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April 8, 1980

Ms. Paula Wolff
Program Director
Office of the Governor
Room 202 State House
Springfield, Illinois 62706

Dear Ms. Wolff:

It is my pleasure to submit to you at this time the pre-implementation report from the Project Team of Volunteers in Public Management that has been working at your request reviewing the audit process in the State of Illinois.

The Project Team wishes to express its appreciation for the cooperation it has received from the people throughout state government with whom they have worked. The volunteers on this Project are looking forward to continuing this fine relationship during the implementation stage of the Project.

As stated in the report, the Project Team feels that with the implementation of the recommendations the audit process in state government will be enhanced, and audits will be used as a more effective management tool.

The Project Team appreciates your continuing support in this effort and looks forward to working with you and your associates during the implementation period.

Sincerely,

Joseph C. Ashmead
Assistant Director
Government Affairs

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VOLUNTEERS IN PUBLIC MANAGEMENT

TO: Paula Wolff, Program Director, Office of The
Governor

FROM: The Project Team for Volunteers in Public Management

RE: Pre-implementation Report

PROJECT GOAL - Provide a data base to meet the goals as stated in Project Program and to use this data through seminars and background reference material for a permanent group in the Department of Administrative Services. To improve the audit process from the Executive Branch of Government perspective, thereby making the audit an effective management tool.

INTRODUCTION - The Project Team for Volunteers in Public Management, during the course of this report, will identify the proposed recommendations for the solution of the types of problems which exist in the internal audit functions of the State of Illinois. In making our recommendations, we will use sound business practices and procedures proven in the private sector and adapted to provide for a more effective use of audits within state government.

In order to accomplish its goal, the Project Team selected a representative sample of large and small agency audit functions and performed on site interviews of the audit managers in the selected agencies. The interviews were conducted in order to obtain background data on the types of audit work performed and the role of the internal audit function in these agencies. Further, the Project Team reviewed a sample of each selected agencies' audit work schedule (audit plan), programs, workpapers, reports and training materials to provide support for the results of the interviews.

In addition to the on site survey of a selected number of audit functions, the Project Team initially reviewed material relating to government accounting and auditing and to State government in general. The Project Team reviewed many external audit reports, met with members of the Auditor General's staff, Legislative Audit Commission staff, and attended a Legislative Audit Commission hearing to determine the role of the external auditor.

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After all the data obtained by this audit survey were thoroughly reviewed, the Project Team determined that the following additional steps would be taken to achieve the desired result inherent in the project goal.

1. Develop and present seminars for Directors of Agencies, Boards, Commission and/or Administrators in the use of an internal or external audit as a management tool.
2. Develop seminar material and present seminars for internal auditors and other appropriate State personnel in management controls that can be obtained from effective use of internal audits.
3. Establish within the Department of Administrative Services a function to review and analyze audit findings in order to assist agencies in developing and maintaining sound management and fiscal systems.

The data gathered during audit interviews points to a need to enhance the audit function in order to provide management with a professional appraisal of the strengths and shortcomings of agency operations. The implementation of the Project Team recommendations will provide an audit function that will better serve agency needs on an ongoing basis. The Volunteers in Public Management Project Team at this time would like to emphasize the need for cooperation on the part of all parties involved in order to achieve the successful completion of the project. It is the expectation of the Volunteers on the Project Team that a positive and forceful effort will be made by the Office of the Governor, the Department of Administrative Services, all Agency Directors and Auditors, in order to implement the recommendations contained in this report.

I. TYPE OF AUDITS TO BE PERFORMED:

The Project Team investigation has indicated that internal auditing presently being performed in state agencies reviewed does not adequately cover the full extent of operations within the agencies. Financial and Compliance internal auditing is being performed only on a limited basis. The agencies surveyed did not have detailed audit programs to cover all major functions established by statute, and most financial audits were limited to a periodic review of vouchers and a reconciliation of bank balances. In a majority of the agencies reviewed, Program and EDP audits are not being performed. Management auditing is being performed in only about half of the agencies contacted.

The Project Team recommends the following types of audits be performed as a basic requirement of any agency audit functions:

- A. A Financial audit that establishes accurate books and records as well as good Fiscal procedures and internal controls over them.
- B. A Compliance audit which covers the proper collection and use of funds in accordance with all applicable legal requirements and restrictions.

C. A management audit which determines:

- 1) whether the audited agency is managing or utilizing its resources, including public funds of the State, personnel, property, equipment and space in an economical and efficient manner; and
- 2) causes of inefficiencies or uneconomical practices including inadequacies in management information systems, internal and administrative procedures, organizational structure, use of resources, allocation of personnel, purchasing policies and equipment.

Should manpower exist to a sufficient degree to allow for increased audit coverage, the Project Team recommends the following additional audit reviews should be performed:

A. A program audit which is a post audit that determines according to established or designated program objectives, responsibilities or duties, including statutes and regulations, program performance criteria or program evaluation standards:

- 1) whether the objectives and intended benefits are being achieved, and whether efficiently and effectively;
- 2) whether the program is being performed or administered as authorized or required by law; and
- 3) whether the program duplicates, overlaps, or conflicts with another State program.

II. STANDARDIZATION OF AUDIT PRACTICES:

The Project Team investigation identified a wide variance in the manner in which agency audits were established, performed, and monitored. Also, the degree of importance attached to audit findings and the manner in which they are reported to agency management varies considerably. The following components of an audit function should be a standard requirement of each agency having an internal audit function; however, each component should be tailored to meet individual agency needs.

- A. Work Schedule (Audit Plan) - Almost all of the agencies surveyed made use of an audit work schedule. These work schedules covered time frames from two months to five years. The Project Team finds this range of time inadequate since the audits to be performed on an ongoing basis must be defined in order to develop budgetary requests for a fiscal year. Also, most of the work schedules reviewed did not cover all of the agency's major functions. Follow-up reviews were not performed with an established frequency. Data showed a few instances in which the work schedule was not being adequately monitored and major changes were not being approved by the agency director.

The Project Team recommends that the agency director require a work schedule be developed by internal audit on a fiscal year basis. The work schedule should cover areas of major concern to the director in addition to audits to be performed on an established frequency basis.

The work schedule should be closely monitored with any major changes reported to the Agency Director for his review and approval.

- B. Audit Programs - Almost all agencies contacted had some form of audit program detailing audit procedures to be performed on a specific audit; however, the quality of these programs varied considerably. Some programs had detailed audit procedures which thoroughly covered an agencies' operations; while, other programs were mere scope statements which partially covered the areas being audited. In many of the agencies reviewed these variances in quality can be attributed to both a lack of formal guidelines and the absence of a thorough program review by management.

The Project Team recommends the use of an audit program which thoroughly covers the area being audited and is detailed enough to adequately achieve the particular audit objective. To meet these requirements, an audit program should be reviewed both before and during an audit to insure that all major internal controls are being adequately covered. After an audit is completed, the audit program should be maintained in a confidential program file for review and up-date.

- C. Audit Workpapers - In all of the agencies surveyed, some form of audit workpapers were used to support the audit work performed. However, most workpapers examined by the Project Team exhibited unacceptable indexing, cross-referencing and note/tickmark explanations. Many of the workpapers examined were not reviewed prior to the preparation of the audit report. Also, though workpapers are usually retained for some time frame, many agencies did not have a standard retention period. Most workpaper deficiencies stem from the fact that a majority of the agencies surveyed have either not established or maintained a formal set of audit workpaper guidelines covering the preparation, review, and retention of audit workpapers.

The Project Team recommends the development and use of formal workpaper guidelines by each agency's audit function. Formal rules covering a suitable indexing, cross-referencing, and a note/tickmark explanation system should be included in the guidelines. In addition, the guidelines should stress the following.

- 1) Only documentation which is necessary to support the audit work performed should be made a part of the audit workpapers.
- 2) All audit findings should be adequately identified and cross-referenced to the related audit report comment.
- 3) All audit workpapers should be reviewed by the audit supervisor for reasonableness relative to the report findings being submitted.
- 4) A standard workpaper retention period should be established and made a part of the formal workpaper guidelines.

- D. Audit Reports - The audit report is used by the auditor as the vehicle to properly inform agency management of problems identified during an audit. However, in many of the audit reports examined by the Project Team, immaterial report findings were included. Findings of a less significant nature should be submitted to management for corrective action at an audit exit conference, and the resolution of these minor findings should be noted in the audit workpapers.

In addition, some reports were not written in a concise manner. The Project Team noted many reports in which the formal response of the auditee was included in the report. This practice forces the auditor to withhold the timely release of an audit report until the formal response is received from the auditee.

The Project Team wishes to note the absence of a formally established time frame within which the auditee must respond to an audit report. The enforcement of time frames for the receipt of responses to an audit report is necessary for the prompt resolution of problems identified in the report.

The Project Team recommends that only significant findings should be formally reported; while, findings of a less significant nature should be discussed with management and resolved during the audit exit conference. A summary of significant findings should be attached to the copy of the audit report. The agency director should be included in the distribution of the audit report with a summary in order that responsible agency management can be alerted to audit findings. A time frame for the receipt of audit responses should be established and closely monitored.

- E. The Follow-up of Audit Report Findings - In most agencies, the Project Team has noted follow-up efforts which are unsatisfactory. Follow-up work is either poorly documented or not documented. Many audit findings are repeated in subsequent audit reports. For those agencies where follow-up efforts are performed, an inordinate amount of time is spent implementing audit recommendations.

In order to accomplish the desired results of an effective follow-up effort and allow the auditor the opportunity to be involved, the Project Team recommends the agency director or his designate follow-up on the resolution of audit report findings in order to insure corrective action is implemented. The internal auditor should be kept informed of this effort. He should maintain adequate records documenting this follow-up process.

III. TRAINING

The Project Team noted that most of the agencies surveyed utilized on-the-job training in lieu of having a formal in-house training program covering the internal audit function. Though all of the auditors interviewed have attended some form of independent continuing education seminar or used self study materials and taken advantage of tuition aid when it has been available, the training that has been obtained does not

always insure that agency auditors are kept informed of new developments affecting their field and their specific agency. Further, the on-the-job training, though adequate and necessary, does not always provide the formal training in standardized audit practices and techniques.

IV. GENERAL COMMENTS:

- A. Internal Control - In a majority of the agencies reviewed the auditors are not performing a detailed analysis of internal control prior to commencing an audit. The accepted method to be used for documenting such controls (i.e. Internal Control Questionnaires, flowcharts, and narratives) are being utilized by only a small number of these agencies.

The Project Team recommends the development and use of an Internal Control Questionnaire (ICQ), a flowchart, or a narrative explaining the existing internal control system.

- B. Audit Sampling Techniques - During an examination of audit workpapers, the Project Team noted that either judgmental or statistical sampling techniques are utilized. However, sample selection procedures and the evaluation of sample results are not always documented in the audit workpapers.

To insure the integrity of the results obtained through the use of a particular sampling technique, the Project Team recommends that sample selection and evaluation techniques be fully documented within the audit workpapers.

- C. Participation in Non-Audit Activities - In a majority of the agencies surveyed, the internal auditors perform some non-audit functions. In order to maintain objectivity, the Project Team recommends that the internal auditors in state government never be assigned non-audit activities.

- D. Interface of Internal and External Auditors - The survey conducted by the Project Team indicated that, in a majority of the agencies, the external auditors generally reviewed the work of the internal auditor as part of their audit procedures; and, in some isolated instances, the external auditors have utilized internal audit manpower to perform the external audit. However, most of the internal auditors interviewed indicated they receive no advice or assistance from the external auditors on accounting or auditing matters. Internal auditors and external auditors should establish a professional relationship with each other in order to meet all statutory responsibilities.

The Project Team recommends an increased involvement on the part of internal auditors in the external audit process.

V. ADMINISTRATIVE SERVICES CONTROL FUNCTION

It is the recommendation of the Project Team that the Management, Fiscal Systems Group to be established in the Department of Administrative Services be staffed by personnel with the skills necessary to perform this function. To insure the constructive and efficient use of this group, it is further recommended that the

Executive Branch of State government take the appropriate action to insure cooperation between this group and all agency boards and commissions reporting to the Governor. Furthermore the Executive Branch of Government should provide the Department of Administrative Services all necessary support on an ongoing basis to make the Management, Fiscal Systems Group a viable and efficient resource for the improvement of the management function in government in the State of Illinois.

- A. This consulting group would provide management, and fiscal systems expertise to all agencies boards, and commissions reporting to the Governor. It would be available to review existing systems, suggest appropriate changes, provide necessary training and continually upgrade management, and fiscal systems in State Government.
- B. Identify problem areas common to all agencies by a review of their present operations as identified in external and internal audit reports. The group would receive all internal and external audit reports, review them and provide constructive consultation in all areas showing non-compliance.
- C. The Management and Fiscal Systems Group should receive annual audit work schedules and a semi-annual update of these schedules showing audits completed and audits cancelled or added from all agencies reporting to the Governor with internal audit staff.
- D. Be the resource group to help agencies in developing formal ongoing training programs for new management, fiscal and audit personnel, in the respective agencies. The training should include state organization, personnel policies, CUSAS, Illinois Statutes and basic Management and Fiscal Systems, audit techniques and requirements for Federal financial participations. Also aid agencies in developing advance training for more experienced management, fiscal and audit personnel to provide a continuing upgrading of the management and fiscal systems in state government.
- E. Provide the resources to assist agencies in evaluating findings of internal and external audits. Provide the technical knowledge that will assist agencies in making constructive responses to the audit findings.
- F. Perform special investigations, reviews or evaluations as requested by the Executive Branch of State Government, with the approval of the Director of Administrative Services.
- G. On an ongoing basis review all internal and external audit reports and provide a summation of audit findings that are repeated. Upon request provide specific recommendations to the appropriate agency director for the elimination of audit findings, especially repeated audit findings.
- H. Prepare a monthly report on activities and findings for the review of the Director of the Department of Administrative Services, agency directors and appropriate personnel in the Executive Branch of Government.

- I. Provide for and submit to the Director of Administrative Services an ongoing internal training program to continually upgrade the skills of the Management, Fiscal Systems Group.
- J. On a continuing basis be aware and respond to all monitoring functions of Management and Fiscal Systems in State Government.
- K. Develop a self-evaluation reporting form for all agency boards and commissions reporting to the Governor that do not have an internal audit staff. This self-evaluation report should be sent to the Management, Fiscal Systems Group, Department of Administrative Services, on a quarterly basis allowing them to provide the necessary evaluation and training needed by these agencies

VI. CONCLUSION

The Project Team does not wish to give the impression that the above recommendations will solve all the problems of Internal Auditing in the State of Illinois. The data developed in this report makes it self-evident that the implementation of these recommendations will provide for the use of audits as a means by which agency management can be assured that it's objectives are being carried out, that internal controls are proper and functioning, and that statutory requirements are being met.

In gathering data for this report, the Project Team has been meticulous in our effort to base recommendations on fact and not opinion. It is also making recommendations that are constructive in nature with the sincere hope that the implementation of these recommendations will take place on a timely basis. The Project Team for Volunteers in Public Management is ready at this point to work with all parties concerned in the implementation of these recommendations for the solution of the problems as defined in our Project Goal.

Joseph C. Ashmead, Project Director
Volunteers In Public Management

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CC: Arthur Quern, Nancy Keeley, Vincent Toolen, Sally Ward