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The Role of the Internal Auditor

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**FROM “PROCESS POLICE” TO GUARDIAN OF PUBLIC TRUST: THE EVOLVING ROLE
OF THE INTERNAL AUDITOR AND THE RELEVANCE TO TEXAS PUBLIC SCHOOLS
BY JUAN J. CRUZ**

A survey of recent news headlines illustrates an abundance of Texas school districts that have been charged with, or suspected of, tampering with grades, attendance and testing; misappropriating public funds; ignoring conflicts of interest in procurement; and generally engaging in other questionable or illegal conduct. Although not an anomaly within the state, the turmoil unraveling in the El Paso Independent School District (“EPISD”) over the last two years is one of the more conspicuous examples of this.

Corporate financial scandals in the last decade have created a concentrated focus on white-collar corruption and heightened scrutiny of corporate governance and risk management. Resultant regulation addressing primarily publicly-held companies¹ imposes affirmative duties on auditors to assess the risk of fraud.² The American Institute of Certified Public Accountants has similarly tightened professional auditing standards and increased auditing responsibility. These measures, among others, require companies listed on the US Exchanges to disclose their governance measures, board structures and board oversight of risk management via internal auditing processes;³ the role of the private sector internal auditor is rapidly changing.

Although directed at the private sector, public entities are not impervious to this wave of regulatory change. State agencies are also required to promote and practice sound internal control and provide accountability for their activities. Moreover, internal auditors within public entities face additional political risks from which their private-sector counterparts are largely exempt. School district internal auditors play a key role in fostering and preserving, or in the alternative undermining, the public trust with respect to finances and operations, as well as testing and instruction. Despite this, the task of our school district internal auditors remains largely misunderstood.

The recent events in the EPISD are a stark reminder that not only can governance in the public sector fail, but also such ethical lapses have both tangible and intangible costs. The Texas Education Agency’s disabling of the EPISD Board of Trustees and the placement of the district under a Board of Managers was a clear attempt towards repairing the damage to the district’s credibility and restoring public trust. While the Trustees have been heavily scrutinized for their failure to adequately supervise former Superintendent Lorenzo García, amidst the turbulence the Board also emerged significantly confused over the proper interface between the district’s Internal Auditor, the Superintendent, and the Board of Trustees. In the months leading up to the exposure of multiple wrongdoings, an internal audit had indeed uncovered discrepancies in several areas of EPISD operations. The Board of Trustees, however, had previously delegated authority of internal audit oversight exclusively to the Superintendent, who then had the sole

¹ *E.g.*, Sarbanes-Oxley Act of 2002 Pub.L. 107-204; 74 F.R. 68334.

² Statement of Auditing Standards (SAS) No. 99 (AU sec 316), Consideration of Fraud in a Financial Statement Audit; SAS No. 1 (AU sec 1), Codification of Auditing Standards and Procedures; PCAOB AS5.

³ U.S. Securities and Exchange Commission’s Proxy Disclosure Enhancements Release Nos. 33-9089; 34-61175; 17 C.F.R §§ 229, 239, 240, 249 and 274 (2005).

decision-making power in responding to the audit.⁴ This is not to suggest that a different tact would have with certainty prevented the crises. However, by circumventing best practices of internal audit accountability and reporting protocol, an ethical collapse was nearly certain to occur.

A. DEFINING THE INTERNAL AUDITOR

Despite budget cuts and reductions in staff, school district leadership must ensure effective controls and high standards of organizational governance, accountability and transparency. In response, internal audit must remain independent and objective in ensuring that audit work focuses on the issues most important to the respective district and follows district protocol.

This rather large charge begs the question: What exactly is the role of the internal audit staff in the overall function of a public school district? Diverging definitions of the “internal auditor” abound and experts in the field agree that one of the internal audit profession’s greatest challenges is clarifying its role, responsibilities, and true value.⁵ In search of answers, in preparing for this paper and presentation, we surveyed our school district internal auditors state-wide, and requested anonymous input identifying the issues of greatest professional concern. While several narrowly-focused issues arose, such as risks in certain cash accounting situations, the vast majority of concerns involved the structure of reporting, communication and cooperation between the various entities in the school district. The remainder of this paper is dedicated to clarifying these issues.

The internal auditor potentially plays a vital role in ensuring continuing organizational effectiveness and accountability but only when the role of audit activity is clearly defined and the proper reporting structure is in place. The Institute of Internal Auditors (“IIA”), an international professional association recognized as the professional leader in certification, education and guide of ethical professional conduct, defines the internal audit function as an independent and objective assurance and consulting activity designed to add value and improve an organization’s effectiveness.⁶ But what defines the scope of their work? What is their hand in either defining or maintaining a school district’s ethical culture and how do we better ensure it is effective? The dearth of case law on point and minimal content in the Texas Education Code betrays the importance of and complexity in answering these questions.

1. Traditional Perceptions

Question: *Why did the internal auditor cross the road?* Answer: *“Because he looked in the file and that’s what they did last year.”* Jokes aside, internal auditors can fall victim to poor branding and the field, as have other professional occupations, has amassed a slew of undesirable

⁴ Zahira Torres & Hayley Kappes, *EPISD Board Shirked Law, Duty to Oversee District Auditor*, 6/22/2012, El Paso Times, available at, http://www.elpasotimes.com/news/ci_20913996/episid-board-shirked-law-duty-oversee-district-auditor.

⁵ SmartPros Ltd., *Internal Auditor Jobs on the Rise* (2007), <http://accounting.smartpros.com/x57694.xml>.

⁶ The Institute of Internal Auditors (“IIA”), available at <https://na.theiia.org/standards-guidance/mandatory-guidance/Pages/Definition-of-Internal-Auditing.aspx>.

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