

Agenda Item: 7.4

Prepared by: Mark Majek, Kathy Thomas, Deborah Bell, and David MacCabe

Meeting Date: April 2018

Summary of Request:

The BON Internal Audit Charter requires conformance with the *Government Auditing Standards* developed by the United States Government Accountability Office and the *International Professional Practices Framework (IPPF)* of The Institute of the Internal Auditors. The *IPPF* is comprised of the *International Standards for the Professional Practice of Internal Auditing*, the *Definition of Internal Auditing* and the *Code of Ethics*.

Government Auditing Standard 3.62 Requires audit organizations to maintain a system of quality control that includes having an external peer review performed by reviewers independent of the organization at least once every three years. The review is conducted to appraise the quality of BON internal audit activities and to assess conformance with professional auditing standards.

Historical Perspective:

The current engagement is the second external peer review conducted at the BON. A periodic peer review, or quality assurance review, of the internal audit function is an essential component of a comprehensive quality assurance and improvement program.

Pros:

The Board of Nursing will be in compliance with the Internal Auditing code of ethics and auditing standards.

Cons:

None.

Staff Recommendation:

Board Action: Move to accept the external quality assurance review report as prepared by David J. MacCabe dated March 30, 2018.



EXTERNAL QUALITY ASSURANCE REVIEW REPORT
Internal Audit Function

March 30, 2018

Conducted by

David J. MacCabe, CIA, CGAP, CRMA, MPA

Internal Audit Consultant

Overall Opinion

Based on the information received and evaluated during this external quality assurance review, it is our opinion that the Texas Board of Nursing Internal Audit function receives a rating of **“Pass/Generally Conforms”** and is in compliance with the Institute of Internal Auditors (IIA) *International Standards for the Professional Practice of Internal Auditing* and Code of Ethics, the United States Government Accountability Office (GAO) *Government Auditing Standards*, and the Texas Internal Auditing Act (Texas Government Code, Chapter 2102). This opinion, which is the highest of the three possible ratings, means that policies, procedures, and practices are in place to implement the standards and requirements necessary for ensuring the independence, objectivity, and proficiency of the internal audit function.

We found that the Internal Audit function is independent, objective, and able to render impartial and unbiased judgments on the audit work performed. The internal auditor is qualified, proficient, and knowledgeable in the areas audited. Individual audit engagements are planned using risk assessment techniques; audit conclusions are supported in the working papers; and findings and recommendations are communicated clearly and concisely.

The Internal Audit function is well managed. The internal auditor has effective relationships with the Board and is well respected and supported by management. Surveys and interviews conducted during the quality assurance review indicate that management considers Internal Audit a useful part of the overall agency operations and finds that the audit process and report recommendations add value and help improve the agency's operations.

The Internal Audit function has reviewed the results of the peer review team's work and has accepted them to be an accurate representation of the Department's operations.

Acknowledgements

We appreciate the courtesy and cooperation extended to us by the internal auditor, the president and the Board audit liaison, the executive director, and the operations director who participated in the interview process. The feedback from the interviews provided valuable information regarding the operations of the Internal Audit function and its relationships with management and the Board.



March 30, 2018

David J. MacCabe, CIA, CGAP, CRMA, MPA

Quality Assurance Reviewer

Background

Internal Audit Requirements

The IA function was created in 2012 in response to the requirements of Texas Government Code 2101 (commonly referred to as the Texas Internal Auditing Act). Ms. Jaye Stepp has provided contract internal audit services to the BON over the past six years.

The BON Internal Audit Charter requires conformance with the *Government Auditing Standards* developed by the United States Government Accountability Office and the *International Professional Practices Framework (IPPF)* of The Institute of Internal Auditors. The IPPF includes four elements: the *International Standards for the Professional Practice of Internal Auditing*, the Core Principles, the Definition of Internal Auditing, and the Code of Ethics.

Government Auditing Standard 3.62 requires audit organizations to maintain a system of quality control that includes receiving an external reviewer performed by reviewers independent of the audit organization every three years. IIA Standard 1312 requires an external quality assessment must be conducted at least once every five years by a qualified, independent assessor or assessment team from outside the organization.

The first external peer review or external quality assessment at the BON was completed in May 2015.

Qualifications and Independence of the External Reviewer

The external reviewer meets the requirements for qualified, independent external assessors defined in both the *IIA Standards* and the *Government Auditing Standards*. The reviewer previously served as the chief audit executive for three Texas state government agencies and had participated in approximately 85 QARs or peer reviews throughout the United States. The external reviewer also meets the independence requirements specified in standards.

Objectives, Scope, and Methodology

The primary objectives of the peer review or QAR were to evaluate the IA function's conformance with the *Government Auditing Standards*, The IIA's *International Professional Practices Framework*, and the Texas Internal Auditing Act. Additional objectives included identifying leading practices and suggesting areas where improvements may be beneficial.

The review focused on IA work performed during the period from April 2015 through March 2018. The methodology for this QAR included the following steps:

- Reviewing the self-assessment report prepared by the internal auditor in planning and preparation for this external review;
- Reviewing the actions taken in response to recommendations contained in the May 6, 2015 peer review report.
- Reviewing the Internal Audit Charter for conformance with professional standards and the Texas Internal Auditing Act;
- Reviewing and validating the IA function's process for assuring objectivity and independence;
- Reviewing continuing professional education (CPE) records and the tracking system used to record CPE credits;
- Reviewing the Quality Assurance and Improvement Program (QAIP);
- Conducting personal interviews with the Board president, a Board audit liaison, the executive director, the operations director, and the internal auditor.
- Reviewing the IA function's policies and procedures pertaining to the audit engagement process and communications through the planning, field work, and reporting phases;
- Reviewing two sets of engagement working papers completed during the review period;
- Providing examples of leading practices from other leading internal audit activities; and
- Reviewing the following IA function documents and products:
 - Master peer review documentation;
 - Risk assessment matrices;
 - Audit Recommendations Tracking System (ARTS) reports;
 - Internal Audit Procedures Manual; and
 - Other relevant documents.

Detailed Results

The results of the quality assurance review for the Texas Board of Nursing (BON) Internal Audit (IA) function are presented in the order of the *Standards for the Professional Practice of Internal Auditing*. No significant weaknesses were identified during the review that would prevent the Department from fulfilling its responsibilities.

IIA Code of Ethics

IA demonstrates its commitment to the IIA *Code of Ethics and the Ethical Principles provided in the Government Auditing Standards*. This is attained through a professional and respectful demeanor, attending periodic ethics training classes, and practicing ethical behavior while conducting audit work activities.

In addition, the agency's *Ethics Policy* is an indication of an organization-wide commitment to accountability and integrity.

Purpose, Authority, and Responsibility

The Internal Audit Charter outlines the purpose, authority, and responsibility of the IA function and information about the processes, policies, and procedures of the IA function. The current charter was signed by the Board president, executive director, and internal auditor on October 23, 2017.

The charter recognizes the mandatory nature of the IIA's Code of Ethics, the Core Principles, and the *Standards*. The nature of assurance and consulting services and the Definition of Internal Auditing were included in the prior charter but was inadvertently left out of the 2017 charter revision. The internal auditor stated this reference will be included in the next charter revision.

Independence and Objectivity

IA is independent both in terms of the agency's organizational structure and in audit practices. The internal auditor is an independent contractor who reports functionally to the Board and administratively to the executive director. This organizational reporting provides authority to promote independence, ensures adequate consideration of audit reports and encourages appropriate action on audit issues and recommendations. Removal of the internal auditor requires Board approval.

The charter helps ensure continued independence by specifying that the internal auditors remains free of operational and management responsibilities that could impair the ability to make independent reviews of all areas of the agency's operations. The internal auditor has not had prior responsibility for any areas audited and signs independence statements for each audit engagement.

Proficiency and Due Professional Care

The internal auditor has the knowledge, skills, and abilities to perform audit work. She is a certified public accountant and certified internal auditor with 17 years internal auditing experience in Texas state government. She also holds two other professional certifications.

The internal auditor meets the Texas State Board of Public Accountancy requirements for 120 hours training every three years. Internal auditors are required by the Department's policies and procedures to enhance their knowledge, skills, and abilities by obtaining at least 40 hours of continuing professional education each year.

Quality Assurance and Improvement Program

The internal auditor has implemented a quality assurance and improvement program (QAIP) that (1) helps ensure that IA adds value and improves the agency's operations and (2) provides assurance that the IA conforms with the *Standards* and the IIA Code of Ethics. The QAIP involves audit policies and procedures, checklists, periodic client surveys, and external peer reviews scheduled every three years. Each audit report indicates that the work was performed in accordance with *Standards*. IA also provides an annual QAIP report to the Board.

Managing the Internal Audit Activity

The internal auditor conducts an annual risk assessment that forms the basis for the Annual Audit Plan, which is adjusted annually in response to emerging risks or based on changing agency and Board priorities. This periodic risk assessment exercise engages key BON staff members in discussing key business risks and evaluating the sufficiency of internal controls to mitigate those risks.

Each internal audit report addresses risk and control issues within the agency. The internal auditor has developed thorough policies and procedures to guide the internal audit activity. She reports performance relative to the annual plan in an annual report submitted to the agency Board, executive director, the Governor's Office, the State Auditor, and other state oversight entities.

Nature of Work

IA evaluates risks related to financial and operating information as well as the effectiveness and efficiency of operations, the safeguarding of assets, and compliance with laws and regulations. The Department also evaluates the extent to which operational and program objectives have been achieved. IA contributes to the organization's risk management and governance processes by providing information and assistance to executive management and the Board about how the accomplishment of goals is monitored and how accountability is ensured.

Engagement Planning

During engagement planning, the internal auditor considers the objectives of the activity being reviewed and the related risks and controls. Resources needed for each audit are adequately considered during planning. Risk assessments are used to develop the objectives of each audit. Interviews conducted during this quality assurance review indicated that the objectives of audits are clearly communicated to the auditees. An engagement audit program is documented and approved for each audit. The scope of audits is adequately planned and documented in planning documents and audit reports.

Workpaper reviews indicated thorough planning by the internal auditor. Detailed programs and templates guide the auditor through the process of collecting information, identifying risks and controls, and developing objectives appropriate for the audit engagement. These efforts are enhanced with the cooperation and assistance of BON managers and staff members.

Performing the Engagement

The internal auditor conducts analysis and review to obtain sufficient, reliable, relevant, and useful information to achieve the audit objectives and draw logical and supportable conclusions. Workpapers are detailed, relevant, and link back to engagement objectives. A field work audit program is developed and followed for each engagement. Audit programs, procedures, and forms contain useful templates for the planning, field work, reporting, and closeout phases of an audit engagement.

Audits are appropriately planned and conducted by the internal auditor. Typical duties include conducting planning meetings, reviewing records, conducting interviews, and documenting observations to ensure the sufficiency of evidence and compliance with *Standards*.

Communicating Results

Audit results are communicated in a timely manner. Potential issues and concerns are communicated throughout the audit engagements giving management the opportunity to provide additional information and/or to initiate corrective action. Audit results are presented to management before they are finalized in a report, which helps ensure there is agreement about the areas for improvement and the recommended solutions.

Audit reports typically contain an executive summary, the audit objectives, scope, methodology, results and conclusions, recommendations, and management's responses and action plans. The results of interviews with management indicated that internal audit reports are accurate, objective, clear, concise, and complete. The Internal Audit Director distributes internal audit reports to the Board, to executive management, and to management of the activity being audited.

Monitoring Progress

The internal auditor has established the Audit Recommendations Tracking System (ARTS) to monitor management actions taken to address audit recommendations. The internal auditor provides an annual report on this subject to the Board.

Resolution of Senior Management’s Acceptance of Risks

During the quality assurance review, no instances were identified of management accepting an inappropriate level of risk that would require the Internal Audit Director to notify the Board.

Leading Practices Observed

The internal auditor is committed to continuous improvement. Several leading practices were observed that demonstrate an outstanding level of service and professionalism:

During the quality assurance review, we observed numerous practices that demonstrate outstanding commitment and professionalism. These leading practices include the following:

- The internal auditor continues to foster an excellent working relationship with the Board members, executive management, and staff members. This relationship is due to an audit process that serves the needs of management and the Board.
- Audit reports are well coordinated, well written and include background information on the areas reviewed.
- Audit workpapers are well documented, logically organized, and easily followed. The auditor documents relevant information that support the engagement results and conclusions.
- Agenda materials developed for Board meetings are provided on a timely basis and are excellent in content, format, and quality.
- The internal auditor prepared a comprehensive self-assessment as part of the planning and preparation for the external peer review.
- The internal auditor has earned four professional certifications and regularly attends continuing education offered by several different auditing and accounting organizations.
- The internal auditor is active and well-respected in the internal auditing community and serves in the Peer Review Committee of the Texas State Agency Internal Audit Forum (SAIAF). She was a key participant in the 2007 revision of the SAIAF Peer Review Manual.

Board Member and Management Comments

Interviews were conducted with the Board president, Board audit liaison, executive director, and operations director. Listed below are representative comments offered by the persons interviewed. Comments were very complimentary of the services and support provided by the internal auditor.

Jaye is prompt, thorough, reliable, consistent, and always meets deadlines.

Her presentations are succinct, not so technically-oriented, and she uses language we can understand.

Jaye is forward-thinking, methodical, very organized, and gets things done right.

She is approachable, inclusive, and keeps everybody informed.

Her audit work is thorough, well thought out, and provides rational recommendations to strengthen our processes and procedures.

She is honest, trustworthy, and has the respect of the Board and management.

Jaye has good rapport with everybody she works with and is responsive to questions.

Table 1: IIA and GAO Peer Review Ratings and Definitions

International Standards for the Professional Practice of Internal Auditing	GAO Government Auditing Standards
<p>Generally Conforms</p> <p>The assessor has concluded the following:</p> <ul style="list-style-type: none"> • For individual standards, that the internal audit activity conforms to the requirements of the standard (e.g., 1000, 1010, 2000, 2010, etc.) or elements of the Code of Ethics (both Principles and Rules of Conduct) in all material respects. • For the sections (Attribute and Performance) and major categories (e.g., 1000, 1100, 2000, 2100, etc.), the internal audit activity achieves general conformity to a majority of the individual standards and/or elements of the Code of Ethics, and at least partial conformity to others, within the section/category. • For the internal audit activity overall, there may be opportunities for improvement, but these should not represent situations where the internal audit activity has not implemented the Standards or the Code of Ethics, has not applied them effectively, or has not achieved their stated objectives. 	<p>Pass</p> <p>A conclusion that the audit organization's system of quality control has been suitably designed and complied with to provide the audit organization with reasonable assurance of performing and reporting in conformity with applicable professional standards in all material respects.</p>
<p>Partially Conforms</p> <p>The assessor has concluded the following:</p> <ul style="list-style-type: none"> • For individual standards, the internal audit activity is making good faith efforts to conform to the requirements of the standard (e.g., 1000, 1010, 2000, 2010, etc.) or element of the Code of Ethics (both Principles and Rules of Conduct) but falls short of achieving some major objectives. • For the sections (Attribute and Performance) and major categories (e.g., 1000, 1100, 2000, 2100, etc.), the internal audit activity partially achieves conformance with a majority of the individual standards within the section/category and/or elements of the Code of Ethics. • For the internal audit activity overall, there will be significant opportunities for improvement in effectively applying the Standards or Code of Ethics and/or achieving their objectives. Some deficiencies may be beyond the control of the internal audit activity and may result in recommendations to senior management or the board of the organization. 	<p>Pass with Deficiencies</p> <p>A conclusion that the audit organization's system of quality control has been suitably designed and complied with to provide the audit organization with reasonable assurance of performing and reporting in conformity with applicable professional standards in all material respects with the exception of a certain deficiency or deficiencies that are described in the report.</p>

IIA International Professional Practices Framework	GAO Government Auditing Standards
<p>Does Not Conform</p> <p>The assessor has concluded the following:</p> <ul style="list-style-type: none"> • For individual standards, the internal audit activity is not aware of, is not making good faith efforts to conform to, or is failing to achieve many/all of the objectives of the standard (e.g., 1000, 1010, 2000, 2010, etc.) and/or elements of the Code of Ethics (both Principles and Rules of Conduct). • For the sections (Attribute and Performance) and major categories (e.g., 1000, 1100, 2000, 2100, etc.), the internal audit activity does not achieve conformance with a majority of the individual standards within the section/category and/or elements of the Code of Ethics. • For the internal audit activity overall, there will be deficiencies that will usually have a significant negative impact on the internal audit activity's effectiveness and its potential to add value to the organization. These may also represent significant opportunities for improvement, including actions by senior management or the board. 	<p>Fail</p> <p>A conclusion, based on the significant deficiencies that are described in the report, that the audit organization's system of quality control is not suitably designed to provide the audit organization with reasonable assurance of performing and reporting in conformity with applicable professional standards in all material respects, or the audit organization has not complied with its system of quality control to provide the audit organization with reasonable assurance of performing and reporting in conformity with applicable professional standards in all material respects.</p>

Report Distribution

Texas Board of Nursing

Ms. Kathy Shipp, MSN, RN, FNP, Board President

Ms. Deborah Hughes Bell, CLU, CHF, Board Liaison to Internal Audit

Executive Management and Internal Audit

Ms. Katherine A. Thomas, MN, RN, FAAN, Executive Director

Mr. Mark Majek, Operations Director

Ms. E. Jaye Stepp, CPA, CIA, CGAP, CRMA, Internal Auditor