

# IN RETROSPECT

Re-examining taxpayer issues previously researched by Florida TaxWatch to ensure constructive results.

## Improving Internal Auditing Will Help Government Manage Better — Save Taxpayers Over \$70 Million

Managers are meant to manage. Who knows the agency mission, structure and operations better than the agency managers themselves. The problem is that their hands are partially tied because a critical management tool is missing. **State agencies lack the direction, structure and resources to systematically audit their own operations, program performance and financial controls.**

Internal auditors are those day-to-day agency watchdogs who must thoroughly survey, review and analyze agency performance and control systems to proactively safeguard public assets. Effective internal auditing is a resource for the agency head, providing systems and intelligence to avoid having problems become crises. It is also a citizen confidence builder - assuring that government agencies and programs perform properly and productively.

In 1983, Florida TaxWatch issued a detailed analysis of the state's internal audit function and specific recommendations to substantially improve it. Now, three years later, TaxWatch finds that Florida remains lacking in its internal audit and oversight capability. An undue reliance on putting out daily fires prevents top managers from planning comprehensively and executing the necessary management practices to meet the growing demands of a burgeoning state.

The need for a viable internal audit function is greater now than ever. The State Comprehensive Plan - a costly blueprint for Florida's future - makes it imperative that agency managers act to streamline operations and extract old or outmoded programs to free up resources for new priorities and more productive pursuits.

Moreover, the inherent inefficiencies of a transition period between state administrations should be reduced. With adequate systems in place, internal auditors can help ensure that institutional knowledge is passed on and controls are maintained while the ship of state changes hands.

Florida TaxWatch calls on the Florida Legislature to provide the direction and structure to substantially beef up state internal auditing. Stopping crises before they happen, helping managers perform and manage better to save big tax dollars are good reasons why the fastest growing major state should not be without effective internal fiscal and performance oversight.

### Highlights

- Only 87 (.08%) of more than 112,000 state employees perform internal auditing to detect and prevent fraud, waste, abuse and inefficient expenditures from Florida's (1985-86) budget of \$14 billion.
- The Departments of Education and Health and Rehabilitative Services - which spend over half the state budget (\$8.3 billion) - have only 8 agency wide internal auditors. Six other agencies have no internal auditing, with close to \$1 billion at risk.
- Internal auditors surveyed by Florida TaxWatch spend a combined average of 29% of their time on non-audit functions, thereby diluting agency bird-dogging efforts.
- Only 1 in 4 senior level internal auditors report directly to their agency head. The vast majority report to lower level managers, thus reducing or distorting direct channels of accountability.
- Only 2 agencies have internal audit committees to monitor financial/accounting controls, signifying insufficient agency commitment to solving agency problems.
- Florida TaxWatch estimates that substantially beefing up the state's skeletal internal audit system could yield savings of \$70 million or more.

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# Current Internal Auditing Leaves Door Open For Fraud and Abuse; Misses Opportunities to Save Big Tax Dollars

## Internal Auditing in State Government

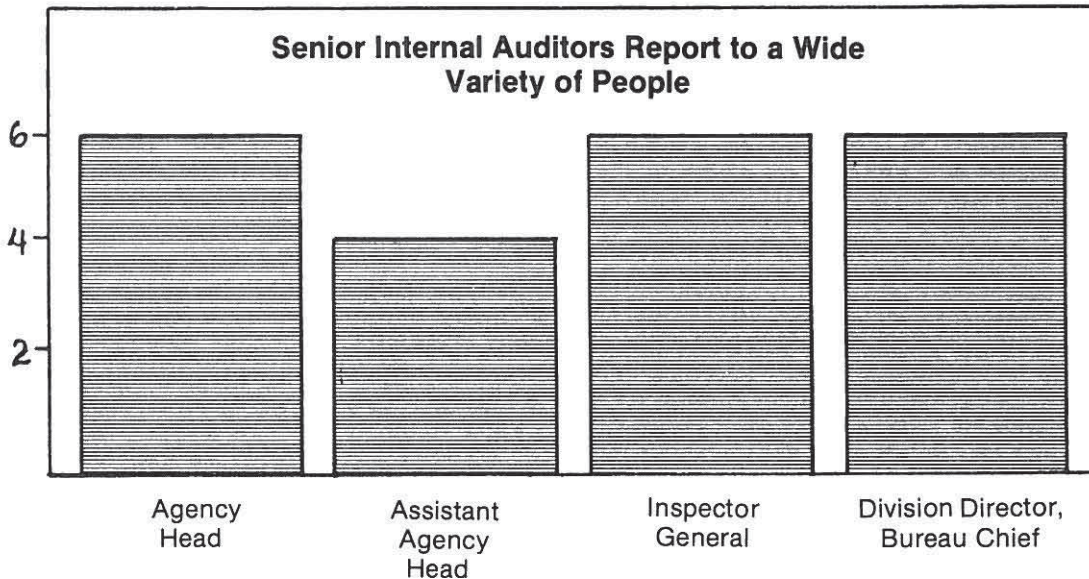
DEPARTMENT	1985-86 BUDGET (\$ in millions)	# POSITIONS	# INTERNAL AUDITORS
Education	\$5,237.0	28,642	1
HRS	\$3,124.0	30,435	7
Transportation	\$1,518.3	9,015	24
Revenue	\$1,076.0	1,359	6
Labor	\$ 621.1	4,012	8
Administration	\$ 506.3	549	4*
Corrections	\$ 347.6	12,133	6
Highway Safety	\$ 149.9	4,583	5
Natural Resources	\$ 134.5	1,845	5
Environmental Regulation	\$ 113.5	1,035	2
Agriculture	\$ 107.1	3,678	no response
Community Affairs	\$ 92.1	324	2
General Services	\$ 80.8	1,101	2
Citrus	\$ 67.4	188	0
Business Regulation	\$ 63.6	707	1
Insurance	\$ 61.4	925	1
Law Enforcement	\$ 53.3	1,039	4
State	\$ 47.4	724	1**
Banking and Finance	\$ 36.2	686	1
Commerce	\$ 32.3	319	1
Game and Fish	\$ 30.0	807	1
Professional Regulation	\$ 24.4	529	1
Governor's Office	\$ 22.1	367	0
Public Service Commission	\$ 14.7	346	0
Legal Affairs	\$ 13.1	335	0
Military Affairs	\$ 6.7	212	3
Judicial Branch	\$ 228.0	6,132	1
	\$13,808.8	112,027	87

\* In Division of Retirement only

\*\*In Division of Cultural Affairs only

Source: Agency responses to Florida TaxWatch survey (April 1986) and Florida's Ten Year Summary of Appropriations Data, Executive Office of the Governor.

# Internal Auditors Lack Access to Agency Heads, Blocking Public Accountability



Source: Florida TaxWatch, Inc., May 1986.

The organizational structure of the internal audit function is a major indicator of its value to an agency. Independence maximizes timely communication of problems to the agency head so that proactive or remedial action can be taken. Conversely, a broken line of direct access to top management clearly has a negative impact on an internal auditor's independence and objectivity.

Responses to Florida TaxWatch's April 1986 survey show that only 6 of 22 (or 27%) of the senior level internal auditors report directly to their agency head. Four report to deputy/assistant agency heads while 12 are assigned to lower level officials - virtually eliminating direct contact with top management.

As reported previously, lack of follow-up action on internal audits by agency heads - due in part to broken lines of internal auditor access to the agency head - results in reduced accountability and crisis or reactive management, such as:

- Failure by the Department of Transportation to act on three successive internal audits of an engineering consulting firm that may have committed grand theft by falsifying financial records and inflating

costs to the state under a cost reimbursement contract;

- Failure by the Department of Highway Safety and Motor Vehicles to act on internal auditors' identification of deficiencies in the vehicle accounting system that led to removal of four top ranking Department officials; and

- Failure by Florida State University to act on a series of internal audit and Auditor General reports of deficit spending over a period of at least three years.

## Agencies Fail to Establish Watchdog Committees to Help Them Manage Better

In addition to reporting directly to the agency head, Florida TaxWatch again recommends that the internal auditor should report to an audit committee within each agency. The committee should be established by the agency head and include representatives outside of management.

Unfortunately, only the Departments of Revenue and Insurance report having active auditing committees.

# Internal Auditing Keeps Problems From Becoming Crises . . .

## Department of Health and Rehabilitative Services

**Program Contracts.** An internal audit of 4,000 contracts worth \$500 million revealed that tighter management controls were needed. Corrective action recommended by the internal auditor will help ensure that HRS receives the desired quantity and quality of vendor services.

**Vendor Payments.** An internal audit of the Developmental Services Program Office's vendor payment system generated an estimated \$190,000 in additional Medicaid Waiver reimbursements.

**Client Information System.** The Department's Client Information System gathers data on 1.4 million clients. An internal audit recommended a reorganized survey instrument to save personnel time and money.

## Department of Community Affairs

**Recoupment of Liabilities.** An internal audit of fine print in long-standing contracts revealed a potential of \$1 million owed the Department by determination and follow-up of contingent liabilities.

**Recoupment of Interest.** More than \$50,000 annually is now returned to the Department for investment by the State as a result of an internal audit that identified loopholes used by subgrantees to retain the funds.

## Game and Freshwater Fish Commission

**Gasoline Purchases.** Internal audit recommendation of a new procedure regarding gasoline purchases saves an estimated \$348,000 annually.

**State Land Rental.** A vendor renting state land paid the Commission incorrectly. An internal audit of the vendor's financial statements detected significant errors, resulting in payment of \$51,000 to the state.



## ★★★ Just a Few Tax Saving Successes

### Department of Insurance

As a result of internal audits:

- Internal controls at the state Fire College have been improved.
- Budget controls over capital outlay funds have been improved; and
- Procedures have been developed to streamline the inventory process.

### Department of Environmental Regulation

**Contract Disputes.** Internal auditors aid program managers in resolving vendor disputes by auditing their claims.

### Department of Natural Resources

**Land Sales.** An audit of the state Racketeer Influenced and Corrupt Organization (RICO) program resulted in an Administrative Rule and a statutory amendment to clarify procedures for disposal of forfeited lands. Administrative costs will be reduced and interest earned on funds generated through sales will increase.

### Department of General Services

**Improving Cash Flow.** In response to internal audit recommendations, the Department has developed cash flow procedures for control of all incoming receipts.

### Department of Business Regulation

**Work Area Layout.** An internal audit recommended a new floor plan for the mail room and new operating policies for the print shop.

**Work Flow Enhancement.** Following an internal audit, license renewal procedures were revised to improve work flow.

### Department of Banking and Finance

**State Warrants.** An ongoing internal audit has strengthened the Department's financial controls by monitoring the ordering, storing, production, distribution and security of state warrants.

**Records Management.** Internal auditors are reviewing the Department's filing systems. Establishing a new records management program should improve operations and save tax dollars.

# . . . Pinpoints Ways to Improve Government Management to Save \$\$\$

## From Good Internal Auditing ★★★

### Department of Revenue

**Courier Service.** An internal audit recommended that field offices transmitting checks for deposit in the state treasury should use a private courier service when they collect more than \$15,000 a day, and the U.S. Postal Service takes longer than two days to deliver the money to Tallahassee. Using a private courier earned the state more than \$207,200 additional interest between August 1985 and March 1986.

### Department of Transportation

**Toll Collections.** Following a grand jury investigation, internal auditors monitored toll booths statewide. Recommended internal controls and security of the \$150 million annual toll collection operation now save about \$1 million annually.

### Department of Labor and Employment Security

**Telephone Charges.** An internal audit discovered a pattern of third-party calls charged to the Department. A follow-up investigation prompted \$8,000 worth of refunds.

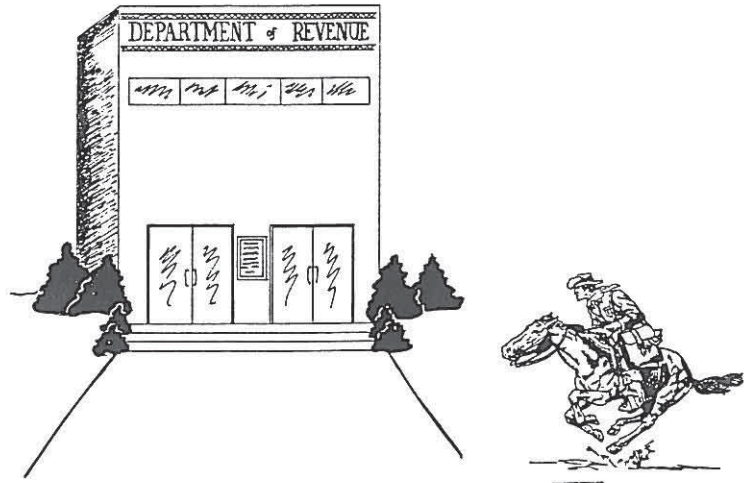
**Payroll Control.** Payroll/Leave Without Pay internal audits have resulted in more control being exercised over this function. Cases of overpayment/underpayment have been detected and corrected.

### Department of Corrections

**Work Time Reporting.** A conviction for grand theft resulted when internal auditors discovered that an Avon Park Correctional Institution employee was paid as an education instructor for the Department and two junior colleges for the same work hours.

**Vendor controls.** An employee at the Broward Correctional Institution misappropriated state funds by depositing duplicate vendor payments in her personal checking account. The internal audit revealing this abuse recommended modified internal control procedures to prevent recurrence.

**Inmate Welfare Fund.** The chief financial officer at Brevard Correctional Institution was replaced after an internal audit uncovered a shortage of \$45,085 in the Inmate Welfare Fund.



### Department of Highway Safety and Motor Vehicles

**Vehicle Title Forms.** Internal auditors reading the fine print in a vendor contract recovered \$12,500 worth of motor vehicle title forms.

**Tag Decals.** Tag decals were the subject of a Department internal audit of a county tax collector's office. The audit proved an employee was diverting decal funds to her personal bank account. She was fired and \$38,822 was returned to the Department.

**Space Utilization.** An audit measuring every available inch in a new annex building in Tallahassee revealed substantial additional usable space, thus eliminating the need to rent space in another building.

### Department of Law Enforcement

As a result of internal audits, the Department implemented the following:

**Training Academy.** Reorganized to achieve greater benefits from dollars expended.

**Seized Vehicle Sales.** Mandated proper care and monitoring of seized articles and vehicles, achieving increased monetary benefits from their use and disposition.

**Personnel Administration.** Streamlined recruitment, selection and promotion policies. Enhanced procedures for conducting of background investigations of prospective employees.

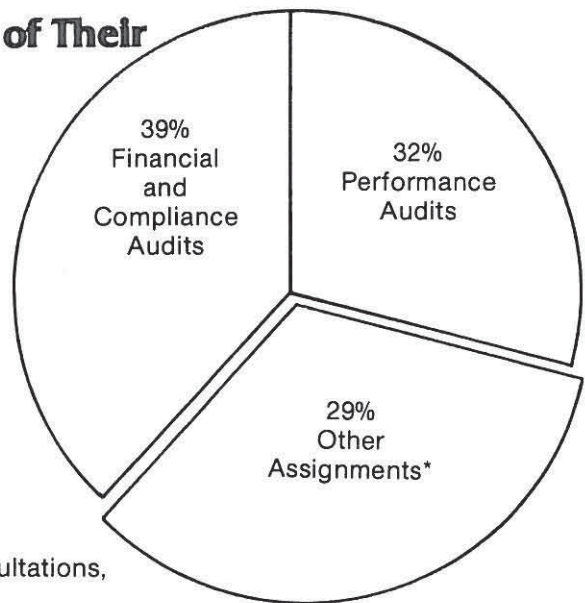
**Expenditure Controls.** Improved monitoring of funds expended by 43 law enforcement training centers/facilities.

# Anomalies Point Up Need For Unified Internal Audit System

These anomalies point to a fragmented, catch-as-catch-can internal audit system. A more systematic, unified approach is needed to boost management and accountability, and to free up resources for new priorities and more productive pursuits.

## Internal Auditors Spend Almost 1/3 of Their Workday on Non-Auditing Tasks

Internal auditors report devoting a combined average of 29% of their time to functions other than conducting internal audits. One auditor works full-time developing an Agency Functional Plan (required by the new State Comprehensive Plan), while another spends all her time on "technical assistance." An Internal Audit Supervisor and three Internal Auditors at the same agency work at least 50% of the time on "other assignments."



\* includes training, investigations, consultations, technical assistance and budgeting.

Source: Florida TaxWatch, Inc., May 1986.

## Internal Auditing Positions: Less Than Meets the Eye

While the Department of Administration classifies 141 state workers as Internal Auditors, Florida TaxWatch's April 1986 survey reveals that only 47 (33%) of these people actually conduct agency internal audits. The majority work in the field, monitoring specific federal and state grant programs with a limited scope. The survey also shows that 40 employees in non-internal auditor positions are assigned to perform internal audits.

## 22 Job Descriptions for the Same Function

The 87 state employees performing internal audits are in 22 separate position classifications. These include 15 different auditor categories plus assorted positions such as Engineer III, Computer Analyst II, Systems Project Analyst and Management Review Specialist/Administrator.

# State Fails to Act to Save Big Bucks

## 1983 TaxWatch Recommendations

- The function of internal auditor should be provided by law to require the identification of management controls necessary to ensure fiscal accountability and compliance with applicable laws and regulations - and the performance of operational audits to continually monitor the effectiveness of these controls.
- The senior level internal auditor should report his tentative findings and recommendations directly to the agency head. This will assure maximum independence of the auditor while providing timely information to top management.
- In addition to reporting directly to an agency head, the internal auditor should report to an audit committee established within each agency. The committee should include representatives outside of management within the agency.
- Public accountability demands a more general distribution of internal audits. This should include the Auditor General and Joint Legislative Auditing Committee, appropriate legislative committees, the Division of Auditing of the Department of Banking and Finance and the Governor's Office of Planning and Budgeting.
- Internal auditors must possess professional qualifications and training and experience in state government auditing. Priority should be given to persons with training and experience prerequisite for a Certified Public Accountant or Certified Internal Auditor.
- The salary level of internal auditors should be commensurate with professional responsibility and authority.

## Current Status

- As in 1983, the Department of Transportation remains the only agency which is statutorily required to perform internal auditing. Legislation expanding this requirement to all agencies died in the 1984 and 1985 General Sessions. Senate Bill 81 and House Bill 532 are currently being considered by the 1986 Legislature.
- Only 6 of 22 (or 27%) of the senior level internal auditors responding to Florida TaxWatch's April 1986 survey report to their agency head.
- Only two agencies, the Departments of Revenue and Insurance, report having active auditing committees.
- The Department of Transportation is the only agency that distributes its audits to these committees and offices.
- Responses to the Florida TaxWatch survey show that auditors' qualifications are in line with their professional duties.
- Florida TaxWatch is satisfied that senior level internal auditors are adequately compensated. However, the 18 (auditor and non-auditor) job classifications of other employees conducting internal audits should be reviewed with an eye toward uniformity and appropriate compensation.

# Now is the Time for the Legislature to Act

To maximize resources, save tax dollars and improve government management, the Florida Legislature should:

- Create an internal audit function for state government by law. Current pending legislation: Senate Bill 81 and House Bill 532;
- Prescribe the qualifications for internal auditors, based on standards of the Institute of Internal Auditors;
- Establish control/reporting relationships within state agencies; and
- Direct that the new internal audit system be implemented as nearly as possible within existing agency resources.

Florida **TaxWatch** further recommends:

- Each state agency should employ a Chief Internal Auditor, appointed by and directly responsible to the agency head.
- Each state agency should have an internal audit committee, established by the agency head and including representatives outside of management within the agency. This committee should meet periodically with management and the Chief Internal Auditor to review matters relating to the annual financial statement, the internal audit program, the system of internal controls and the findings of external auditors.
- The scope of internal auditing within each state agency should be concentrated on

## Effective Internal Auditing System Can Save a Conservative \$70 million.

Florida **TaxWatch** estimates that establishing an effective internal audit function could save 1% of the almost \$1 billion budget of six state agencies without internal auditors. Substantially beefing up internal auditing in all other agencies could yield savings of 1/2% of more than \$13 billion worth of (1985-86) state expenditures, equivalent to combined savings/cost avoidance of approximately \$70 million.

This is a very conservative estimate. In 1978, the Inspector General of the U.S. Department of Health, Education and Welfare stated that the incidence of waste, fraud and abuse in that agency amounted to between 4.7% and 5.4% of the Department's budget. Furthermore, Florida Attorney General Jim Smith estimates that fraudulent and abusive bid-rigging practices at the Department of Transportation inflated contract expenses by 10%, or as much as \$45 million annually between 1973 and 1980.

examination and evaluation of the adequacy and effectiveness of the agency's internal control systems and the quality of performance in carrying out assigned responsibilities. Ancillary functions currently assigned to internal auditors should be reduced.

- The Joint Legislative Auditing Committee may establish an inter-agency advisory committee to ensure appropriateness and compliance with internal auditing laws, standards and regulations.

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