



**ANNUAL REPORT
ON
STATEWIDE INTERNAL AUDIT ACTIVITIES**

Department of Administrative Services

December 31, 2007

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Oregon

Theodore R. Kulongoski, Governor

Department of Administrative Services

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December 31, 2007

The Honorable Kurt Schrader, Co-Chair
The Honorable Mary Nolan, Co-Chair
Interim Joint Committee on Ways and Means
900 Court Street NE, Room H-178
Salem, OR 97301-4048

Re: Annual Report on Statewide Internal Audit Activities for 2007

Dear Co-Chairpersons:

It is an honor to present to you the Department of Administrative Services' third annual report on statewide internal auditing activities as required by ORS 184.360 (4).

As background, ORS 184.360 specifies that the department adopt rules to set standards and policies for internal audit functions within state government. In January 2006, we adopted Oregon Administrative Rules 125-700-0010 through 125-700-0060.

Our report contains the following information on the statewide internal audit activities for 2007:

1. Activities of the Statewide Audit Advisory Committee;
2. Summary of statewide internal audit activities in state government between July 1, 2006 and June 30, 2007;
3. Additional "value-added" work performed by the Internal Audit units;
4. Staff information including vacancies, recruiting efforts, and professional certifications of internal audit staff.

The Statewide Audit Advisory Committee approves this document. If you have questions, or would like to obtain additional information, please contact me or Pamela Stroebel Valencia at (503) 378-4037.

Sincerely,

Kris Kautz, Interim Director
Department of Administrative Services

Statewide Audit Advisory Committee

The Statewide Audit Advisory Committee is comprised of members from state government and the private sector. The committee meets six times per year. In FY 07 the following members served on the committee:

Lindsay Ball, Chair and DAS Director
Charles Hibner, Director, Oregon Audits Division
Carol Welch, Senior Director of Corporate Audit, Nike Inc.
Debbie Ferguson, Chief Audit Executive (CAE), Standard Insurance
Craig Stroud, Budget and Finance Manager, Oregon Zoo
Kingsley Click, Director, Judicial Department, (delegated to Sarah Gates, Deputy Director)
Cory Streisinger, Director, DCBS
John Radford, State Controller, DAS
Ken Rocco, Director, LFO (delegated to Dallas Weyand, Principal Legislative Analyst)
Marlene Hartinger, CAE, ODOT
Margaret McDowell, CAE, DAS
Pamela J. Stroebel Valencia, CAE (beginning May 14, 2007), DAS

Addressing Recruitment

The Statewide Audit Advisory Committee worked diligently this past year to address internal audit recruitment concerns. Last year, the committee undertook creation of an internal auditor developmental program to assist employees who meet the education requirement for an Internal Auditor 2 position, but do not meet the two-year experience requirement. Two candidates successfully completed the program and one was offered a permanent internal audit position with a state agency. The committee has a strong desire for the department to continue funding this program. Internal audit representatives continue to represent state government at various college and university career events and several agencies hosted internship positions within their internal audit units.

Expanding Outreach

Also of significant focus this past fiscal year was outreach to the internal audit community in state government. In the spring of 2007 the committee surveyed all state internal auditors and several management representatives to receive feedback on operations of the committee, relationships between internal auditors and management, and issues of concern for internal auditors.

Moving Forward

In FY 08 the committee will continue to address challenges in the area of recruitment and retention of state government internal auditors. In addition, as a result of the survey and a meeting held with the audit community the committee developed an action plan for the current fiscal year that also includes these important areas of focus:

- Revise the format agencies use to report internal audit activities to the department;
- Survey agency directors and executive management on the value of internal auditing;
- Develop training on the role of internal auditing to promote a consistent internal audit message across state government;
- Review tools to help assess appropriate internal audit coverage levels in agencies and discuss options for small agencies and audit shops;
- Develop or explore training to recommend for internal audit committee members;
- Discuss and explore options for peer/quality assurance reviews; and
- Begin to compile best practices and potential statewide issues from FY 07 annual internal audit activity reporting for continuing discussions with the internal audit community.

Overall Summary of Internal Audit Activities in State Government

The Department of Administrative Services has identified the following 29 agencies that meet the criteria established by Oregon Administrative Rule 125-700-0020 requiring an internal audit function or have created an internal audit function without qualifying under the criteria. Information contained in the table below is as of June 30, 2007.

Agency	Number of FTE	Number of Vacancies	Annual Risk Assessment	External Quality Assessment ¹ Year Completed/Due
Administrative Services	3	1	Yes	2006/2011
Agriculture	0	Contract	No	N/A
Community Colleges & Workforce Development	.5	Contract	No	N/A
Consumer & Business Services	1	0	Yes~	2004/2009
Corrections	2	0	Yes	2006/2011
Economic & Community Development	0	Contract	No	N/A
Education	1	0	Yes	N/A/2009
Employment	1	0	Yes	2005/2010
Energy	0	Contract	Yes~	N/A
Environmental Quality	0	Contract	No	N/A
Fish & Wildlife	0	Contract	No	N/A
Forestry	1	1	Yes	N/A/2009
Housing & Community Services	0	Contract	No	N/A
Human Services	9	2	Yes	2005/2010
Judicial Department	3	0	Yes	No
Justice, Department of	1	0	Yes~	N/A/2010
Liquor Control Commission	.25	Assigned	Yes+	N/A/2010
Lottery	3	0	Yes~	2005/2010
Military*	1	0	No	No
Parks & Recreation	1	1	Yes~	2006/2011 [^]
Public Employees Retirement System	3	0	Yes	2005/2010
Public Utility Commission	0	Assigned	Yes~	N/A
Revenue	1	0	Yes	N/A/2009
State Police	0	Contract	In Process	N/A/2010
Transportation	6	0	Yes	2005/2008
Treasury	1.4	0	Yes~	2007/2012
Oregon University System	13	1	Yes	2006/2011
Oregon Youth Authority	1	0	Yes	N/A/2009
Veterans Affairs	1	0	Yes	N/A/2009
TOTAL	54.15	6		

*These agencies did not submit annual reporting information in adherence with OAR 125-700-0050 (4)

~Summary template submitted – not original risk assessment; many agencies reported it would be available for review at the agency upon request

¹Required every 5 years

+Risk Assessment performed by Oregon Audits Division

[^]Report submitted was not in compliance with OAR 125-700-0055

Note: As of June 30, 2007, 6 of the 54.15 approved FTE positions were unfilled (11%); some agencies are contracting for internal audit services or have assigned the responsibility to someone other than an internal audit position of Chief Audit Executive or Internal Auditor.

Quality Assurance Reviews

In accordance with the Institute of Internal Auditors' Professional Practices Framework and OAR 125-700-0055 each agency with an established internal audit function must receive an external quality assurance review every five years.

Two agencies were due for these reviews in FY 07. Office of the State Treasurer received this review and the final report was issued in November, 2007. Treasury received a rating of generally conforms.

Oregon Judicial Department was also due for this review in FY 07, however due to the full turnover of their internal audit function (3 FTE), they have decided to wait to receive the review until it could provide value by assessing the current function.

In addition, two agencies completed self-assessments of their internal auditing processes during FY 07 following guidance set out by the Institute of Internal Auditors. Department of Corrections had no findings. Oregon State Lottery had low risk findings and determined previous findings had been partially resolved.

Professional Certifications and Advanced Degrees

In the statewide internal audit community, the stated percentages of employees hold the following professional certifications:

Certified Public Accountant (CPA)	42%
Certified Internal Auditor (CIA)	22%
Certified Information Systems Auditor (CISA)	18%
Certified Fraud Examiners (CFE)	13%
Certified Government Audit Professional (CGAP)	11%

Additional certifications held by at least one internal audit member in state government are: Certified Information Systems Manager (CISM), Certified Information Systems Security Professional (CISSP), Certification in Control Self-Assessment (CCSA), Certified Investment Derivative Auditor (CIDA), and Global Information Assurance Certification-Systems and Network Auditor (GSNA).

In addition within the audit community, the following percentages of employees hold these advanced degrees:

Masters in Business Administration (MBA)	9%
Masters in Public Administration (MPA)	5%

One internal audit staff holds a Masters in Public Policy and Management (MSPPM) and one a Masters of Taxation (MT). One internal auditor also holds a law degree, Juris Doctor.

Of the internal auditors in state government, 84% hold at least one professional designation or advanced degree.

Turnover and Recruiting

Eleven agencies (40%) had open internal audit positions during FY 07; five of which had more than one opening. One agency with a single-person audit shop had two failed recruitments for an Internal Auditor 2; one with an under fill option. A shop of three FTE had all three positions vacant for close to a full calendar year between 2005 and 2006; this shop is located in Portland and had failed recruitments on all three positions, and more than one failure on two of the recruitments. Many internal audit and agency managers reported small applicant pools for recruitments.

Several agencies requested and received internal audit positions in their 2007-2009 budgets and are working to fill positions in fiscal year 2008, including: State Police, State Lands, Environmental Quality, Student Assistance Commission, and Housing and Community Services.

Community Colleges and Workforce Development currently has a part-time internal audit function but hopes to request a full-time position in its 2009-11 budget request. Economic and Community Development is working with another agency on contracting for part of an internal audit position.

Statewide Internal Audit Activity

The scope of statewide internal audit activities go beyond issuing formal internal audit reports to include performing management reviews and special investigations, providing consulting activities, and other activities as requested by internal audit committees and agency Directors. The following information provides some insight into these activities.

Audits and Reviews

The Department of Administrative Services (department) requested agencies provide certain information about the internal audit activity for their agency. The department received information from all but two of the agencies required to have an internal audit function (Oregon Administrative Rule 125-700-0020 Internal Auditing Requirements).

The department's review of the information submitted by the agencies indicates that much of the work performed by the audit function is specific to that agency's programs. For example, Oregon University System reviewed its Student Loan Program. Internal Auditors track the status of corrective action on items recommended in audit reports and rank the risk impact of no implementation on a scale of high, medium, and low.

Agency Reported Audits and Reviews July 1, 2006 through June 30, 2007

Agency	Name of Audit/Review
Administrative Services	<ul style="list-style-type: none"> ➤ Electronic-Waste Process Controls Review – State Services Division ➤ EBay Security Controls Review - State Services Division ➤ Report on the Follow-up of Prior Internal Audit Findings and Recommendations ➤ Small Purchase Order Transaction System (SPOTS) Cards – Operations Division Review
Consumer and Business Services	<ul style="list-style-type: none"> ➤ Internal Control for Revenue Collection of Retaliatory Tax
Corrections	<ul style="list-style-type: none"> ➤ Health Services Purchasing Review ➤ Staff Training ➤ Health Services Budget
Education	<ul style="list-style-type: none"> ➤ State School Fund
Energy	<ul style="list-style-type: none"> ➤ Energy Loan Program Database Review
Human Services	<ul style="list-style-type: none"> ➤ Travel Reimbursement Information Processing System ➤ Behavior Rehab Services - The Next Door
Oregon Judicial Department	<ul style="list-style-type: none"> ➤ Multnomah Parking Program ➤ 15 Trust Check Audits ➤ State Court Service Center Office Supply Operations

Agency Reported Audits and Reviews (continued)

Oregon State Lottery	<ul style="list-style-type: none"> ➤ Confidential Report: Phase II - User Access Management: Epicor ➤ VISA Card Program Review ➤ Follow-up to Prior Audit Findings ➤ Marketing Scratch-It Review Process Audit
Public Employees Retirement System	<ul style="list-style-type: none"> ➤ Employee Accounts ➤ SPOTS ➤ Payroll & Overtime ➤ Fictitious Accounts
Revenue	<ul style="list-style-type: none"> ➤ ACH Debit and Credit Processes
State Police	<ul style="list-style-type: none"> ➤ 9-1-1 Emergency Reporting System Program
Office of the State Treasurer	<ul style="list-style-type: none"> ➤ Change Management/Systems Development Life Cycle Compliance Audit ➤ Access Control ➤ Private Equity Internal Controls Audit
Transportation	<ul style="list-style-type: none"> ➤ DMV Field Office Audit Report Jan-Jun 06 ➤ Human Resource Procedures for Investigating Allegations of Asset Misuse ➤ Voyager Fuel Cards ➤ Internal Controls and Oversight of Cell Phones ➤ DMV Field Office Audit: Change of Manager ➤ Oversight of the Board of Maritime Pilots ➤ Accountability and Transparency of Board of Maritime Pilots ➤ Office of Maintenance Cash Handling
Oregon University System	<ul style="list-style-type: none"> ➤ Information Security Policies ➤ English Department ➤ Student Loan Program ➤ Admissions ➤ PICMET ➤ Bookstore Operations ➤ Central Fiscal Controls ➤ Academic International Programs ➤ Banner Student Grades ➤ Procurement Cards ➤ Departmental Information Systems ➤ Grant Payments ➤ Performance Evaluations & Leave Reporting
Veterans' Affairs	<ul style="list-style-type: none"> ➤ Contractor Expenses Audit ➤ Klamath County Veterans Service Office ➤ Tillamook County Veterans Service Office ➤ Linn County Veterans Service Office
Oregon Youth Authority	<ul style="list-style-type: none"> ➤ Review of the Implementation of Recommendations in Internal Audit Engagement Report IA05.1 ➤ Serious Incidents and Internal Controls in Family Foster Care Review

Consulting Activities

Consulting activities are an on-going activity by agency internal auditors. Many Chief Audit Executives participate on their agency's executive teams as a *non-voting* advisory member. In addition, some auditors serve on committees within their agencies when new programs are being established to ensure controls are adequate.

The Institute of Internal Auditors defines consulting services as advisory and related client services activities, the nature and scope of which are agreed with the client and which are intended to add value and improve an organization's governance, risk management, and control processes without the internal auditor assuming management responsibility. Consulting activities can include: reviewing processes and making recommendations for improvement, reviewing new policies and procedures for adequacy of controls, providing facilitation services, and conducting training.

Other Audit Activities

Other key activities of the Internal Audit units included the following:

- Acting as liaison with the Secretary of State Audits Division as they perform financial, performance, and information technology audits of agencies and other external entities who perform audits of state government agencies;
- Participation in recruiting and career fairs;
- Participation in national, state, and local professional organizations such as:
 - American Institute of Certified Public Accountants;
 - Oregon Society of Certified Public Accountants;
 - Institute of Internal Auditors;
 - Information Systems Audit and Controls Association;
 - Association of Certified Fraud Examiners;
- Participation on various committees within agencies;
- Providing training to management and agency staff to raise awareness of pertinent topics including internal controls, fraud, ethics, managing resources, information security, Payment Card Industry Standards (PCI), capitalization of assets, federal reporting requirements and;
- Receiving management training.

Agency Reported Value Added Activities

Agencies reported to the Department of Administrative Services that Internal Audit units have added value and assisted management in making improvements to the operations and performance of the agency's programs. In addition to the types of consulting and other activities described previously, a few specific examples of activities reported for FY 07 are as follows:

Administrative Services:

- Completed a Financial Controls review for the Office of Health Policy and Research.
- The Chief Audit Executive staffs the Statewide Audit Advisory Committee (SAAC) and holds meetings with pertinent members of the internal audit community to discuss issues SAAC is working on and obtain understanding, acceptance, and support for initiatives.

Community Colleges and Workforce Development:

- Performed sub-recipient monitoring for WIA federal grant awards passed through to local areas, such as community colleges and non-profit organizations. Assisted program staff in conducting annual program and fiscal monitoring of the Department's seven Local Workforce Investment Area offices and certain lower level sub-recipients.
- Reviewed contracts between community colleges and Joint Apprenticeship Training Committees (JATC) to determine compliance with contract terms and accuracy of enrollment and course completion by student apprentices' reported to the colleges by the JATC.
- Periodically reviewed general ledger and federal grant transactions to verify the accuracy of recorded transactions.

Consumer and Business Services:

- Provided feedback regarding data security and identified areas where sensitive and/or confidential hard copy information was maintained in unsecured areas to help ensure compliance with Senate Bill 583 and the Statewide Data Classification policy.

Corrections:

- Assisted in the facilitation of the Food Quality Review Group that independently inspected the quality of the department's food storage and production. The review group provided assurance of the overall quality of food storage and meal production, while also providing minor recommendations for improvement.
- Performed reviews of three topic areas: the MCCF/SCI Staff Recreational Fund; Personal Mileage Reimbursements; and Payroll – Employee Allegation.

Forestry:

- The Quality Assurance Program issued two Management Letters in fiscal year 2007 covering personnel internal investigation topics.
- The Program Director regularly received requests for, and provided input and research into, ethics and compliance related topics for personnel of varying positions throughout the agency.

Human Services:

- Issued 10 consulting engagement reports on topics including: ODC/ODHHS, EBT Card Controls, Klamath Lake Employment Training Institute, DMAP Interpretive Services, and Josephine County Mental Health.

Justice

- Provided consulting services to a program regarding best practices and internal controls for handling incoming checks. As a result of the auditor's suggestions, the program streamlined its

process for efficiency and implemented additional controls. To provide a tool to other program managers, the internal auditor created a reference sheet entitled "Basic Best Practices of Internal Controls: Handling Cash and Checks." The auditor presented the document to executive management, who distributed it and discussed with their managers and staff. Program managers have invited the internal auditor to speak to their staff and managers on this topic and to follow up by conducting reviews to assess effectiveness of controls.

- Provided quality assurance services to a major federal grant program by offering options and suggestions for developing certain procedures to ensure its sub-recipient monitoring program would comply with federal guidelines. Changes discussed included how to apply a risk-based approach to ensure adequate coverage of sub recipients, review of key sub recipient fiscal controls, and best practices for documenting the results of sub recipient monitoring activities. The recent Single Audit follow-up review by external auditors determined that the program met the federal requirements.

Oregon Judicial Department:

- New Internal Audit staff became acquainted with the department.
- Issued 6 management letters on various topics.

Oregon Lottery:

- At the request of the Information Technology department, conducted a formal consulting engagement to review access within the Lottery's Video System. Internal Audit identified improvements that could be made to existing access levels to ensure user access was appropriately limited. Management used the report to improve user access within the Video System.
- Performed and issued reports on continuous monitoring of user access using a data query tool to provide monthly reports of user access within two Lottery systems. The reports are designed to provide management with information on segregation of duties, timely termination of user access rights, and that sensitive access is appropriately limited. Management used some information reported to improve user access within the systems.
- Managed two audit contracts of a CPA firm to perform an annual SAS 70 audit of the major service provider. The audit provides Lottery and the Oregon Audits Division assurance that controls around the systems are adequate.

Public Employees Retirement System:

- Provided consulting services to management on a variety of topics throughout the year.

Revenue:

- Assisted in implementing or revising multiple Information Technology controls for Federal and state as they related to the Department of Revenue.
- Assisted in increasing controls over cash handling.
- Assisted in providing recommendations for controls over paperless processes.
- Performed reviews and consulting engagements at several field offices and of several programs.

Transportation:

- At management's request, auditors reviewed two public transit districts to assess their governance structures, accountability mechanisms, and financial and managerial procedures. That analysis led Audit Services to identify opportunities for the Public Transit Division to increase monitoring activities, clarify expectations and deliverables in grant contracts, and provide additional materials that would support the ability of transit districts to improve, such as examples of best practices, performance matrices, and definitions.

- Provided information to statewide agreement coordinators on opportunities to improve intergovernmental agreements. Audit Services also serves in an advisory capacity to the Contract Leadership Team, which provides oversight and coordination of agency contract activities.

State Treasurer:

- Performed a Banking Staffing Review, analyzing staffing needs based on internal and external customer business needs and current workload.
- Developed a PCI risk evaluation tool that has allowed state agencies to understand and comply with this complex security standard.
- Provided Quality Assurance for the Debt Management system replacement project.
- Performed due diligence reviews of investment consultants and custodians.

Veterans Affairs:

- Provided informal consulting services including advice and counsel to agency executive management and program managers throughout the year.

Oregon Youth Authority:

- Performed ongoing consulting engagements during FY07 regarding the implementation of a system for Enterprise Risk Management, aligning performance measures to high level objectives.
- Participated as a team member on a special review team and worked to review controls and internal environment issues at one of the agency's camps.