Fiscal Year 2018/2019 Annual Audit Plan

Table of Contents

Introduction 3
Purpose and Mission 3
Auditing Charter and Internal Auditing Definition 3
Risk Assessment 3
Proposed Audit Projects for Fiscal Years 2018 & 2019 4
Audit Projects 4
Office-wide Projects 5
Acceptable Level of Risk 6
Contingency 6
Planning, Administrative & Other 6
Advisory Services 6
Follow-up 6
External Auditor Liaison 7
Management Controls 7
Closing 7
Appendix A 8
About Internal Audit at the Secretary of State 8
Quality Assurance 8
Appendix B 9
Model – Levels of Internal Control 9

Introduction

The Chief Auditor's Office appreciates the opportunity to provide our vision for audit activities at the Texas Secretary of State (SOS) for the remainder of Fiscal Year (FY) 2018 and FY 2019.

This proposal is the result of a risk assessment process through which the Chief Auditor's Office conscientiously reviewed risks related to internal agency processes, agency expenditures and revenue, and agency information technology. This document presents our proposed audit services, information technology, and advisory service project areas for the remainder of FY 2018 and FY 2019, and outlines our risk assessment methodology. We believe the areas identified for audit will result in the best return on the audit resource investment.

Purpose and Mission

The audit plan is requires by the Texas Internal Auditing Act (Chapter 2102, Title 10, Govt. Code, Vernon's Codes Annotated), Government Auditing Standards, and the International Professional Practices Framework promulgated by the Institute of Internal Auditors (IIA).

The Chief Auditor's Office provides assurance and advisory services that help the Secretary and management meet agency goals and objectives. We provide independent and objective information, analyses, and recommendations to assist management in effecting constructive change, managing business risk, and/or improving compliance and accountability in operations.

Auditing Charter and Internal Auditing Definition

The Chief Auditor's Office Audit Charter (Charter), approved by the Secretary in May 2018, and clearly defines the scope of activities and responsibilities internal auditing encompasses. The Charter also defines our role, authority, organization, independence, professional standards, reporting relationships and quality assurance processes.

As defined in the Charter, internal auditing encompasses the examination and evaluation of the adequacy and effectiveness of the agency's system of internal control and the quality of performance in carrying out the goals and objectives of the agency. The Texas Internal Auditing Act adopts the IIA definition of internal audit:

> ***An independent, objective assurance and consulting activity designed to add value and improve an organization's operations. It helps an organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes.***

The Chief Auditor's Office will be able to contribute additional value to the agency by combining information technology audit components and techniques into all projects as appropriate. Many of the agency's operations and processes involve both business and information technology components. Combining these components into our audits simultaneously will provide greater efficiency and effectiveness to all projects. We believe that using this approach will maximize the value we add to the agency.

For more background information on the Chief Auditor's Office, please see **Appendix A.**

Risk Assessment

Risk assessment, as defined by the IIA, is a *"systematic process for assessing and integrating professional judgments about probable adverse conditions and/or events."* The Committee of Sponsoring Organization (COSO) of the Treadway Commission Internal Control – Integrated Framework states *"Risk assessment involves a dynamic and interactive process for identifying and assessing risks to the achievement of objectives."*

In conducting our risk assessment, the Chief Auditor's Office received input from the Secretary of State, Interim Deputy Secretary of State, Executive Management, and Section Managers. Input was received from all areas within the agency.

For Audit purposes, the Chief Auditor's Office identified the universe of auditable activities primarily as those activities conducted to address the strategies funded by the General Appropriations Act. We also identified auditable activities to include fees collected and all contracts entered into by the agency. Each of the fees and contracts included in the assessment was ranked using specific elements of risk related to that category. The high risk fees and contracts were selected for audit projects. These projects were then prioritized to determine which fees and contracts should be included in the proposed audit plan.

We then ranked all identified activities within each category using specific elements of risk related to that category, including fraud risk as appropriate. From this ranking, specific project topics were identified for each of the high risk areas. Lastly, we prioritized each potential project to determine which projects should be included in the proposed audit plan.

We will update our risk assessment as additional information is obtained and expenditures occur throughout the plan period. Our continuous evaluation of risks will ensure the most efficient use of audit resources.

Operations throughout the agency are heavily dependent on Information Technology (IT). Included in the universe of auditable activities were IT systems, functions, and processes (systems).

IT systems, functions, and processes were ranked using specific elements of risk related to that category. These systems were then ranked and specific project topics were developed based on the high risk systems. These projects were then prioritized to determine which projects should be included in the proposed audit plan.

The risk assessment process included a review of project areas by the Audit Director to ensure adequate coverage of risk and to avoid inappropriate duplication of coverage. The results of the process are presented in the following tables.

A listing of alternative projects was also developed, but is not included in this document. Alternative projects are additional areas that we believe could potentially benefit from the use of audit resources. We seek approval to use these projects in circumstances where additional or substitute projects are required.

We will consult with the Secretary, Deputy Secretary and executive management to adjust the plan as needed based on priorities, management requests, workloads, changes in operations, and availability of audit resources. Through approval of this proposal, the Secretary authorizes the Deputy Secretary to approve any amendments to the audit plan that become necessary.

Proposed Audit Projects for Fiscal Years 2018 & 2019

Below are the proposed Audit and Office-wide projects to be conducted by the Chief Auditor's Office.

Audit Projects

An Audit on the Status of Outstanding Audit Recommendations (OAR)

An Audit for Compliance with Texas Administrative Code (TAC) 202 Requirements.

An Audit of Agency-wide Revenue Processing

An Audit of Elections Administration & Funds Management

An Audit of Key Performance Measures

An Audit of SOS's Continuity of Operations Plan and Testing

Office-wide Projects

Internal Audit Quarterly Reports

Client Assistance/Consulting

Annual Internal Audit Report FY 2018

Annual Internal Audit Report FY 2019

FY 2020 Annual Audit Plan

Special Requests form the Secretary or Deputy Secretary

Acceptable Level of Risk

We believe that completing the projects proposed above, or appropriate alternatives, will reasonably cover the risks identified by the risk assessment.

While the list of proposed projects results from our consideration of a wide-ranging scope of auditable activities, it does not address or provide coverage for all SOS components or systems. Our goal is to optimize our resources to provide reasonable coverage in the areas we believe require the most attention.

Due to a variety of factors, some significant activities that might warrant review may not be carried forward to the list of proposed audit projects, but they did receive consideration.

Ultimately, we cannot address every risk. It is important for the Secretary and executive management to understand the limitations of the audit coverage and the attendant risks for areas not audited. In our opinion, this listing of proposed projects allocates audit resources to the most important priorities and significant risks of the SOS and allows flexibility to address other risk areas that may become known during the audit plan period.

However, according to the Texas Internal Auditing Act, it is the Governing Board or Administrator's responsibility to conclude whether the resources are adequate to address the identified risks. Specifically, Senate Bill 1694 of the 78th legislative session amended the Texas Internal Auditing Act to require the governing board or administrator of a state agency to periodically review the resources dedicated to the audit program and determine if adequate resources exist to ensure that risks identified in the annual risk assessment are adequately covered within a reasonable time frame.

The Audit Director asserts that staff resources are adequate to address the high risk areas linked to proposed audit projects. Any additional audit coverage would require additional staff resources.

Beside staff resources, the Audit Director has been provided sufficient operating resources. The Director is confident that should additional resources become necessary that such a request will be addressed in good faith.

Contingency

While we will always work to address any appropriate special requests, we have specifically set aside resources for special requests from the Secretary or Deputy Secretary.

Planning, Administrative & Other

A percentage of total available audit hours are allocated to planning, administrative and other special projects. These projects include advisory services, follow-up, and external auditor liaison duties.

Advisory Services

Audit staff may participate ex-officio in agency committees and work groups as needed and directed by the Secretary or requested by executive management. We can provide advice and suggestions on management issues, concerns, and draft policies and procedures upon request.

Follow-up

Follow-up is an important part of our audit effort and is required by professional standards. The status of all recommendations will be presented annual follow-up reports to the Secretary and executive management. Follow-up reporting continues until all recommended actions and management action plans are implemented or the specific risk reported is otherwise mitigated or accepted.

External Auditor Liaison

The Audit Director serves as the liaison with the Texas State Auditor's Office (SAP), and other external audit groups having oversight responsibility for SOS activities. We will assist these external entities on their projects as appropriate. Our goal in the role of liaison is to provide assistance to the extent that professional and organizational reporting responsibilities allow. We will conduct examinations in a manner that allows for maximum audit coordination and efficiency.

Management Controls

Management is responsible for establishing a system of internal/management controls adequate to reasonably assure that established objectives are accomplished. The COSO Internal Control – Integrated Framework states, "Internal Control is a process, effected by an entity's board of directors, management, and other personnel, designed to provide reasonable assurance regarding the achievement of objectives..."[3] During FY 2018, the Audit Director will continue to provide agency managers with information on internal control processes and procedures. The Levels of Internal Control Model developed by the University of Texas System Audit Office contains the following control tiers:

- Level 1 Controls (Operating Controls)
- Level 2 Controls (Monitoring Controls)
- Level 3 Controls (Oversight Controls)
- Level 4 Controls (Internal Audit)

This model identifies the four levels of internal control and relates them to the three dimensions of transactions, time, and involvement in the process. The model and its application within SOS are shown in **Appendix B**.

Management controls are most effective when they are built into the organization's infrastructure and are a fundamental part of management's philosophy. Use of the model supports quality and empowerment initiatives, avoids unnecessary costs, and enables a quick response to changing conditions.

Closing

The Audit Director thanks the Secretary, executive management and staff for their involvement in the development of this proposal. I look forward to helping the agency meet its objectives during the audit plan period.

For further information please contact James Walker, Internal Audit Director at (512) 475-2726 or by email at jwalker@sos.texas.gov.

James Walker, CPA, CISA, Internal Audit Director

Appendix A

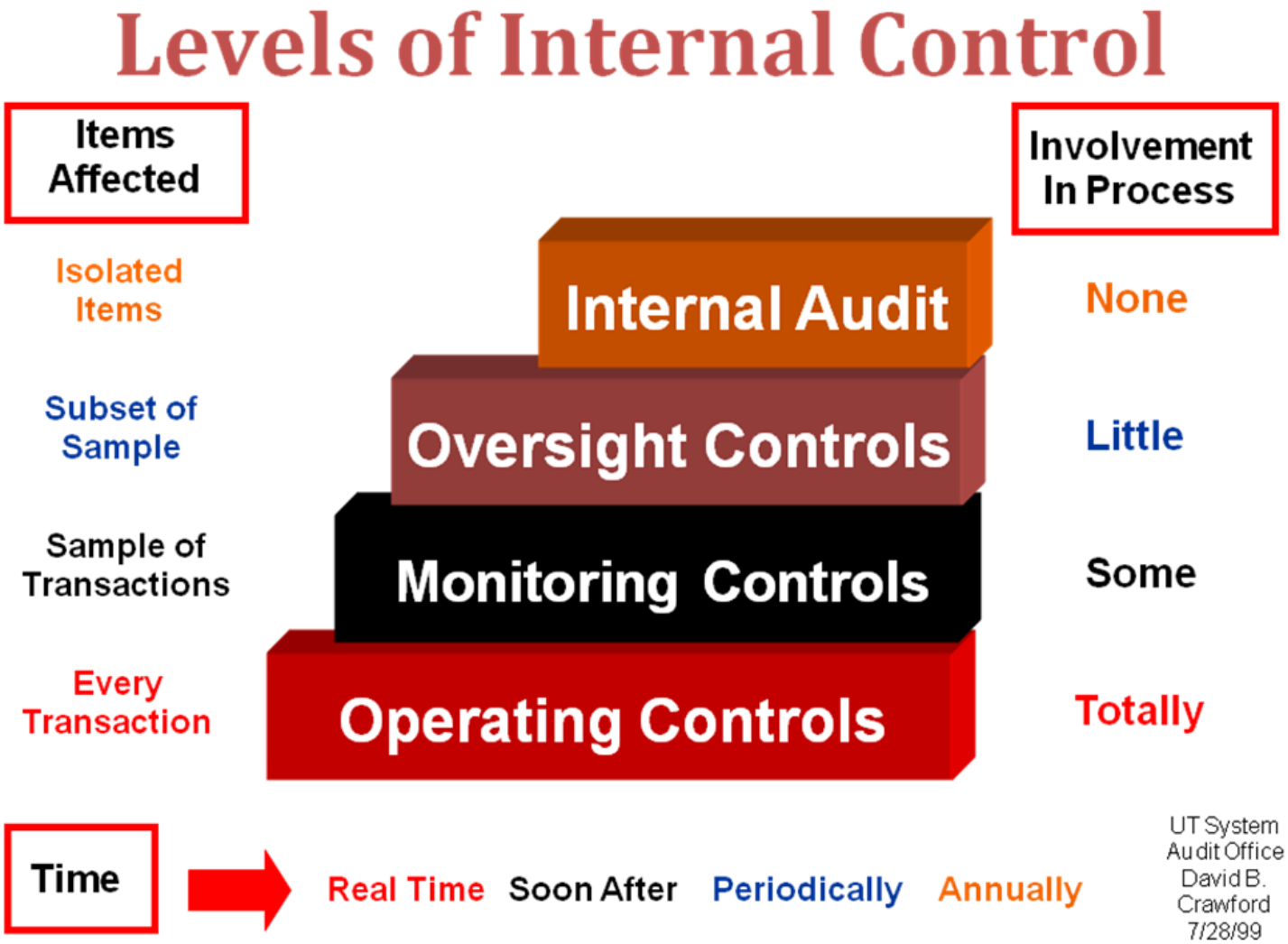
About Internal Audit at the Secretary of State

Until August 31, 2016, the internal audit function at the Secretary of State was outsourced to a local Certified Public Accounting firm. At the expiration of that contract, a decision was made not to renew the contract but rather hire a full time employee to serve as the Internal Audit Director. Due in large part to the hiring freeze affecting all state agencies in 2017, the new Director was not hired until April 1, 2018.

The Audit Director has over 30 years audit experience in both state government and the private sector. His experience includes 12 years working for several other large Texas state agencies. He is a Certified Public Accountant (CPA) and a Certified Information Systems Auditor (CISA). He is a member of the Institute of Internal Auditors (IIA) and the Information Systems Audit and Control Association (ISACA).

Quality Assurance

Quality assurance is an important component in providing high quality auditing services. Professional standards require audit departments to have a periodic external quality assurance (peer) review. Additionally, the Texas Internal Auditing Act requires a peer review every 3 years. As a newly formed internal audit department, the first peer review will be completed in FY 2020.

Appendix B

Model – Levels of Internal Control