regularly scheduled leadership meetings will continue to be used as a forum for presentation of major budget related processes, projects and initiatives.

Responsible party: CFO  
Estimated completion date: April 2010

The budget reports provided by the budget officers to the DEAs as part of their regular monthly meetings will include a specific presentation on monthly and year to date budget amendments. The budget policies for fiscal year 2011 will be revised to include specific language on budget amendments.

Responsible parties: CFO, Budget director and staff  
Estimated completion date: September 2010
Texas Water Development Board

Audit of the Budget and Financial Analysis Process

____________________________
Gilbert W. Mokry, Jr., CPA, CFE
Auditor

____________________________
Lawrence C. Gambone, CPA
Auditor

____________________________
Shari Daffern, CPA, CIA, CFE
Director of Internal Audit