



## **Department of Accounts**

# **Executive Amendments to the 2006-2008 Biennial Budget**

- **Agency Risk Management and Internal Control Standards (ARMICS)**
- **Financial Reporting Quality Assurance Initiative**
- **Accounting Staff Recruitment and Retention**
- **Other Amendments**

**Senate Finance Subcommittee on General Government**

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**David A. Von Moll  
State Comptroller**



# Why is internal control important?

- **Strong risk management and internal controls is good government – it helps gain and preserve public trust**
  - **Strengthens accountability**
  - **Promotes operational efficiency**
  - **Improves financial reporting**
  - **Strengthens compliance with laws and regulations**
  - **Reduces risk of losses**
- **Proactively address internal control best practices (walk-the-talk on “Best Management State”)**
- **Proactively mitigate risks of adverse audit results**

# Agencies are currently required to develop and maintain a...

- Sound agency internal control framework
- Formal program to assess their agency control framework
- However, prior to ARMICS:
  - No internal control framework or assessment standards
  - No structured accountability – “rubber stamp”
  - No central oversight

# Increasing Expectations

- **Corporate scandals increased the emphasis on internal control and its impact on accurate financial reporting**
  - **COSO/Treadway Commission**
  - **Sarbanes-Oxley – studies report \$4-7 million as the average first year implementation cost by businesses with an average \$5 billion in revenue**
  - **OMB Circular A-123**

# Increasing Expectations

- **Audit environment is increasingly demanding and intolerant – increases risk of adverse audit results**
  - **Statement of Auditing Standards No. 112 – *Communicating Internal Control Matters Identified in an Audit (SAS 112)***
  - **Material weaknesses in financial reporting could result in a qualified audit opinion**
- **Management can no longer rely on the external audit as a control mechanism**
- **APA – Notice has been given**
  - **Review of the Financial Accounting and Control Operations of the State Comptroller, November 2005**
  - **Report on Audit – Agencies of the Secretary of Finance, June 2005**

# SAS 112 - Arizona Example

<b>Finding Category</b>	<b>Pre-SAS 112</b>	<b>Using SAS 112</b>
<b>Material Weaknesses</b>	<b>3</b>	<b>32</b>
<b>Reportable Conditions Significant Deficiencies</b>	<b>11</b>	<b>156</b>
<b>Management Letter Items</b>	<b>65</b>	<b>78</b>
<b>Points of Discussion (i.e. verbal findings)</b>	<b>340</b>	<b>185</b>
<b>Total</b>	<b>419</b>	<b>451</b>

# Agency Risk Management and Internal Control Standards

## ■ Internal Environment

*The control environment reflects top management's expectations for how seriously agency employees should view and execute their fiduciary duties.*

- Tone at the top and throughout the agency
- Integrity and ethical values
- Risk management philosophy and risk tolerance
- Commitment to competence – human resource standards
- Accountability - assignment of responsibility and authority

## ■ Risk Assessment

*Risk assessment is the process of analyzing potential events and considering their likelihood and impact to determine how those events could impact the achievement of objectives.*

- Likelihood and impact

# Agency Risk Management and Internal Control Standards

## ■ Control Activities

*Policies and procedures that ensure risk responses are completed.*

- Review and Oversight
  - Approvals, authorizations, verifications, reconciliations
- Segregation of duties
- Physical and security controls
- Information system controls

## ■ Information and Communication

*Identifying, capturing and communicating relevant information in a form and timeframe that enables people to carry out their responsibilities.*

- Relevant and timely, Internal and external

## ■ Monitoring

*Process of assessing whether controls exist and function.*

- Ongoing or periodic

# ARMICS Implementation Plan

- Issuance Date – November 15, 2006
- Staged implementation deadlines
  - Agency-level Internal Control Assessment
    - September 30, 2007
  - Process and Transaction-level Internal Control Assessment
    - March 31, 2008
  - Corrective Action Plans
    - June 30, 2008

# **ARMICS Initiative Resource Requirements**

- ▶ **For 2007, \$65,000 (GF) - For 2008, \$650,000 (GF) and 7 new FTE**
  - **Implementation and Ongoing Agency Training – DOA and RFP**
  - **Implementation and Ongoing Consulting Services – DOA and RFP**
  - **Compliance Oversight Reviews – DOA**
- **Strong central leadership and implementation assistance services will minimize (but not eliminate) agency resource requirements**

# Why is financial reporting important?

- **Financial reporting is management's full and fair disclosure of financial operating results and financial condition**
  - Promotes financial control and management accountability
  - Basis for evaluating performance and budget accountability
- **Many parties rely on accurate financial reporting for informed decision-making**
  - Agency management
  - Citizens and businesses
  - Governor
  - Legislators
  - Investors and bond ratings agencies
  - Auditors and oversight bodies
  - Federal government

# **Financial Reporting Quality Assurance (Q/A) Initiative**

- **Improve reliability, consistency, accuracy and timeliness of agency reporting processes that feed the Commonwealth's Comprehensive Annual Financial Report (CAFR)**
  - 150 agencies, 52 HE institutions (and 71 foundations), 25 other component units
  - Attachments – 2,000 agency, 280 Higher Ed, 100 other component unit
- **Eliminate CAFR misstatement and audit adjustment risks**

# Financial Reporting Initiative Resource Requirements

- ▶ For 2007, \$64,850 (GF) - For 2008, \$650,000 (GF) and 7 new FTE
- Financial Reporting Directive Training
- Financial Reporting Q/A Program Reviews – Risk based
  - Dedicated and embedded financial reporting experts in agencies to analyze agency data (fluctuation analyses) and reporting processes (Directive Attachments and Templates)
  - Dedicated analysts will target, promote and oversee the implementation of reporting process improvements and/or risk mitigation strategies

# Accounting Staff Compensation – Recruitment and Retention

- ▶ For 2008, \$348,802 (GF)
- Sarbanes/Oxley is a significant factor impacting demand for accounting professionals
- Certification rules requiring a 5-year degree is also impacting supply of accounting professionals
- Accountants starting pay \$45,000-\$50,000
- DOA Compensation – 40 professional accountants

Position	DOA Current Average	DOA Target Average	Private Sector Average	City of Richmond Average
Analyst	\$53,578	\$65,000	\$77,900	\$65,426
Asst. Director	\$65,452	\$75,000	\$85,800	\$83,235
Director	\$92,507	\$95,000	Not Available	\$102,103

# Other Amendments

- ▶ **Establish an alternate cold site location to enhance disaster recovery preparedness**

Provides funding for additional information technology hardware to allow for the restoration of all critical business functions within two days. This cold site location will allow state government to continue running key financial business applications even in the worst case scenario. For 2008, \$100,000 (GF).

- ▶ **Upgrade web applications software**

Provides funding to upgrade the computer software to run WEB applications such as Reportline, Web FAACS, Payline, Redi Virginia and others. In addition to maintaining a stable and supported environment, upgrades will deliver more capabilities, flexibility and improve the ability to support future enhancements. For 2008, \$75,000 (GF).

- ▶ **Provide additional funding and two positions for oversight of the \$250 million procurement card program**

Provides the funding and positions to administer and oversee the procurement card program. DOA has a contract with General Electric to provide procurement card services for the Commonwealth and the contract terms provide for rebates based upon certain levels of volume. DOA's administrative costs are paid through a portion of the rebate revenue. For 2007, \$50,000 (NGF) and two positions. For 2008, \$50,000 (NGF).



**Contact:**

**Department of Accounts**

**David A. Von Moll, State Comptroller**

**Phone 804.225.2109**

**[david.vonmoll@doa.virginia.gov](mailto:david.vonmoll@doa.virginia.gov)**