

# Utah State Board of Education Internal Audit Department

## Module 3 Script - LEA Audit Committee (10,000+ Enrollment)

November 23, 2020

## Introduction

Welcome audit committee members.

This training is specifically for audit committee members that are serving in local education agencies with more than 10,000 students. Please make sure you have participated in Module 1 and Module 2 trainings prior to participating in this training as they provide context for the content of this Module.

Utah law requires an LEA audit committee to establish an internal audit program that provides internal audit services for the programs administered by the LEA, if the LEA has 10,000 or more students. (53G-7-402, R277-113-4(6)(a))

So, how do you establish an internal audit program?

## Audit Director

As a first step, the LEA board will need to hire an internal audit director.

The "audit director" is the person who directs the internal audit program (53G-7-401(2)). One responsibility of the audit committee is to advise the LEA board in the appointment of the audit director or in contracting for internal audit services. (R277-113-4(6)(b))

The LEA board, advised by the audit committee, has two choices: 1) it can appoint or direct hire the internal audit director, or 2) it can contract for internal audit services. If the Board contracts for services, a representative from that organization will serve as the LEAs internal audit director. (53G-7-402(3))

The Utah State Board of Education does not recommend one option over the other. LEA boards should just ensure that they consider which option will provide the best value for their LEA. In considering value, please be aware of the requirements for the internal audit program.

### Internal Audit Program

What does the law say about the program you must create?

First the law states that internal audit is an "independent appraisal activity". (53G-7-401(4))

The law further requires that the internal audit program must (53G-7-401(5)):

- (1) be independent of the local education agency offices or other operations, and
- (2) objectively evaluate the effectiveness of the local education agency governance, risk management, internal controls, and the efficiency of operations.

Furthermore, the internal audit program must be conducted in accordance with [professional auditing standards].

Did you catch that independence was mentioned twice? Independence was covered in Module 1; but, as a reminder, independence is defined as "the freedom from conditions that threaten the ability of the internal audit activity to carry out internal audit responsibilities in an unbiased manner." In other words, the internal auditor cannot be supervised by LEA administration; they must directly communicate and

interact with the board to avoid conflicts of interest. Remember, an individual reviewing the work of LEA administration, who is also supervised by LEA administration is technically a monitor, not an auditor.

Independence helps ensure that auditors can be objective.

The audit committee must establish an internal audit program that objectively evaluates the effectiveness of the LEAs governance, risk management, internal controls, and the efficiency of operations.

This obligation for objectivity is extremely significant and important as it is at the heart of transparency and accountability. In other words, the internal audit program will help ensure that your LEA is doing what it says it is doing in every program and with every dollar.

Finally, the internal audit program needs to be done in accordance with professional internal auditing standards. Remember our discussion about Redbook and Yellowbook in Module 1? These are the professional internal auditing standards that must be followed. These standards include requirements for continuing professional education for the internal audit director, as well as requirements for the knowledge, skills, and abilities needed to perform their responsibilities.

#### Hire or Contract

So back to the decision – hire or contract? The LEA board makes that decision after considering the requirements for an internal audit program – independence, objectivity, and compliance with professional standards. And all of this to provide you with information so you can fulfill your governance responsibilities as a board member.

If you choose to hire an internal audit director, you will appoint that individual similarly to the appointments of the Superintendent and Business Administrator. Instructions for that process are found in Utah law (53G-4-304), which states,

- (1) A local school board may appoint other necessary officers who serve at the pleasure of the local school board.
- (2) These officers shall qualify by taking the constitutional oath of office before assuming office.

If you choose to contract for internal audit services, the contracted entity will be considered an “other local school board officer” that reports directly to the board. Also, you must follow Utah Procurement Code (63G-6a) and you should ensure that your request for proposal or competitive bids process includes the requirements in law and rule (R123-5), such as that the auditors follow professional standards.

Your internal audit director will become an invaluable asset to your audit committee. They are your assurance service expert, and they can help support the audit committee in fulfilling their responsibilities.

## **CASE STUDY**

To reiterate what was just discussed, in our Roslyn School District example discussed in the prior training Modules, one of the recommendations in the audit done by the New York State Comptroller's Office is:

"The Board should establish an audit committee to perform duties that include: Oversight of the internal auditor selection process." (Anatomy of a Scandal p.16-17)

## **Internal Audit Policies and Procedures**

With your internal audit director in place you'll want to work with them to establish necessary policies and procedures – this is required by professional auditing standards.

These policies and procedures will help ensure compliance with auditing standards and ensure an efficient and effective internal audit program.

Necessary policies and procedures will generally include the following:

- Internal Audit Charter
- Risk-based Audit Plan
- Audit and Reporting Processes
- Non-audit Services
- External Audit Liaison
- Quality Assurance

## **Audit Plan**

Once the process for developing a risk-based audit plan is in place, the internal auditor can implement it in collaboration with the audit committee.

Generally, the audit plan should be reviewed and updated at least annually; because it is based on risk though, it could be updated more frequently. (53G-7-401(3), R277-113-4(6)(d))

To make sure we are all on the same page about risk – risk is defined as an event that could impact the achievement of your objectives. So before spending time on risk, please make sure LEA objectives have been determined.

An audit plan is a prioritized list of audits, based on risk, to be performed by an internal audit program within a specified period of time.

There are many ways to go about identifying and assessing risks, including consideration of

- Concerns from hotlines or media,
- Board member and administrator observations, and
- Performance or procedural questions, including from audits done by other LEAs, the state, and other organizations.

Following the established policies and procedures, risks are included on a preliminary list and are assessed – the assessment could be high, medium, low, a scale of 1-5, a matrix, or whatever works best for your LEA.

Internal audit should seek input from LEA administration on the risk assessment. Internal audit should also collaborate with the audit committee on the risk assessment. Based on these discussions the proposed audit plan is developed.

The audit plan should outline the high-level scope and objectives of each audit – meaning what questions is the audit trying to answer. The audit plan should also list the projects in priority order; priority being based on risk. So, priority #1 is the most significant risk, priority #2 is the second most significant risk, and so on. The audit plan will also include estimated project timelines and necessary resources to complete projects.

Ultimately the audit committee will make a recommendation that the board adopt the audit plan with its prioritized list of projects. The audit committee and board should particularly be aware of resources and timelines for audits to ensure they can be done in a timely manner to provide information to the board for decision-making.

Also, be aware that because the audit plan is risk based, projects may be added or removed as needed based on risk.

The audit committee should meet regularly, and the meeting agenda should include regular progress updates on assurance activities, including internal audits and other functions performed by internal audit. (R277-113-4(6)(e))

Please remember that while an audit is in process, it is confidential; therefore, detail information about open audits and investigations should be treated as protected until the final audit report is issued. Also be aware that audits are required to go through a quality review process, where the work and evidence is reviewed after it is completed. Sometimes the review process will identify additional questions to answer or consider information in a different light that could impact a conclusion. This means that discussion of potential audit findings should generally not take place outside of audit committee meetings. Even discussions in audit committee should be done with great care and with a reminder that potential findings should not be shared until conclusions are finalized in the audit report.

In Module 2 we discussed the audit reporting process. Once the audit report is finalized and has been released, the report can be discussed publicly.

## **Performance Evaluation**

The final steps in establishing and managing the internal audit program include evaluations of the LEAs internal audit program and the LEA internal audit director.

### The Internal Audit Program Evaluation

An internal audit program is required to have a peer review or external validation at regular intervals; under Redbook standards the review is required every 5 years; under Yellowbook standards the review is required every 3 years. This review will evaluate if the internal audit program is complying with

professional standards and offer suggestions for improvement, but it requires some internal work as well, so it should be included on the audit plan since it will require internal audit resources. The review can be contracted out, or internal audit programs can set up an exchange to help complete the required review – reviewers must meet competency standards though. For example, state internal audit programs, including the Internal Audit Department of the Utah State Board of Education, help each other out with this requirement by putting together teams of 3-4 individuals from different state agencies to review other state agencies internal audit programs. This is also a great opportunity to learn about best practices of other organizations.

#### The Internal Audit Director Evaluation (R277-113-4(6)(c))

An audit committee must conduct or advise the LEA board in an evaluation its internal audit director, whether hired or contracted. To ensure expectations are understood, it will be helpful to establish a policy and procedure for this evaluation. The policy and procedure may outline requirements for goals, progress update timelines, as well as the annual formal evaluation. The policy should be specific to if your director is hired versus if they are contracted.

There are many online resources to help you with this process. Alternatively, you could use a process similar to the evaluation process used for the evaluation of the Superintendent or School Director and Business Administrator.

### **Final Items**

A couple of last items for you to be aware of with your internal audit program.

Internal audit reports must be available, upon request, to the Audit Director of the State Board of Education, the Office of the State Auditor, and the Office of Legislative Auditor General. (53G-7-402(4))

Additionally, if an LEA audit committee discovers a significant audit matter in the course of its duties that it does not feel its internal auditor is equipped to handle appropriately, the audit committee should refer those audit matters to either the Audit Director of the State Board of Education, the Office of the State Auditor, or the Office of Legislative Auditor General. (53G-7-402(5))

### **Conclusion**

This concludes the final Training Module.

If you have specific questions on this training, please contact the USBE Internal Audit Department at (801) 538-7813 or [audit@schools.utah.gov](mailto:audit@schools.utah.gov).

As a reminder, there is also additional information available on our website: <https://schools.utah.gov/internalaudit>, and if you'd like to subscribe to our quarterly newsletter please send us an email and we'll add you to the distribution list.

Finally, if you believe some additional training would be helpful for your audit committee, the USBE Internal Audit Department is happy to schedule something with you – just give us a call or send an email.