

Fiscal Year 2016
ANNUAL REPORT OF
INTERNAL AUDIT
ACTIVITIES

State of Rhode Island
Department of Administration
Bureau of Audits

Bureau of Audits
Annual Report on Internal Audit Activities
FY 2016

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I. EXECUTIVE SUMMARY

Introduction

The State of Rhode Island Executive Branch of government is undergoing a significant amount of changes initiated from both internal and external sources. Some of these changes include:

- Limitations of available funding to accomplish strategic objectives
- Organizational and operational efficiency initiatives at the program, department, and agency-wide level
- Transition of key leadership and operational positions
- Expanding use of emerging technology such as cloud services

These changes indicate opportunities for exciting strategic developments for the State; however, they also expose our organization to a significant amount of operational, financial, and reputational risks. The role of Internal Audit (IA) is to work proactively with management to navigate these risks and provide assurance that existing governance, risk management, and control processes are in place and optimized for effective and efficient risk mitigation. This report highlights the outcomes of key activities performed by Internal Audit during Fiscal Year (FY) 2016 to help management identify and address significant risks facing the Executive Branch of government. Additionally, this report will provide statistical details about our unit's performance metrics and utilization of resources.

This Annual Report of Internal Audit Activities contains the following sections:

- **System-wide audits** – Results of these audits performed with a common focus and scope of work by the Bureau of Audits. (Page 4)
- **Significant and recurrent control issues** - A summary from the body of Internal Audit work performed during the year. (Page 4)
- **Executive Branch initiatives** - An update on Internal Audit's participation. (Page 5)
- **Internal Audit Program** - An overview of improvements implemented in governance, methodology, and systems. (Page 6)
- **Statistical Information** - A summary of the system-wide Internal Audit Program for FY 2016. (Page 7)

FY 2016 Statistical Highlights

During FY 2016, the Bureau of Audits:

- Completed 89% of the approved Internal Audit plan (goal 75%).
- Completed audit, advisory services, and investigation projects resulting in 17 public reports.
- Produced 173 recommendations for improvement to governance, risk management, and control processes with corresponding agreed upon Management Corrective Actions (MCAs)
- Validated that 238 MCAs were completed by management
- Summary of MCAs balances and status:

Summary of MCA Balances as of June 30, 2016	
Beginning MCAs (open at start of FY 2015)	260
Ending MCAs (open at the end of 2016)	195
Outstanding MCAs	
High risk MCAs	53
Medium/low risk MCAs	142

Summary and Conclusions

We acknowledge that management has ultimate responsibility for establishing internal controls to manage risks. We further note that management has taken steps to improve accountability and controls by developing and implementing performance metrics. In conjunction with the 17 Audit, Advisory Services, and Investigation public reports issued, we identified no conditions believed to represent material deficiencies in internal controls to the Executive Branch system as a whole from a financial standpoint.

Further, based on our FY 2016 work, we can assert the following as being generally true with no reportable exceptions:

1. There is respect for the Internal Audit Program objectives; a high level of cooperation is received, and there is no interference with either the accomplishment of our tasks or our responsibilities to report to The Group.
2. Management works collaboratively with Internal Auditors to address issues raised during Audits, Advisory Services engagements, and Investigations.
3. Management is comfortable seeking out Internal Audit for advice and consultation on matters with internal control implications when brought to their attention.
4. The Bureau reports all matters of importance to The Advisory Group (the Group).
5. There are opportunities for the Departments and Agencies to implement more effective controls in a number of areas, and there are ongoing challenges to achieving effective controls and compliance.

II. INTERNAL AUDIT PROGRAM – RESULTS & ANALYSIS

A. System-wide Audit Results

System-wide audits are conducted for the purpose of reviewing a prevalent existing or potential issue and determine possible risks. Typically, these audits are performed as a result of our risk assessment or at the request of management, the Group, and/or the Governor, and have a common focus and scope of work. Results may be summarized from a system perspective, and key themes are addressed by leadership or comparisons may be made between departments and agencies. The following is an overview of system-wide audits performed with the results and themes summarized.

Financial Management Controls – The financial management units monitor and manage the overall financial health of their respective organizations. These units are responsible to follow sound accounting and control principles, monitor budget to actual expenditures, and to process financial transactions. We performed audits to assess the effectiveness and efficiency compliance, and the strength internal controls associated with the day to day operations. We found inefficiencies with the purchasing and payment operations at all departments or agencies audited. We did not find significant weaknesses in internal controls over day to day operations. Management is addressing noted issues by correcting and/or implementing the Management Corrective Actions (MCA) within the agreed upon time frame.

B. Significant and Recurrent Internal Control Issues

Many of the significant and recurrent internal control issues are specific to the management environment where the issues were identified. However, other issues are the result of a broader, system-wide cause and may require continual attention by management. From the majority of audit work performed during the year, including investigations, the following are the most significant and recurrent control issues.

IT Security and Information Privacy (repeated) - We continue to identify significant control weaknesses related to IT security and protection of sensitive information, including inadequate system access controls and insufficient physical controls over IT equipment. Ensuring controls are in place across the organization is challenging due to the decentralization of IT infrastructure and organizational responsibility. Many departments have not yet performed an IT security risk assessment or documented an IT security plan to address higher risk areas. Ongoing efforts to address IT security and information privacy control issues include enhancing or refining the IT governance structure, improved monitoring of network activity, and training and awareness programs. Internal Audit will continue to prioritize this area for audit and advisory activity in the next fiscal year.

C. Internal Audit's Participation in Initiatives

Internal Audit has continued to partner with management to support key initiatives and priorities both at the program and agency level. This section highlights some of the key areas in which Internal Audit has provided support.

State Employee Worker Compensation Program and DLT Billing Evaluation - In response to a management request, the Bureau of Audits served as an adviser during a review of the worker compensation program. The report from the consultant evaluating the options to improve is due to management in the near future. Additionally, the Bureau discovered a discrepancy with the State's annual assessment from the Department of Labor and Training Workers Compensation Administrative Fund. We corrected the job classification information supplied to DLT; this action resulted in savings in excess of \$600,000 over last fiscal year cost.

Fraud Detection and Prevention Initiative – A reduction of fraud, waste and abuse is part of the Governor's initiative to improve government operations. The Bureau of Audits is spearheading the acquisition of off the

shelf/open source software as a solution to this initiative. The RFP was issued July 13th to engage a vendor to identify and implement the technology, and subsequently train staff. We anticipate net savings/cost avoidance/recoupment to be \$1.5M for FY 17.

Enterprise-wide Federal Grant Management - To address a repetitive single audit finding, the Grants Management unit within the Bureau of Audits is in the planning phase for an RFP to acquire grant management software.

Purchasing Regulation Rewrite – The Bureau of Audits loaned a senior internal auditor to the Office of Regulatory Reform (ORR) to study existing regulation and write updated regulation and related legislation. This staff member will be loaned to the ORR again during FY17 to work on this project.

D. Improvements to Internal Audit Methodology, Processes and Systems

Internal Audit operates in an environment of continuous change. We must continue to adapt and improve our methodologies, use of technology, communication strategies and expertise in order to meet the challenges of new auditing standards, emerging risks, and changes to the environment. This section outlines some of the improvements we have made in these areas.

Consolidation of Internal Audit Units – The passage of the Rhode Works bill during March transferred the Department of Transportation External Audit unit into the Bureau of Audits. FY17 Budget Article 4 consolidated the internal audit and fraud units from the University of Rhode Island, Office of Post-Secondary Commissioner, and Department of Human Services into the Bureau of Audits. The budget article moved the Bureau into the Office of Management and Budget and renamed the unit the “Office of Internal Audit”. The new office consists of three functional units: Continuous Auditing, Performance and Efficiency Auditing, and Fraud Detection and Prevention. The new unit organizational chart can be found at Appendix 1.

Quality Assurance - The Institute of Internal Auditors’ (IIA) professional standards require that an external Quality Assessment Review (QAR) of an Internal Audit function be performed at least once every five years to be compliant with auditing standards. We entered into a memorandum of agreement with North Carolina Office of Internal Audit to perform the QAR. The QAR team will be on site from August 22nd to 25th. This year, in preparation of our first external QAR, we updated our policies and procedures manual to include the continuous auditing unit, updated our audit quality questionnaires, electronically distributed the questionnaires after each audit and performed an internal review of work papers for compliance with the standards. We believe we shall receive certification by September 1st.

Continuing Education – The Bureau of Audits’ policy is for each employee to annually attend at least ten hours of professional continuing education. All staff complied with or exceeded the requirements of this policy. These efforts help ensure that our audit staff is informed of emerging risk issues and auditing techniques, and provides them with the opportunity to receive necessary continuing education requirements to maintain their professional certifications.

E. Statistics

This section provides a summary of statistical information on the system-wide Internal Audit program for FY 2016. Resource and effort data is summarized and analyzed by type of audit service and across functional areas, demonstrating the breadth of coverage provided. Management corrective actions are analyzed by functional area, severity, and status.

1. Resources and Effort

Table 1 – Internal Audit Program Staffing provides statistics on our Internal Audit staff, benchmarked against the plan and prior year figures, including a summary of statistics in experience, education, professional certifications and turnover. Headcount levels changed due to the consolidation of the External Audit unit from RIDOT as compared to the prior year. This increase in staffing levels, along with one FTE on leave throughout the entire first quarter of the fiscal year, has had a direct impact on the statistics. Therefore, the turnover rate decreased over FY 15 levels.

Qualification statistics for our staff declined in comparison to the prior year due to the consolidation of staff who do not have certification.

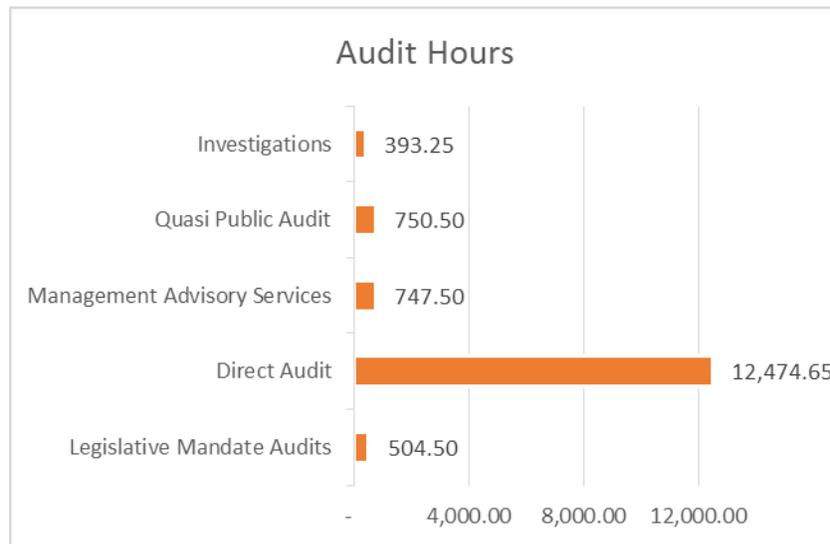
Table 1 –Internal Audit Program Staffing

Internal Audit Staff	FY16 Plan	FY16 Actual	Prior Year Actual
Authorized	12	18	12
Average Actual Filled	11	17	9
Percent Filled	92%	94%	75%
Ending Head count	11	17	9.4
Turnover	8%	6%	25%
Training hours per auditor	30	28	31
Qualifications			
Average Years Total Audit Experience	N/A	14 years	16 years
Average Years BOA Audit Experience	N/A	7 years	10 years
Average Years Audit Chief Experience	N/A	30 years	30 years
Percent of Audit Staff with Bachelor Degree	N/A	100%	100%
Percent of Audit Staff with Advanced Degrees	N/A	24%	67%
Percent of Staff holding Professional Certifications	N/A	53%	78%

N/A Not applicable to plan data

Each year, approximately 70 to 75% of our staff time is allocated to direct hours. Direct hours include all effort spent completing our annual plan of audit, advisory and investigation projects, as well as audit support activities such as IT support, system wide audit support, audit planning and quality assurance.

Table 2 – Projects provides a summary of our direct hours including a breakdown by category, service line, number of completed projects in each area, and average hours per completed project.



Projects	FY16 Plan	FY16 Actual	Prior Year Actual
Risk Based Audits			
Audit Program Hours	10,300	13,671	7,816
Percent of total project effort	80%	92%	66%
Number of Completed Projects	16	13	13
Management Advisory Services			
Advisory Service Hours	1,300	0	2,542
Percent of total project effort	10%	0%	21%
Number of Completed Projects	N/A	0	15
Mandated Audits			
Mandated Hours	400	504	652
Percent of total project effort	3%	3%	5%
Number of Completed Mandated Audits	N/A	1	3
Investigations			
Investigation Hours	200	0	198
Percent of total project effort	2%	0	2%
Number of Completed Investigations	N/A	0	3
Quasi-Public Audits			
Audit Program Hours	200	695	191
Percent of total project effort	2%	5%	2
Number of Completed Quasi Public Audits	1	3	1
Total			
Audit, Advisory Services & Investigation hours	12,400	14,870	11,399
TeamMate Support and Quality Assessment	500	257	468
Total Direct Hours	12,900	15,127	11,867
Summary Information			
Total Number of Completed Projects	19	29	32
Number of projects per auditor	N/A	2.36	3.56
Percent of Audit Plan Completed	N/A	89%	81%

Chart 1 – Completion of Audit Plan shows the results of our focus on audit plan completion over the past three years. We continue to exceed our established benchmark for audit plan completion (75%).

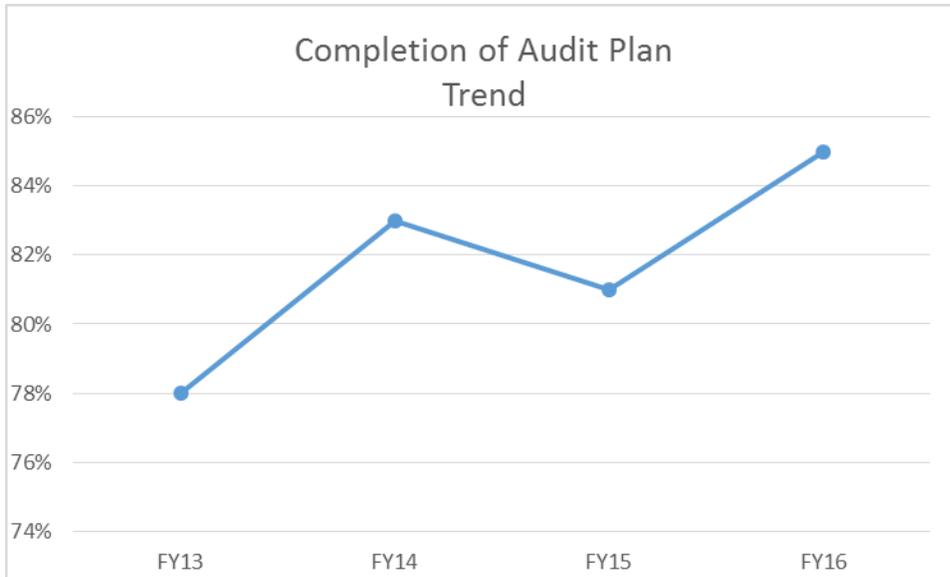
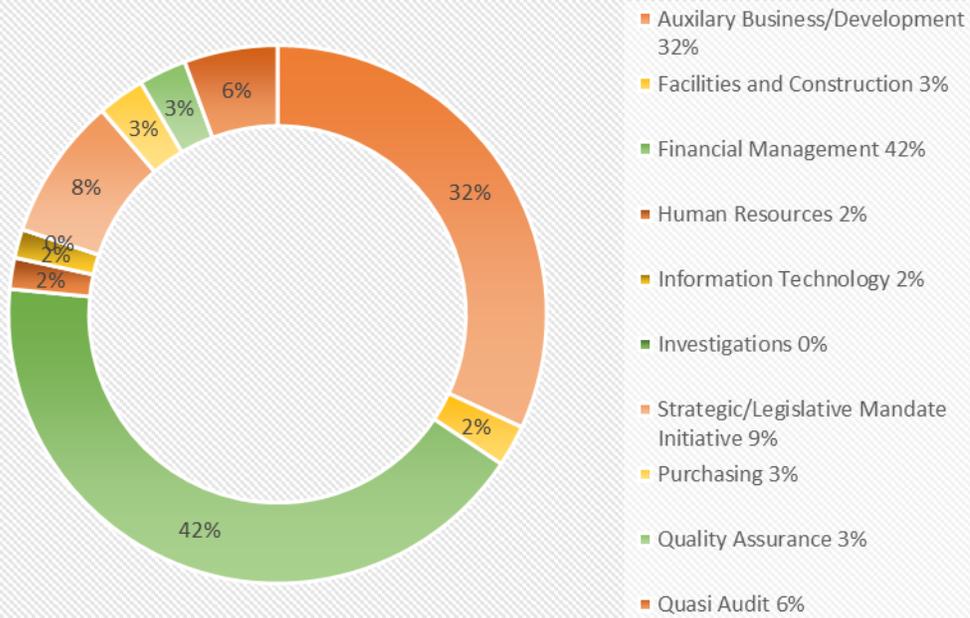


Chart 2 – Distribution of FY 2016 Hours - depicts the breadth of coverage of Internal Audit project hours over the major functional areas. Our effort remained concentrated in the areas of financial management, and auxiliary business/development.

Distribution of Audit Hours



2. Management Corrective Actions

MCA Distribution

As previously indicated, our FY 16 audit program work produced 17 audit, and advisory service reports, resulting in 173 MCAs. As shown in Table 3 – Comparison of MCAs and Hours, the distribution of MCAs correlates with the effort expended across the functional areas, with the exception of a few areas.

Table 3 – Comparison of MCAs and Hours

Functional Area	MCA %	Hours %
Financial Management	64%	54%
Strategic/Legislative Mandates	4%	12%
Information Technology	0%	0%
Auxiliary, Business & Employee Support Services	32%	34%
Human Resources	0%	0%
Facilities & Construction	0%	0%

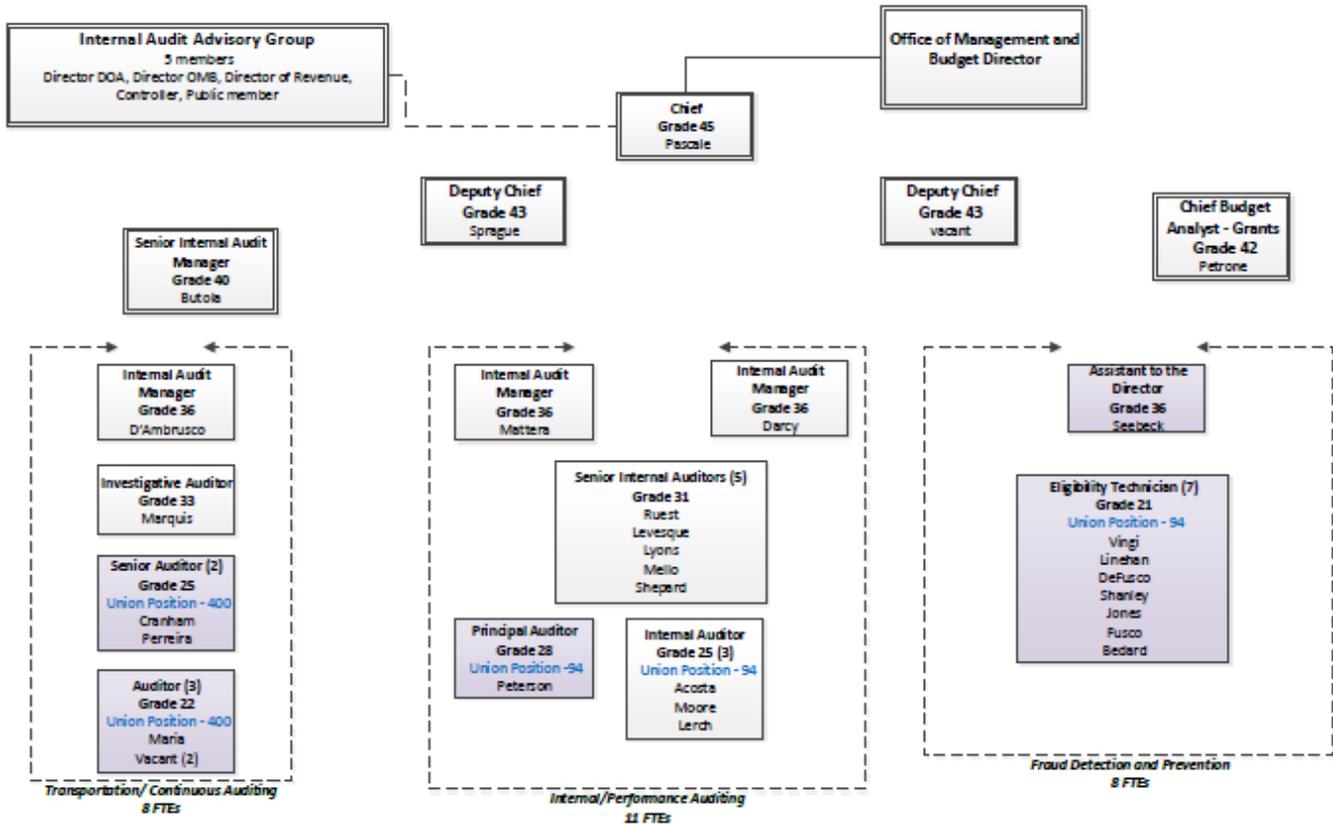
Status of Completion of MCAs

MCAs are classified initially as open and are only moved to closed status after validation by auditors that the agreed upon corrective actions have been taken or the associated risk has been adequately mitigated and sustainable improvement has been achieved.

During FY 16, 173 recommendations for improvement were made. All recommendations are assigned an estimated completion date and are tracked. The status of all Bureau reports that contain outstanding recommendations is shown in the chart below.

Tracked Management Corrective Actions (MCAs)									
As of June 30, 2016									
Agency	Report Title	Report Date	Not Due	0-3 Months	3-6 Months	6-12 Months	12-18 Months	Over 18 Months	Total Outstanding
DOA	Security Policy Gap Analysis	3/3/14						68	68
DCYF	Procurement Contract Controls	7/30/15				7	12		19
DOA	Facilities Maintenance and Repairs	10/13/15	14						14
DCYF	Center for Southeast Asians	10/6/15	2						2
DOA	Purchasing Delegated Authority	10/22/15	18						18
DPS	Fire Marshall	2/3/16	9						9
Quasi	RI Turnpike and Bridge Authority	3/9/16	1						1
DCYF	RI College Child Welfare Institute	3/29/16	1	2					3
DCYF	Child and Family service of Newport	4/27/16	2						2
DCYF	Family Service of RI	4/28/16	2						2
Quasi	RI convention Center Authority	4/29/16	1						1
	Rhode Island College	6/20/16	44						44
BHDDH	Contract Management Practices	6/16/16	10						10
Quasi	Rhode Island Higher Education Assistance Authority	6/29/16	2						2
Grand	Grand Total		106	2	0	7	12	68	195

APPENDIX 1 – ORGANIZATION CHART – Effective July 1



Office of Internal Audit
 Positions presented as Consolidated per Budget Article plus addition of Grants per OMB
 Total FTE count = 32
 Note: Assistant to the Director - Grade 36 added with Budget Amendment

Position titles shaded in grey will be eliminated via attrition and replaced with more recent Audit titled positions

Auxiliary/Business Development

Department of Administration

- Limited Scope Audit Administration of Facilities Maintenance and Repairs
- Review of State Agencies' Usage of Master Price Agreement 417 (MPA-417) "Media Buying Services"
- Audit of Delegated Purchasing Authority Controls

Department of Public Safety

- Rhode Island Department of Public Safety, State Fire Marshal's Practices and Procedures Performance Audit
- Rhode Island Department of Public Safety, Division of Sheriffs' Practices and Procedures Performance Audit

Financial Management

Behavioral Healthcare Developmental Disabilities and Hospitals

- Audit of Contract Management Practices of BHDDH Department of Children, Youth and Families
- Limited Scope Audit of the Department of Children, Youth, and Families' Procurement and Contract Management Controls in Place during Fiscal Year 2015
- Limited Scope Contract Compliance Audit of the State of Rhode Island Vendor, Center for Southeast Asians
- Limited Scope Contract Compliance Audit of the State of Rhode Island College's Child Welfare Institute
- Limited Scope Contract Compliance Audit of the Rhode Island Vendor, Child and Family Services of Newport County
- Limited Scope Contract Compliance Audit of the State of Rhode Island Vendor, Family Service of Rhode Island

Department of Revenue

- Taxation Cash Controls over Revenues Collected

Rhode Island College

- Limited Scope Audit of Financial Controls and Human Resource Practices at Rhode Island College

Legislative Mandate

Department of Administration

- Financial Integrity and Accountability Report

Quasi-Public Audits

Rhode Island Convention Center Authority

Rhode Island Turnpike and Bridge Authority

Rhode Island Higher Education Assistance Authority

APPENDIX 3 – FISCAL YEAR 2015 OUTSTANDING RECOMMENDATIONS GREATER THAN SIX MONTHS

There are two audit reports that contain outstanding recommendations that past due more than six months. The Bureau continues to pursue implementation of these outstanding recommendations. In the case of the recommendation made to the Division of Information Technology, we recommend the Group consider the hiring of a Chief Information Officer before taking additional action to require implementation of the recommendation.

DOA, Security Policy Gap Analysis – The States Chief Information Officer will be responsible for a comprehensive rewrite of the department’s security policies. This hiring is in process. Once the new person is on board, we expect all outstanding MCAs to be addressed.

DCFY, Procurement Contract Controls – The DCYF is in the process of implementing these recommendations as part of a project that is redesigning most of the agency’s policies. The agency has made significant progress in the implementation of its new processes and these recommendations are expected to be completely addressed in the near future.