

# Arlington County's Internal Controls

## May 6, 2014

### Overview

The Revenues & Expenditures Committee (R&E) and the Arlington County Civic Federation (ACCF) have been recommending the establishment of an independent budget review authority for at least three years. On Oct. 1, 2013, ACCF delegates voted to approve a resolution to “establish an independent authority to review the Arlington County budget and selected programs and projects” by an overwhelming margin (40–2–1).<sup>1</sup>

While ACCF has been pressing the county to establish an inspector general (IG) or independent budget review authority (similar to those of Fairfax and Montgomery counties), it has been discovered that Arlington County lacks basic internal controls, having effectively eliminated this function in fiscal year (FY) 2011 when it cut two internal auditor positions.<sup>2</sup>

For the past two years, Arlington County's external auditor, CliftonLarsonAllen (CliftonLarson), has recommended that the county strengthen internal controls and improve operational efficiency by establishing an independent internal audit function. CliftonLarson affirms this recommendation based on county government's size and complexity.<sup>3</sup>

Whereas R&E believes that establishing an IG (an independent budget review authority) is desirable, the county *must* meet its basic fiduciary responsibilities by reestablishing a robust internal control system utilizing internal auditors. To be clear, an IG (or similar body) and the county's internal auditors are two parts of the same whole: an independent internal audit function. Typically an IG would report to the Arlington County Board, and the internal auditors would report to the County Manager. To function properly, both the IG and the internal auditors must be objective and impartial and must be granted full, unfettered access to all relevant information and personnel.

At the end of this report in Appendix A is a complete timeline of audit-related events between 2010 and 2014. Below is a recap of what is currently known about the county's plans to reestablish an internal control system, a brief explanation of the internal audit function's scope of work, a discussion of internal audit staffing levels, and an analysis of the Department of Management & Finance's (DMF's) internal audit proposal with respect to another Virginia county's internal audit function.

### The County's Current Proposal

The County Manager's proposed \$1.15 billion budget for FY2015 makes no mention of the internal audit function except for a reference “to the removal of FY 2014 one-time funding for internal audit (\$250,000).”<sup>4</sup> A few more details were released at the County Board's Feb. 27, 2014, budget work session with county staff. DMF presented a slide titled “Major Initiatives,” and the internal audit function was one of those initiatives as described in the three bullet points below:

- Goal: strengthen County operations and minimize risk and fraud through systematic evaluation of operations and internal controls
- 0.5 FTE currently dedicated; internal reallocation for an additional 1.0 FTE
- Additional one-time contractual funding.<sup>5</sup>

In response to R&E's request for additional written details of its internal auditing initiative, DMF explained that in addition to the existing 0.5 full-time equivalent (FTE) staff position devoted to the internal audit function, another existing 1.0 FTE position in DMF would be shifted to the internal audit function. Yet another 1.0 FTE is devoted to the external audit function but may be utilized on a limited basis for internal audit activities. An undefined portion of the \$250,000 one-time money allocated to the internal audit function in FY2014 will be carried over into the FY2015 budget. DMF also stated that there would be \$40,000 in the general fund budget that will be allocated to the internal audit function.<sup>6</sup>

### **Scope of Work**

In response DMF's presentation at the County Board budget work session on Feb. 27, Chair Jay Fisette stated, "Auditors don't look at every piece of paper." Though his intent wasn't clear, his statement may allude to the general public's common misconceptions about how the internal audit function operates.

For the most part, Arlington County's operations are automated and thus are largely paperless. Arlington utilizes a number of computer systems and software programs to conduct its business rather than a single, fully integrated computer system for all departments. Today, the ability to audit the information technology that processes the data is just as important as auditing the data itself.

Auditors (internal and external) utilize a statistical sampling method to select records or test internal controls at random. If the auditor finds problems with a certain percentage of that random sampling, he or she will dig deeper. If there are few or no problems, then the auditor moves on to examine a different set of records or internal controls.

One aspect of internal auditing is the testing of internal controls or a review of operations and compliance. This function would be analogous to the balancing of our own checkbooks or reviewing our credit card statements for errors. For the county, internal audit employees might test the computer systems to determine whether only those employees who have proper authorization may approve purchase orders. Or they might match purchase orders to vendor payments to confirm the amounts or timeliness of payment.

Another aspect of internal auditing is the independent budget or program review. This function mirrors a review of auto or homeowner's insurance coverage when we seek to determine whether the coverage is adequate and priced correctly (or whether we would be better served by another policy or company). For the county, the internal auditors might perform a cost-benefit analysis for a particular function or program to determine, for example, whether outsourcing might provide more efficient and effective results. Or they might analyze how efficiently or effectively a program or department is utilizing specific resources.

Sometimes these functions are performed by a single group of internal auditors, and sometimes governments split these functions between a group that reports to a county manager or executive and a group that reports to an elected board of supervisors.

**Staffing Levels**

Staffing allocated to an organization’s internal audit function varies based on the size or complexity of the organization’s budget and financial structure: Generally, the larger the budget, the larger the internal audit staff. In Sept. 2013, the Arlington School Board established the position of internal auditor. He will report to an audit committee comprising two elected School Board members, the Superintendent, and the Assistant Superintendent of Administrative Services.<sup>7</sup>

The March 2010 *Review Of Commonwealth Internal Audit Functions* by Virginia’s Auditor of Public Accounts lists state agency and institution budgets along with the number of internal auditors assigned to each.<sup>8</sup> As can be seen in Appendix B, most of the state agencies and institutions with budgets in the same ballpark as Arlington’s \$1.15 billion budget have nine or more internal auditors. Only agencies or institutions with budgets much smaller than Arlington’s have an internal audit staff of only one or two employees.

**How Does Arlington’s Internal Audit Proposal Compare?**

Though geographically larger (245 square miles versus Arlington’s 26.1), Henrico County, Virginia’s, budget of approximately \$1.056 billion (including school funding)<sup>9</sup> makes it a reasonably comparable example for a comparison of internal audit functions. Henrico also is one of only two counties in Virginia (Arlington being the other) that is responsible for maintaining its own roads. Table 1 displays a side-by-side comparison of the audit functions for both counties.

**Table 1**

<b>Function/Criterion</b>	<b>Arlington County</b>	<b>Henrico County</b>
# of Internal Audit Staff	1.5 FTEs	4 FTEs (one director and 3 professional staff members). See <a href="http://www.co.henrico.va.us/audit/about-us/our-staff/">www.co.henrico.va.us/audit/about-us/our-staff/</a>
Budget	\$40,000 in ongoing funds plus leftover one-time money from FY2014	\$411,467 in FY2015 (personnel plus operations). See <a href="http://www.co.henrico.va.us/pdfs/finance/WebProposedFY2015/17.pdf">www.co.henrico.va.us/pdfs/finance/WebProposedFY2015/17.pdf</a>
Direct Reporting	To the county manager	To the Audit Committee (composed of 2 county board members & the county manager)
Audit Committee	Committee on Program Performance was created in 2006; consulting funds related to this committee were cut in FY2010; no other information available online	Audit Committee has its own webpage identifying its members, its responsibilities, and its meeting schedule. See <a href="http://www.co.henrico.va.us/audit/audit-committee/">www.co.henrico.va.us/audit/audit-committee/</a>

Audit Charter	N/A (nothing available online)	Charter is available online. See <a href="http://www.co.henrico.va.us/audit/about-us/audit-charter/">www.co.henrico.va.us/audit/about-us/audit-charter/</a>
Publicly Available Internal Audit Reports	N/A (none listed online)	96 (for years 2003 thru 2014). See <a href="http://www.co.henrico.va.us/audit/find-an-audit-report/">www.co.henrico.va.us/audit/find-an-audit-report/</a>
Defining Internal Audit Responsibilities/Scope of Work	N/A (nothing available online)	Know What Gets Audited—See <a href="http://www.co.henrico.va.us/audit/know-what-gets-audited/">www.co.henrico.va.us/audit/know-what-gets-audited/</a> Goals & Objective—See <a href="http://www.co.henrico.va.us/audit/about-us/">www.co.henrico.va.us/audit/about-us/</a>
Waste, Fraud, Abuse Reporting	N/A (not available online). County Board has requested an “ethics and fraud hotline” for employees to report issues	Online Waste, Fraud, Abuse webpage allows online (anonymous or attributed) reporting by anyone. See <a href="http://www.co.henrico.va.us/audit/fraud-hotline/">www.co.henrico.va.us/audit/fraud-hotline/</a>
Virginia Local Gov. Auditors Assoc. Member?	No	Yes (both county and public school internal audit personnel are members)

Henrico’s Office of Internal Audit was established in 1978 by the Henrico County Board of Supervisors,<sup>10</sup> and it reports to an Audit Committee composed of two elected county board members and the county manager. Despite the office’s small 4-person staff (with no administrative support) and miniscule operations budget (\$10,039 in FY2014),<sup>11</sup> this office has produced more than 90 audit reports within the past 10 years alone, all of which are listed by title on the county’s website and are available to the public upon request.

Of Henrico’s four internal audit staff members, two are Certified Public Accountants (one with a master’s degree); three hold a Certified Information Systems Auditor designation; two are Certified Internal Auditors; and the director is a Certified Fraud Examiner.

Whereas Henrico’s internal audit function may not be perfect, it has a highly qualified, professional staff dedicated to the county’s internal audit function. The office’s charter, history, mission, goals and objectives, and scope of work are publicly available on the county’s website, and the office produces a tangible work product that is publicized online and available for public consumption. Henrico’s Audit Committee has its own webpage to identify its members and to explain its function, and it has been reviewing internal audit reports since 1988.<sup>12</sup>

### Summary

Details for the establishment of an internal audit function in Arlington County are few and far between. Arlington County appears not to have a functioning audit committee or similar body; there are no audit reports, past or present, publicly available. And a search of the county’s website using the search term “audit” reveals nothing with respect to the county’s current internal audit function.

In the Oct. 2013 response to external auditor CliftonLarson’s repeated recommendation to establish an independent internal audit function, the county’s management gave this response: “The County anticipates finalizing a[n internal audit] work plan early in calendar year 2014 using a combination of staff and contractors....”<sup>13</sup> At this time, it is unknown whether an internal audit work plan has been drafted.

In April, the Arlington County Board issued budget guidance #33, directing the County Manager to provide an “interim report by Oct. 31, 2014” on the internal audit function.<sup>14</sup> By that date, CliftonLarson also will be reviewing the county’s FY2014 financial statements and may again comment on the county’s internal audit function, or lack thereof.

If Arlington County wants its citizens to have confidence in county government’s use and management of resources, a good first step would be to establish a transparent, professional internal audit function similar in substance to that of Henrico County.

Respectfully submitted,  
Suzanne Smith Sundburg  
Member of the Revenues & Expenditures Committee

## End Notes

<sup>1</sup>Oct. 1, 2013, ACCF Membership Meeting Minutes, <http://www.civfed.org/wp-content/uploads/2014/02/MinOct2013.pdf>

<sup>2</sup>Arlington County’s FY2011 Adopted Budget, p. 46, <http://arlingtonva.s3.amazonaws.com/wp-content/uploads/sites/18/2013/10/FY-2011-Adopted-ALL-IN-ONE-BUDGET.pdf>

<sup>3</sup>CliftonLarsonAllen’s Oct. 2012 and Oct. 2013 letters to management with responses, both unavailable online

<sup>4</sup>Arlington County’s FY2015 Proposed Budget, web p. 159 [http://arlingtonva.s3.amazonaws.com/wp-content/uploads/sites/18/2014/02/FY15P\\_Sec-C-DMF.pdf](http://arlingtonva.s3.amazonaws.com/wp-content/uploads/sites/18/2014/02/FY15P_Sec-C-DMF.pdf)

<sup>5</sup>FY2015 Proposed Budget Work Session on Feb. 27, 2014, p. 8, <http://arlingtonva.s3.amazonaws.com/wp-content/uploads/sites/18/2014/02/Worksession-PPT-FY15-February-27-.pdf>

<sup>6</sup>April 14, 2014, e-mail from Michelle Cowan, director of DMF, unavailable online [See Appendix A for quotation.]

<sup>7</sup>Arlington Public Schools Sept. 2013 10-4.01 internal audit policy, p. 1, <http://www.apsva.us/cms/lib2/VA01000586/Centricity/Shared/school%20board%20policies/10-sb/10-04-01-Internal-Audit.pdf>

<sup>8</sup>March 2010 *Review Of Commonwealth Internal Audit Functions*, p. 17, <http://www.dgif.virginia.gov/meetings/agendas/packages/2010-internal-audit-report.pdf>

<sup>9</sup>Henrico County Approved Fiscal Plan FY2013–14, pp. 26–27, <http://www.co.henrico.va.us/pdfs/finance/WebApprovedFY2014/ApprovedBudgetFY14.pdf>

<sup>10</sup>Henrico County’s Office of Internal Audit history webpage, <http://www.co.henrico.va.us/audit/about-us/office-history/>

<sup>11</sup>Henrico County’s FY2014 Proposed Budget, Internal Audit section, <http://www.co.henrico.va.us/pdfs/finance/WebProposedAFPFY2014/17.pdf>

<sup>12</sup>Henrico’s online history of its Office of Internal Audit, p. 6, [http://www.co.henrico.va.us/pdfs/about-henrico/20\\_InternalAudit.pdf](http://www.co.henrico.va.us/pdfs/about-henrico/20_InternalAudit.pdf)

<sup>13</sup> CliftonLarsonAllen’s Oct. 2013 letter to management with responses, unavailable online

<sup>14</sup>Arlington County Board April 22, 2014, Recess Meeting, “budget guidance item 33,” discussed beginning at 4:41:14, [http://arlington.granicus.com/MediaPlayer.php?view\\_id=2&clip\\_id=2764&meta\\_id=120249](http://arlington.granicus.com/MediaPlayer.php?view_id=2&clip_id=2764&meta_id=120249)

## **Appendix A: Internal Audit Function 2010–2014 Timeline**

### **2010**

R&E's report on the FY2011 manager's proposed budget cites the elimination of two (2.0) full-time equivalent (FTE) audit positions—one in purchasing and one in internal audit—and recommends retaining these positions.

The FY2011 adopted budget confirms the loss of the two audit positions. Budget commentary notes, "the internal audit reduction is partially offset by the addition of \$37,000 to provide contract audit services on an as-needed basis. ... The duties of the positions will be redistributed to remaining staff [1.0 FTE] and contracted out as necessary. This may increase the time needed to follow through on requested internal audits and update accounting policies, and review capital projects in Purchasing."

Sources:  
1) R&E's April 2010 "Report on the County Manager's Proposed FY11 Budget" to ACCF, <http://www.civfed.com/budgFY11reptcomb.pdf>  
2) Arlington County's FY2011 Adopted Budget <http://arlingtonva.s3.amazonaws.com/wp-content/uploads/sites/18/2013/10/FY-2011-Adopted-ALL-IN-ONE-BUDGET.pdf>

### **2011**

Based on previous internal audit staff cuts and the size of the county's budget, R&E's report on the manager's proposed FY2012 budget recommends that the county create and fund an inspector general or special auditor.

Source:  
1) R&E's April 2011 "Report on the County Manager's Proposed Fiscal Year 2012 (FY12) Budget" to ACCF, <http://www.civfed.org/reandschools2011.pdf>

### **2012**

R&E's report on the manager's proposed FY2013 budget repeats its recommendation for the county to create and fund an inspector general or special auditor.

In its October 2012 letter to management, the county's external auditor—CliftonLarsonAllen—issues its recommendation for the county to establish an independent internal audit function. Management responds saying, "Since [the FY2011 audit position cuts], the County has utilized existing staff resources, part time audit staff as well as some contractor funding to provide internal audit support. The County recognizes the importance of an independent internal audit function and anticipates presenting a proposal to revitalize this function as part of the FY 2014 budget."

Sources:  
1) R&E's April 2012 "Report on the County Manager's Proposed FY13 Budget" to ACCF, <http://www.civfed.org/reandschools2012.pdf>  
2) CliftonLarsonAllen Oct. 2012 letter to management, unavailable online

### **2013**

The manager's proposed FY2014 budget (and the adopted budget) identifies \$250,000 in one-time funds to establish an internal audit function but identifies no ongoing funding in the base budget and no additional staff positions for this purpose.

R&E issues a report in April 2013 explaining the importance of a robust internal audit function and profiling the internal audit programs of Fairfax and Montgomery counties. Both counties commit significant ongoing financial resources and professional full-time personnel to support their internal audit functions, resulting in a measureable and significant savings that more than cover the expenditures to fund their internal audit programs.

In September 2013, the Arlington Public School Board establishes an Internal Auditor (IA) to provide "operational, financial, and compliance audit services to the School Board and the Superintendent under the direction of the [Audit] Committee."

In its October 2013 letter to management, the county's external auditor—CliftonLarsonAllen—repeats its recommendation for the county to establish an independent internal audit function: "At present, the County does not have an independent internal audit function. We believe that an organization of the County's size and complexity warrants consideration of an internal audit function." Management responds saying, "As part of the FY

2014 budget, the County Board provided \$250,000 of funding to increase the County's internal audit function within the Department of Management and Finance. The County anticipates finalizing a work plan early in calendar year 2014 using a combination of staff and contractors and has conducted various audit and internal control reviews over the last few months with these resources."

R&E issues a follow-up report in Oct. 2013 concluding that "OIGs and similar independent internal audit bodies that are created to evaluate program efficiency and effectiveness can provide meaningful oversight to inform the budget process, identify savings and efficiencies to ensure the best allocation of limited resources, and give citizens confidence that their government is utilizing tax dollars wisely." In response, ACCF delegates pass this resolution: "Therefore be it resolved: That the County fund a study by independent advisors for the purpose of establishing an independent County budget review authority that will provide Arlington County residents and taxpayers with reasonable assurance that their taxes and fees are being effectively and efficiently spent."

Sources:

- 1) Arlington County's FY2014 Proposed Budget, <http://arlingtonva.s3.amazonaws.com/wp-content/uploads/sites/18/2013/10/FY-2014-PROPOSED-ALL-IN-ONE.pdf>
- 2) R&E April 2013 report to the ACCF, "AUDITING: THE "CORNERSTONE OF GOOD PUBLIC SECTOR GOVERNANCE," [http://www.arlnow.com/wp-content/uploads/2013/04/IG\\_AuditingSectionFINAL4\\_4\\_13.pdf](http://www.arlnow.com/wp-content/uploads/2013/04/IG_AuditingSectionFINAL4_4_13.pdf)
- 3) Arlington Public Schools Sept. 2013 10-4.01 internal audit policy, <http://www.apsva.us/cms/lib2/VA01000586/Centricity/Shared/school%20board%20policies/10-sb/10-04-01-Internal-Audit.pdf>
- 4) CliftonLarsonAllen Oct. 2013 letter to management, unavailable online
- 5) R&E Oct. 2013 report to the ACCF, "HEEDING THE AUDITOR'S ADVICE: 'Establish an Independent Internal Audit Function,'" unavailable online
- 6) ACCF's Oct. 2013 approved resolution, "Proposed Resolution: Establish an Independent Authority to Review the Arlington County Budget and Selected Programs and Projects," [http://www.civfed.org/wp-content/uploads/2013/10/IG-resolution\\_10.1.13.pdf](http://www.civfed.org/wp-content/uploads/2013/10/IG-resolution_10.1.13.pdf)

## **2014**

The County Manager's proposed FY2015 budget is silent on the internal audit function with this exception: "Non-personnel expenses decrease due to the removal of FY 2014 one-time funding for internal audit (\$250,000)."

A Dept. of Management & Finance (DMF) presentation at the Feb. 27, 2014, County Board budget work session lists the internal audit function as a "major initiative" with the following bullet points: "—Goal: strengthen County operations and minimize risk and fraud through systematic evaluation of operations and internal controls, —0.5 FTE currently dedicated; internal reallocation for an additional 1.0 FTE, and —Additional one-time contractual funding."

In response to R&E's request for written details on DMF's plans to establish an internal audit function, R&E receives this reply: "We have allocated one position internally within DMF for the internal audit function, bringing it to 1.5 FTE. We do have one position on staff now (in addition to the 1.5) that spends some time on internal audit functions, but when the external audit season happens, he tends to get pulled off on other critical tasks. Additionally, we have \$40k in ongoing funding for audit services as well as the one-time money (\$250k) that we received in FY 2014 and expect to carryover a portion of."

At it April 22, 2014, recess meeting, the County Board approved the following "budget guidance" item for the County Manager: "33. Internal Audit—The County Board fully supports the County Manager's plans to enhance the County's internal audit program and the expansion of the County's ethics program, including the addition of an ethics and fraud hotline. The enhanced audit function should follow best practices in auditing. The Board directs the County Manager to provide an interim report by October 31, 2014, and an assessment of whether the audit function should be independent and to whom it should report by January 2015."

Sources:

- 1) Arlington County's FY2015 Proposed Budget, [http://arlingtonva.s3.amazonaws.com/wp-content/uploads/sites/18/2014/02/FY15P\\_Sec-C-DMF.pdf](http://arlingtonva.s3.amazonaws.com/wp-content/uploads/sites/18/2014/02/FY15P_Sec-C-DMF.pdf)
- 2) FY2015 Proposed Budget Work Session on Feb. 27, 2014, <http://arlingtonva.s3.amazonaws.com/wp-content/uploads/sites/18/2014/02/Worksession-PPT-FY15-February-27-.pdf>
- 3) April 14, 2014, e-mail from Michelle Cowan, director of DMF, not available online
- 4) Arlington County Board April 22, 2014, Recess Meeting, "budget guidance item 33," discussed beginning at 4:41:14 [http://arlington.granicus.com/MediaPlayer.php?view\\_id=2&clip\\_id=2764&meta\\_id=120249](http://arlington.granicus.com/MediaPlayer.php?view_id=2&clip_id=2764&meta_id=120249)

*The Internal Audit Function in 2009*

There are 37 internal audit functions among the Commonwealth's agencies and institutions of higher education with an average staff size of five auditors. Of the 37 internal audit functions, 15 have staff levels of at least five; and 22 internal audit functions have four or less staff persons. Furthermore, of the 22 smaller internal audit functions, a single internal auditor comprises the function for ten entities. The following table summarizes the 37 internal audit functions by staff size, 2009 operating expenses, and total position level.

2009 Final Budgets, Total Positions, and Staff Size for Internal Audit Functions

<u>Entity</u>	<u>2009 Actual Expenses</u>	<u>Positions</u>	<u>Staff Size</u>
Transportation	\$3,304,701,000	8,850	24
UVA incl. Medical Center & College at Wise	1,842,749,000	12,922	17
VCU & VCU Health Systems	2,234,131,000	12,182	13
Virginia Tech & Co-op Extension	948,308,000	7,262	12
Corrections	1,049,492,000	12,939	9
Virginia Community College System	1,034,956,000	8,908	9
George Mason	604,863,000	3,465	7
Medical Assistance Services	6,118,574,000	353	6
VITA	319,492,000	399	6
Health	534,795,000	3,675	5
ABC	452,713,000	1,048	5
James Madison	369,381,000	2,835	5
Old Dominion	298,339,000	2,283	5
William & Mary, Richard Bland, & VIMS	288,531,000	1,883	5
Virginia Retirement System	49,495,000	300	5
Norfolk State	127,691,000	982	4
Virginia Employment Commission	1,216,655,000	865	3
Behavioral Health & Developmental Services	927,606,000	9,272	3
State Police	264,826,000	2,805	3
State Lottery	252,976,000	309	3
Juvenile Justice	213,113,000	2,405	3
Motor Vehicles	204,508,000	2,038	3
Taxation	165,008,000	997	3
Radford	149,830,000	1,390	3
Virginia State & Co-op Extension	127,773,000	856	3
Longwood	92,649,000	641	3
Treasury	15,182,000	121	2
General Services	204,965,000	663	1
Rehabilitative Services	140,286,000	1,050	1
Christopher Newport	109,425,000	787	1
Conservation and Recreation	94,127,000	539	1
Mary Washington	88,685,000	683	1
State Corporation Commission	76,332,000	653	1
Agriculture and Consumer Services	52,970,000	526	1
Game and Inland Fisheries	48,643,000	496	1
Mines, Minerals, and Energy	26,282,000	234	1
Health Professions	25,301,000	214	1
<b>Total</b>	<b>\$24,075,353,000</b>	<b>71,632</b>	<b>189</b>

Source: Commonwealth Accounting and Reporting System, Appropriation Act Chapter 781