OFFICE OF THE ATTORNEY GENERAL

AND

DEPARTMENT OF LAW

REPORT ON AUDIT

FOR THE YEAR ENDED

JUNE 30, 2005

APA

Auditor of Public Accounts

COMMONWEALTH OF VIRGINIA

AUDIT SUMMARY

Our audit of the Office of the Attorney General and the Department of Law for the year ended June 30, 2005 found:

- proper recording and reporting of all transactions, in all material respects, in the Commonwealth Accounting and Reporting system;

- internal control matters that we consider to be reportable conditions; however, we do not consider any of these findings to be material weaknesses; and

- no instances of noncompliance required to be reported under Government Auditing Standards.

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OVERVIEW

The Attorney General is the chief executive officer of the Commonwealth of Virginia's Department of Law. Effective January 31, 2005, the Attorney General resigned and the General Assembly elected a new Attorney General. The Attorney General and staff represent the interest of the Commonwealth in all civil cases naming the Commonwealth or any of its agencies or officials as a party, and in criminal cases on appeal to the Court of Appeals of Virginia and the Supreme Court of Virginia. In cases involving federal law, the Attorney General represents the Commonwealth's interests in federal court. The Department of Law also enforces consumer protection laws and investigates Medicaid fraud.

The Attorney General is also the legal advisor to the Governor and more than 200 state agencies, boards, commissions, and institutions. The Attorney General renders official opinions on the application of the law upon written request of the Governor, members of the General Assembly, members of the judiciary, state officials, and local constitutional officers.

The Office of the Attorney General (Office) has five legal divisions with offices in Abingdon, Fairfax, Norfolk, Richmond, and Roanoke. A Deputy Attorney General heads each division and reports directly to the Chief Deputy Attorney General, an appointee of the Attorney General. The five legal divisions are:

Civil Litigation and Commerce Division - This division includes the following sections: Insurance and Utilities Regulatory, Trial, Employment Law, Antitrust and Consumer Litigation, and Real Estate and Construction.

Public Safety and Enforcement Division - This division includes the Special Prosecutions Section, which includes the Environmental Unit, Health Professions, Organized Crime, and Medicaid Fraud Control Unit. This Division also includes the Correctional Section, and the Criminal Litigation Section, which contains Capital Litigation.

Health, Education, and Social Services Division - This division includes the following sections: Education, Mental Health/Health Services, Child Support Enforcement, Medicaid, Social Services, and Domestic Violence Initiatives.

Technology and Transportation Division - This division includes the following sections: Transportation, Computer Crimes, and Technology Civil.

Sexual Predators, Tobacco, and Gaming Division - This division handles all cases related to sexual predators, tobacco, and gaming.

In addition to the above legal divisions, there is also a Solicitor General Office, the Administration Division, and the Division of Debt Collection. The Division of Debt Collection is a separate agency within the Office, which collects delinquent accounts for state entities. The financial information below presents separate information on the Office and the Division of Debt Collection.

Attorney General's Office

The Office receives most of its funding from General Fund appropriations, but also collects some special revenue and federal funds. The special revenue funds include collections from agencies and universities for legal services provided by the Office, while the federal funds are primarily grants supporting Medicaid fraud control activities and programs to fight domestic violence and violent teen gangs. The following schedule summarizes the Office's budgeted and actual funding for fiscal year 2005.

2005 Budgeted and Actual Funding

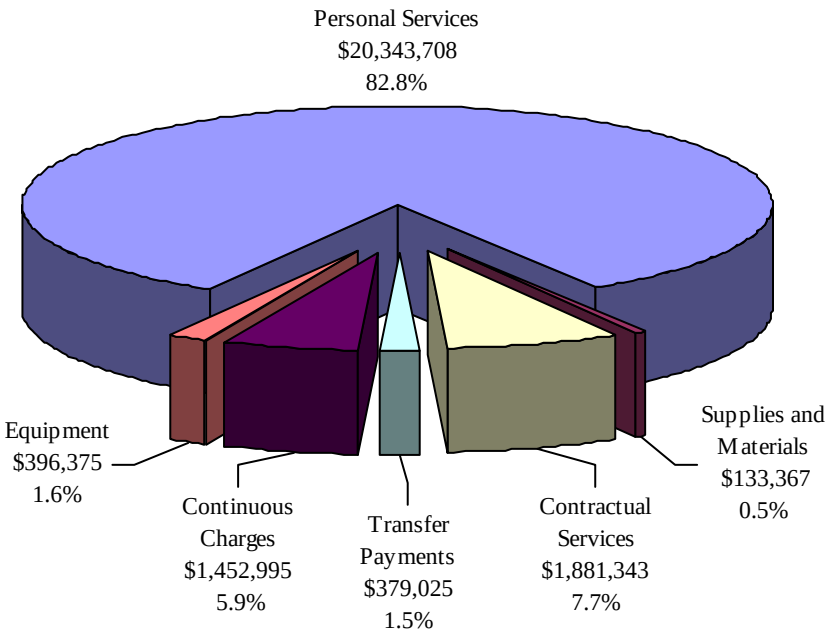
	Original Budget	Final Budget	Actual Funding
General Fund appropriations	$16,828,026	$17,645,608	$17,645,608
Special revenue fund	5,197,011	5,561,220	2,732,453
Federal trust	1,817,524	3,248,852	2,192,874
Total	$23,842,561	$26,455,680	$22,570,935

The difference between the budgeted and actual special revenue funds is due to the Office not collecting as much revenue from agencies for legal services as estimated. The increase in the federal budget is due to additional federal grants available for gang reduction and domestic violence, although federal collections were not as much as anticipated in fiscal year 2005.

The Office also collects and deposits directly into the General Fund of the Commonwealth proceeds from fines, forfeitures, court awards, and settlements. These funds totaled approximately $28,000 in 2005 and are not included in the above table because they are not available to the Office to fund its operations.

The majority of the Office's expenses are payroll costs for its 254 full-time and six part-time employees, which make up over 82 percent of total expenses. The chart below shows fiscal year 2005 expenses broken down by type.

2005 Expenses by Type



Division of Debt Collection

The Division of Debt Collection (Division) is a separate agency within the Office, which collects delinquent accounts for state agencies, state-supported institutions of higher education, and their hospitals. The Division receives delinquent accounts from state agencies and takes appropriate action, including litigation to collect them.

The Division's operations have undergone changes recently as a result of legislation passed by the 2004 General Assembly. This legislation required that agencies forward past due accounts over $3,000 and 60 days old to the Division. This legislation also mandated the following allocation of collections: 30 percent to the state agency or institution, 30 percent to the Division to fund operations, and 40 percent to the General Fund of the Commonwealth. Over the last several years, the Division has received budget and staffing level increases in an effort to increase collections and keep up with the growing caseload. The following table shows selected operating statistics for the last five years for the Division.

Operating Statistics 2001-2005

	2001	2002	2003	2004	2005
Employment level approved by the General Assembly	15	15	17	21	23
Division budget approved by the General Assembly	$952,780	$953,457	$1,126,706	$1,361,076	$1,516,385
Number of accounts	5,571	6,207	6,322	8,312	11,140
Dollar value of accounts	$81 million	$87 million	$91 million	$100 million	$159 million
Gross collections	$11 million	$11 million	$13 million	$13 million	$10 million
Amount returned to the General Fund	$ -	$ -	$ -	$1.5 million	$1.4 million

Source: Commonwealth Accounting and Reporting System and the Division of Debt Collection

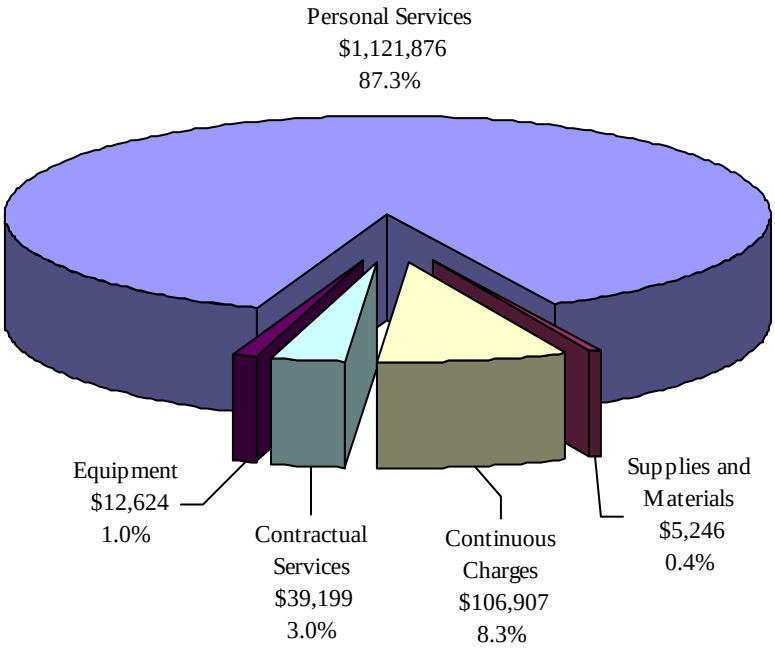
In fiscal year 2005, the Division implemented a new collection management system, CollectMax, to manage legal and accounting activities for their accounts. The system is critical to the agency's operations and stores sensitive information such as debtor's social security numbers, bank account information, employment and earnings data, and in some cases, medical information. The Division paid $11,945 for the software license; $7,000 to convert data from the old to the new system; and $4,996 for additional licenses, training, and maintenance.

The Division funds operations with a portion of fees retained from their collections. The major operating expense for the Division is personal services, which make up over 87 percent of total expenses. The following table and chart show 2005 funding and expense information.

2005 Budgeted and Actual Funding

	Original Budget	Final Budget	Actual Revenues
Special Fund	$1,516,385	$1,516,385	$1,705,269

2005 Expenses by Type*



* Transfer payments of $80 are not included

INTERNAL CONTROL FINDINGS AND RECOMMENDATIONS

Attorney General's Office

Strengthen Controls over Voucher Preparation

The Office needs to continue to strengthen its oversight of vendor payment processing. Specifically, the Office needs to ensure that it maintains adequate documentation to support vendor payments. We found several instances where the Office did not maintain adequate documentation to determine the types of services delivered or payment terms; however, we did not find any improper payments. In addition, the Office needs to improve procedures over coding of vendor payments. We found several payments where the Office was using incorrect or outdated codes.

Miscoding payments or making payments without documentation creates problems in monitoring budgets and controlling costs. In addition, making payment from federal grants without documentation or other supporting materials can result in questioned costs leading to the repayment of funds to the federal government. We recommend that management review and strengthen the current payment processing procedures. As part of this review, management should determine that procedures are adequate to ensure compliance with the Commonwealth Accounting Policies and Procedures Manual. We further recommend that supervisors meet with staff to review the procedures over payment processing and stress the importance of following them.

Division of Debt Collection

Our review of internal controls and procedures in the Division of Debt Collections revealed several areas needing financial management improvement. These issues, when taken as a whole, indicate a lack of financial management and information system expertise within the Division. We recommend that management review current staffing and skill levels to determine whether the Division has the appropriate number of financial management and information system staff and types of skills necessary to perform their responsibilities. Options for management would include hiring additional staff, contracting for financial management and information system staff, or working with Office management to utilize staff and skills already in place at the Office.

Review Build-up of Excessive Balance in Operating Fund

Funding for the Division's operations comes from retaining a percentage of its collections. The Appropriation Act allows the Division to retain 30 percent of collections, not to exceed $1.8 million in any fiscal year. Over the last several years, the Division has retained fees in excess of their operating expenses, resulting in an accumulated cash balance in their operating fund that totals $2.6 million. This amount equates to two year's worth of operating expenses based on 2004 and 2005 actual expenses. The following table details the Division's operating revenues and expenses for the last five fiscal years.

	2001	2002	2003	2004	2005
Beginning balance	$ 786,059	$ 604,984	$ 876,937	$ 1,352,947	$ 2,278,366
Collection fee revenue	835,723	1,322,606	1,579,304	1,964,690	1,705,269
Expenses	(1,016,798)	(1,050,653)	(1,056,470)	(1,024,534)	(1,285,932)
Transfers	-	-	(46,824)	(14,737)	(8,510)
Ending balance	$ 604,984	$ 876,937	$ 1,352,947	$ 2,278,366	$ 2,689,193

We recommend the Division, along with the management of the Office, review this activity to determine the most appropriate disposition of these funds and propose this disposition to the General Assembly. In addition, we recommend the Attorney General and the General Assembly revisit the collection allocation methodology set forth in the Code of Virginia and the Appropriation Act to ensure that a 30 percent allocation to the Division to fund operations is appropriate.

Document Alternative Allocations

The standard allocation of collections on accounts is 30 percent to the state agency or institution, 40 percent to the General Fund, and 30 percent retained by the Division to cover operating costs. The Appropriation Act does allow for the Secretary of Finance to make exemptions to this allocation when the Secretary determines an allocation to the original fund source is more appropriate. The Division uses different allocations for several agencies, but could not provide documentation showing the Secretary's approval of the exemptions. The Appropriation Act requires the Secretary to report the approved exemptions to the Division of Debt Collection within 30 days of the approval. We recommend that the Division work with the Secretary's Office to ensure that the Division receives exemptions timely and provides the documentation necessary to support the allocation.

Transfer Collections to Agencies Timely

The Division did not transfer the agency share of collections back to agencies in a timely manner. We found several payments where it took from one to three and a half months for the Division to transfer the agency's share of collections to the agency. In addition, as of September 2005, the Division has not transferred the agency's share of June 2005 collections to agencies. It is our understanding that these delays occur for a variety of factors such as time needed to implement changes from the new legislation, turnover, and staffing issues.

Provide Account Information for Agencies

The Division does not provide periodic account summaries to creditor agencies to reconcile against their own records. This increases the risk that both CollectMax and the creditor agencies' records have inaccurate or incomplete account information.

Monitor Information on Overall Workload

A best practice for an organization managing and collecting accounts receivable is to monitor the number, dollar values, and ages of outstanding accounts. Division management does not monitor this information or use it to manage operations. When we inquired about the number and dollar value of accounts held by the Division as of June 30, management did not have this information readily available. At our request, management ran a Collect Max report with the information. When we reviewed this information, we found the number of accounts and dollar value of accounts as of June 30 had increased significantly from the prior year. Management could not provide an explanation for this increase. New legislation in 2004 more than likely accounted for the increase; however, it is possible that 2005 information is not accurate given inadequate data conversion controls when transferring accounts to the new collection management system in 2005.

Improve CollectMax Implementation and Security Issues

We found several weaknesses we believe are indicative of a lack of information system expertise involvement in the implementation and operation of the CollectMax system. Division management has a System Administrator that does not have an information systems background and whose job responsibilities

lack clear definition of duties. In addition, it is our understanding that the Chief Information Officer for the Office has provided only limited assistance to the Division in the implementation of CollectMax and its ongoing operations. We found the following specific weaknesses in the conversion and implementation of CollectMax:

- Contrary to industry best practices, the Division performed minimal systematic testing to ensure the data converted accurately and completely from the former system to CollectMax. Instead, the Division relied primarily on vendor assurances that the conversion effort was successful. Having thorough systematic testing of the conversion process is essential given the risks of data duplication, alteration, or loss during conversion. This conversion risk is of special concern since the number of accounts and their dollar value increased significantly since our previous audit and Division management cannot explain the increase.

- Additionally, management cannot explain the levels of and justification for user access. The individual who originally granted user access no longer works at the Division and it appears that this individual did not maintain documentation of their actions. When asked, Division management could not produce a summary of user access showing employee names, titles, and the specific privileges within each level of access. There is also no evidence of periodic, division-wide reviews of user access.

Commonwealth of Virginia

Walter J. Kucharski, Auditor

Auditor of Public Accounts
P.O. Box 1295
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September 16, 2005

The Honorable Mark R. Warner
Governor of Virginia
State Capitol
Richmond, Virginia

The Honorable Lacey E. Putney
Chairman, Joint Legislative Audit
and Review Commission
General Assembly Building
Richmond, Virginia

INDEPENDENT AUDITOR'S REPORT

We have audited the financial records and operations of the **Office of the Attorney General and the Department of Law** for the year ended June 30, 2005. We conducted our audit in accordance with Government Auditing Standards, issued by the Comptroller General of the United States.

Audit Objectives, Scope, and Methodology

Our audit's primary objectives were to evaluate the accuracy of recording financial transactions on the Commonwealth Accounting and Reporting System, review the adequacy of the Office's internal control, test compliance with applicable laws and regulations, and review corrective actions of audit findings from the prior year's report.

Our audit procedures included inquiries of appropriate personnel, inspection of documents and records, and observation of the Office's operations. We also tested transactions and performed such other auditing procedures, as we considered necessary to achieve our objectives. We reviewed the overall internal accounting controls, including controls for administering compliance with applicable laws and regulations. Our review encompassed controls over the following significant cycles, classes of transactions, and account balances:

Revenues
Expenditures and contract management
Appropriations

We gained an understanding of the overall internal controls, both automated and manual, sufficient to plan the audit. We considered materiality and control risk in determining the nature and extent of our audit procedures. We performed audit tests to determine whether the Office's controls were adequate, had been placed in operation, and were being followed. Our audit also included tests of compliance with provisions of applicable laws and regulations.

The Office's management has responsibility for establishing and maintaining internal control and complying with applicable laws and regulations. Internal control is a process designed to provide reasonable,

but not absolute, assurance regarding the reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations.

Our audit was more limited than would be necessary to provide assurance on internal control or to provide an opinion on overall compliance with laws and regulations. Because of inherent limitations in internal control, errors, irregularities, or noncompliance may nevertheless occur and not be detected. Also, projecting the evaluation of internal control to future periods is subject to the risk that the controls may become inadequate because of changes in conditions or that the effectiveness of the design and operation of controls may deteriorate.

Audit Conclusions

We found that the Office properly stated, in all material respects, the financial amounts recorded and reported in the Commonwealth Accounting and Reporting System. The Office records its financial transactions on the cash basis of accounting, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America. The financial information presented in this report came directly from the Commonwealth Accounting and Reporting System.

We noted certain matters involving internal control and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of internal control that, in our judgment, could adversely affect the Office's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial records. Reportable conditions entitled "Review Build-up of Excessive Balance in Operating Fund;" "Document Alternative Allocations;" Transfer of Collections to Agencies Timely;" "Provide Account Information for Agencies;" "Monitor Information on Overall Workload;" and "Improve CollectMax Implementation and Security Issues" are described in the subsection entitled "Internal Control and Compliance Findings and Recommendations." We believe that none of the reportable conditions is a material weakness.

The results of our tests of compliance with applicable laws and regulations disclosed no instances of noncompliance that are required to be reported under Government Auditing Standards.

The Office has not taken corrective adequate corrective action with respect to the previously reporting finding entitled "Strengthen Controls over Contracts." This finding, entitled "Strengthen Controls Over Voucher Preparation" is included in the section entitled "Internal Control Findings and Recommendations." The Office has taken adequate corrective action with respect to audit findings reported in the prior year that are not repeated in this report.

This report is intended for the information and use of the Governor and General Assembly, management, and the citizens of the Commonwealth of Virginia and is a public record.

We discussed this report with management on September 27, 2005.

AUDITOR OF PUBLIC ACCOUNTS

LCR/kva

COMMONWEALTH of VIRGINIA

Office of the Attorney General

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Attorney General

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MEMORANDUM

TO: Linda Ramthun
Audit Director

Karen Killian
Auditor in Charge

FROM: Anne P. Petera
Director of Administration

DATE: September 27, 2005

SUBJECT: Response to Management Letter Comment

Thank you for providing us with an advanced copy of your management letter comment and the opportunity to provide some perspective on the findings and recommendations it contains. I will address each of the items in the same order as presented in your letter.

The Office continues to work toward improving the documentation necessary to support vendor payments. We are pleased to note that no improper payments were found by the audit. While the use of incorrect or outdated codes may happen from time to time due to human error, we believe that expanding the Finance Department staff will allow us to redistribute workloads and dramatically reduce these kinds of errors. We have received approval to hire an additional employee in the Finance Department. In addition, we have redistributed the "Expenditure Structure" published by the Department of Planning & Budget in July, 2005 to all appropriate staff and have implemented a review procedure into the payables process.

Since last year's audit, three of the five members of the Finance & Accounting Department staff have left our employ. Both the new Director of Finance and new Procurement Officer have made proper documentation a priority, working to educate staff about requirements and to ensure proper compliance with the Commonwealth Accounting Policies and Procedures Manual and the Commonwealth's procurement laws and policies. Additionally, we will conduct training in the coming months to review procedures for payment processing with our employees.

The findings and recommendations regarding the Division of Debt Collections (DDC) have been discussed with DDC management in detail. Current staffing and skill levels have been

reviewed and a determination made that additional staff is needed to conduct financial management review and to provide certain financial services for the DDC.

As to the specific recommendations made, we offer the following response. We are in compliance with the Appropriations Act in terms of collecting our fees and not exceeding the annual limit of funds retained to cover operations. The unused portion of our collected fees has accumulated over the past three years. However, the Appropriations Act does not contain any directive language regarding such surpluses. DDC will determine an appropriate disposition of these funds and work with OAG management to develop a recommendation to the General Assembly on such disposition. We will share the APA's recommendation regarding the collection allocation methodology with the new Attorney General during transition.

DDC management will work with the Secretary of Finance to ensure that DDC is timely notified of the Secretary's decisions regarding allocations and exemptions. We will ask that the Secretary of Finance provide adequate documentation of these actions as well.

The addition of one staff member in DDC charged with financial services responsibilities will improve the timeliness of collections transfers to the client agencies. This new employee will also be charged with the task of providing account information to client agencies for reconcilement against their own receivables records, and for the development of financial management reports which will quantify and age the receivables by client agency and for the DDC overall.

The Office CIO will meet with the Collect Max software representatives to review the conversion from our old system and have the vendor describe in detail how the conversion was accomplished, including testing that was done. The CIO will then determine how much additional system wide testing is needed to ensure that the conversion was successful and complete. Should testing not produce acceptable verification of the success of the conversion, then additional alternatives will be developed and implemented. Further, the Collect Max System Administrator will establish levels of user access needed by all DDC employees and develop a procedure for assigning access levels and periodic review of same.

This Office is appreciative of the Auditor of Public Accounts bringing these matters to our attention, and we fully intend to take the actions necessary to improve each area mentioned.

OFFICE OF THE ATTORNEY GENERAL

As of June 30, 2005

Judith W. Jagdmann
Attorney General

Bernard L. McNamee
Chief Deputy Attorney General

Anne Petera
Director of Administration

Thomas A. Gelozin
Director of Finance and Budget