

Arizona Department of Forestry and Fire Management

Procedural Review

As of November 21, 2016
Report 16-308



A Report to the Arizona Legislature

Debra K. Davenport
Auditor General





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AUDITOR GENERAL

MELANIE M. CHESNEY
DEPUTY AUDITOR GENERAL

December 16, 2016

Jeff Whitney, Director
Arizona Department of Forestry and Fire Management

We have performed a procedural review of the Arizona Department of Forestry and Fire Management's internal controls in effect as of November 21, 2016. Our review consisted primarily of inquiries, observations, and selected tests of internal control policies and procedures, accounting records, and related documents. The review was more limited than would be necessary to give an opinion on internal controls. Accordingly, we do not express an opinion on the effectiveness of internal controls or ensure that all deficiencies in internal controls are disclosed.

Specifically, we reviewed cash receipts, cash disbursements, bidding, travel, journal entries, transfers, payroll, capital assets, information technology logical access, and compliance with certain Arizona Revised Statutes.

As a result of our review, we noted certain deficiencies in internal controls that the Department's management should correct to ensure that it fulfills its responsibility to establish and maintain adequate internal controls. Our findings and recommendations concerning these deficiencies are described in the accompanying summary.

This report is intended solely for the information and use of the Department and is not intended to be and should not be used by anyone other than the specified party. However, this report is a matter of public record, and its distribution is not limited.

Should you have any questions concerning our procedural review, please let us know.

Sincerely,

Jay Zsorey, CPA
Financial Audit Director





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The Department should improve its internal control system

Criteria—The Department should maintain an effective internal control system over financial reporting. A system of internal control is expected to provide reasonable assurance that objectives relating to financial reporting will be achieved.

Condition and context—Auditors reviewed the Department's internal control system and noted the following deficiencies:

- The Department did not prepare an annual budget.
- The Department did not monitor its financial activity.
- The Department did not perform a risk assessment over financial reporting.
- The Department did not always follow the *State of Arizona Accounting Manual* (SAAM). For instance, the Department did not have written procedures over cash receipts and incorrectly classified \$9.8 million of federal and state revenues as miscellaneous revenues in the State's financial system. See findings 3 and 4 for additional examples.

Effect—The Department's internal control system may not be designed sufficiently to provide for an efficient and well-controlled financial environment. In addition, the Department did not always report accurate financial information in the State's accounting system.

Cause—Prior to the review period, the Department transitioned from a division of the Land Department to a stand-alone state agency. After the transition, the Department did not have sufficient staff trained in accounting to develop and maintain an effective internal control system over financial reporting.

Recommendation—To help ensure that the Department has an effective internal control system over financial reporting, it should develop and implement the following procedures:

- Preparing an annual budget in sufficient detail to provide a meaningful tool to monitor key performance indicators.
- Monitoring financial activity, such as comparing budgeted amounts to actual expenditures and reviewing financial activity for unusual fluctuations in account balances.
- Performing risk assessments over financial reporting.
- Developing written procedures over cash receipts and properly classifying federal and state reimbursements in the State's accounting system.



The Department should establish policies and procedures to ensure compliance with Arizona conflict-of-interest laws

Criteria—Arizona Revised Statutes (A.R.S.) §38-503 regarding conflicts of interest states that any public officer or employee of a state agency who has, or whose relative has, a substantial interest in any contract, sale, purchase, or service to that particular public agency shall make known that interest in that state agency's official records and shall refrain from voting upon or otherwise participating in any manner as an officer or employee in such contract, sale, or purchase. In addition, state agencies must complete and submit to the State's General Accounting Office (GAO) Form 51 each year if the agency has any related-party transactions that aggregate to \$100,000 or more for financial statement reporting purposes.

Condition and context—The Department did not have controls to ensure that employees in management positions disclosed potential conflicts of interest and, as a result, the Department could not determine if there were any conflicts of interest or related-party transactions.

Effect—There is a risk that a conflict of interest may exist and expenditures may have occurred that resulted in employee personal gain or were otherwise inappropriate. Further, the Department may fail to report related-party transactions to the GAO.

Cause—The Department was not aware that employees in management positions must disclose potential conflicts of interest.

Recommendation—The Department should develop and implement internal controls to require that all employees in management positions disclose potential conflicts of interest to help ensure compliance with A.R.S. §38-503. When a conflict of interest exists, those employees with a conflict must refrain from voting upon or otherwise participating in any manner as an officer or employee in such contract, sale, or purchase. In addition, the Department should monitor and maintain documentation of any related-party transactions related to a conflict of interest. Further, if the Department has related-party transactions that aggregate to \$100,000 or more, they should be reported to GAO for disclosure in the State's financial statements.



The Department should improve internal controls over payroll processing

Criteria—In accordance with the *State of Arizona Accounting Manual* (SAAM) Topic 55 (Payroll and Personnel), the Department should have effective internal controls over payroll processing to help ensure employees are accurately paid and to accurately record and report payroll expenditures.

Condition and context—The Department did not have adequate internal controls over payroll processing. Specifically, one employee was responsible for entering, processing, and reviewing payroll expenditures in the State's payroll system. In addition, the Department did not reconcile payroll expenditures between the State's payroll and financial systems.

Effect—Without effective internal controls over payroll processing, the Department could pay its employees wrong amounts and incorrectly report payroll expenditures in the State's accounting system. In addition, there is increased risk of fraudulent payroll activity.

Cause—The Department was not aware that its payroll controls were inadequate.

Recommendation—To help ensure employees are accurately paid and that payroll expenditures are accurately recorded and reported, the Department should:

- Require an employee not responsible for processing payroll to review the payroll to ensure that it is accurate and has been properly recorded in the State's payroll and financial systems.
- If practicable, rotate payroll duties among employees periodically.
- Perform a reconciliation of the Department's payroll expenditures between the State's payroll and financial systems.



The Department should improve internal controls over its capital assets

Criteria—To comply with the *State of Arizona Accounting Manual* (SAAM) Topic 25 (Long-lived Resources), §05 and §40, the Department should have effective internal controls over its capital assets that are sufficient to control, safeguard, and accurately report capital assets.

Condition and context—The Department had 17 capital assets listed on the State's Fixed Asset Module (FAM). However, it did not have effective internal controls over its capital assets sufficient to control, safeguard, and accurately report them. Specifically, auditors tested 9 capital assets and noted the following:

- Three assets had been transferred to another state agency but were listed as the Department's assets on the FAM.
- Two assets were listed with the wrong description on the FAM.
- Two assets did not meet the State's capitalization threshold but were listed as capital assets on the FAM.

Auditors also tested two of the Department's capital purchases that were above the State's capitalization threshold and noted they had not been recorded as capital assets on the FAM.

Lastly, the Department had not designated a property control officer, and it had no record of when it last performed a physical inventory of its capital assets or reconciled its internal capital assets listings to the FAM.

Effect—Without effective internal controls, the Department's capital assets are exposed to theft or misuse. Further, the Department is not communicating accurate information to the State's General Accounting Office for financial reporting purposes.

Cause—The Department did not have a process to comply with the State's capital assets policies and procedures.

Recommendation—The Department should comply with the State's capital assets policies and procedures to help ensure its capital assets are properly controlled, safeguarded, and reported in the State's financial statements. Specifically, the Department should:

- Maintain an accurate and complete listing of its capital assets on the FAM that includes, at a minimum, the property identification number, description and location of the asset, acquisition method, funding source, acquisition date, disposal date, purchase document number, and cost, as applicable. In addition, the Department should record capital assets within ten business days of their acquisition.
- Designate a property control officer that is responsible for ensuring the Department complies with the requirements outlined in SAAM.
- Conduct a physical inventory of its capital assets, update its internal capital assets listing and FAM for any changes, and perform a reconciliation between its internal listing and the FAM at least annually.

DEPARTMENT RESPONSE



Douglas A. Ducey
Governor

Office of the State Forester

Arizona Department of Forestry and Fire Management



Jeffery C. Whitney
State Forester

December 9, 2016

Debra K. Davenport, Auditor General
State of Arizona Office of the Auditor General
2910 N. 44th Street, Suite 410
Phoenix, AZ 85018

Re: Response to the November 2016 Procedural Review, Report No. 16-308

Dear Ms. Davenport:

The Department of Forestry and Fire Management (“Department”) appreciates the opportunity to respond to the findings of the procedural review performed by your audit team. Please accept my gratitude to you for the dedication, commitment, time and research your staff contributed to the Department’s audit and appreciation for all the recommendations and discussions between our staff and yours.

Below, please find the department’s responses to the audit findings.

Finding 1: The Department should improve its internal control system.

Response: The Department concurs with the finding that we should improve our internal control system. The Department has been without a Financial Administrator since April 2015, and the person in that position most recently didn’t have an accounting specific degree. The first step in improving our internal controls is hiring an accountant to be our Financial Administrator. A viable candidate has been found through the recent interview process and barring any issues should be on-board in early January. The immediate task for this individual will be to review your recommendations and take measures to remedy any issues discussed.

Finding 2: The Department should establish policies and procedures to ensure compliance with Arizona conflict-of-interest laws.

Response: The Department concurs with the finding that we should establish policies and procedures to ensure compliance with Arizona conflict-of-interest laws. This past summer the Department began to do this by having all managers, and non-managers with financial responsibilities, complete GAO CI-101 “Annual Declaration and Disclosure” document. This will continue to be done on an annual basis as well as part of the onboarding process for new employees.

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Finding 3: The Department should improve internal controls over payroll processing.

Response: The Department concurs with the finding that we should establish stronger internal controls with regards to payroll processing. We currently have one permanent employee for this position and who has, until recently, entered almost all payroll manually from submitted paper timesheets. The Department has recently converted all permanent staff to Electronic Time Entry (ETE) which should greatly minimize manual entries within payroll processing. This payroll person also is not an ETE proxy and has no authority with ETE other than to enter her own time. We are also implementing a review process to ensure at a minimum, a second person is reviewing and reconciling payroll to ensure its accuracy.

Finding 4: The Department should improve internal controls over its capital assets.

Response: The Department concurs with the finding that we should improve internal controls over our capital assets. The Department is currently in the process of conducting a physical inventory of our capital assets and reconciling with FAM within AFIS. This process will be done on an annual basis with specific process and procedures to be set forth by our designated Property Control Officer.

The Department agrees with all the findings and recognizes the inherent importance of maintaining a proper system of internal controls with regards to all financial processes within the Department. As mentioned above, a major step towards correcting the findings above is the hiring of an accountant for the Financial Administrator position, which should be completed in January, 2017.

Thank you again for the effort and time put into helping us to better serve the state of Arizona and its taxpayers

Very truly yours,

Jeffery C. Whitney
State Forester

