Key Points of Report

Comptroller of Public Accounts
1994 Statewide Financial and Compliance Audit
April 1995

Overall Conclusion

The Comptroller's Office collected and accurately reported $17 billion in net tax revenues and transfers of $10.6 billion during fiscal year 1994. As the State's financial reporting officer, the Comptroller is responsible for compiling and publishing the State's Comprehensive Annual Financial Report (CAFR). The Comptroller's Office can make improvements to the State's financial reporting process. In addition, the Comptroller's Office had continuing difficulties reconciling cash between the Uniform Statewide Accounting System and the Treasury's cash accounting system during fiscal year 1994.

Key Findings

- The Comptroller's Office should improve the effectiveness of the Financial Reporting Section's quality control function to ensure that errors in draft versions of the CAFR are detected and corrected prior to review by the State Auditor's Office. The Comptroller has established an independent quality assurance function that will be responsible for providing more timely detection and correction of such financial reporting errors.
- The Uniform Statewide Accounting System (USAS) is not currently used to generate the CAFR. Currently, the State compiles its financial position once a year by an extensive, mostly manual, consolidation of the relevant financial data. The Comptroller's Office is developing a detailed action plan to meet this USAS objective which is required by the Government Code.
- The Comptroller's Office and the State Treasury need to improve the system used to reconcile cash between the Uniform Statewide Accounting System and the Treasury's cash accounting system. The Comptroller and the Treasury had continuing difficulties with the reconciliation process during fiscal year 1994. The Comptroller's Office has coordinated its efforts more closely with the State Treasury in developing an effective reconciliation process.

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Overall Conclusion

As the State's financial reporting officer, the Comptroller is responsible for compiling and publishing the State's Comprehensive Annual Financial Report. Internal Control Issue 1 and both Accounting and Reporting Issues identify improvements that can be made to the State's financial reporting process.

Internal Control Issues

Internal Control Issue 1:

Improve Effectiveness Of Quality Control Function

The Comptroller's Office needs to improve its quality control function to provide timely detection and correction of financial reporting errors before the comprehensive annual financial report (CAFR) is completed. As a result of weaknesses in the quality control function, errors occurred in the unaudited comprehensive annual financial report which required correction before the CAFR was released.

As the State's financial reporting officer, the Comptroller's Office is responsible for the accuracy and completeness of the State's annual financial reports. The Comptroller's Financial Reporting Section compiles the State's annual financial report by an extensive consolidation of approximately 300 agency financial reports. The State Auditor's Office has worked closely with the Financial Reporting Section to compile the State's annual financial reports since the first report was produced for the 1987 fiscal year. The State Auditor's Office has aided in this process through extensive review of draft reports to ensure the accuracy of the final report.

Recommendation: We recommend that the Comptroller improve the effectiveness of the quality control function to ensure that errors are detected and corrected prior to review by the State Auditor's Office.

Management's Response: We have benefited from the Auditor's involvement in the production of the annual financial reports, but recognize the need to more clearly establish a division of functions between the agencies. We also agree to improve our quality control function to reduce normal reporting errors in drafts of the financial reports prior to their being presented to the Auditor for review. We have already established an independent quality assurance function that will be responsible for providing more timely detection and correction of financial reporting errors.

Internal Control Issue 2:

Improve Cash Reconciliation Process

The Comptroller's Office and the State Treasury need to improve the cash reconciliation process between the Uniform Statewide Accounting System (USAS) and the Treasury's cash accounting system. With the implementation of USAS in 1994, the old reconciliation method proved ineffective since the new system requires a higher level of sophistication in the reconciliation process. This improved process had not been perfected when USAS became the State's primary accounting system. As a result, the Comptroller and Treasury had continuing difficulties with the reconciliation process during fiscal year 1994.

An effective reconciliation system provides monitoring and control to ensure the accuracy of the State's cash records, including individual agency accounting records. The lack of an effective reconciliation process increases the risk that errors and irregularities will not be detected in a timely manner by management.

Recommendation: We recommend the Comptroller continue coordination efforts with the State Treasury to complete improvement of the cash reconciliation system by May 1995. These actions can be accomplished by:

- clearing all outstanding reconciling items within one monthly accounting cycle

- continuing to identify conditions that create reconciling items and installing processes to eliminate reconciling items caused by those conditions

Management's Response: We agree that a more effective cash reconciliation process was needed in 1994. The implementation of USAS in 1994 impacted our cash reconciliation process in ways that we had not anticipated. USAS captures data at a higher level of detail, increasing the need for greater automation to ensure timely reconciliation. We have coordinated our efforts more closely with the State Treasury in developing an effective reconciliation process that is accomplishing the criteria outlined above by the State Auditors. Although we had difficulties with the reconciliation process because of the newness of the system, we were able to confirm that all accounts were properly and accurately superintended. The improvements in the reconciliation process will ensure the continued integrity of the financial accounts in a timely manner.

Accounting and Reporting Issues

Accounting and Reporting Issue 1:

Effectively Use The Statewide Accounting System

The Uniform Statewide Accounting System (USAS) is not used to generate the comprehensive annual financial report (CAFR). Currently, the State compiles its financial position once a year by an extensive, mostly manual, consolidation of the relevant financial data. This data is obtained from approximately 300 state agencies and universities and from analysis of information on USAS.

The Legislature has appropriated approximately $100 million since 1988 for the development and implementation of the statewide accounting system (USAS). These funds were made available to improve the amount, timeliness, and quality of financial information, including strengthening management capabilities.

Government Code, §403.013 (d) states that the Comptroller shall prepare a CAFR "from information requested from the Comptroller under Subchapter B, Chapter 2101, until it can be prepared from information contained in a fully operational uniform automated statewide accounting and reporting system." Although the Comptroller's Office has not met this USAS objective, they have organized a work group to address how to improve processes for the collection of financial data. The work group plans to develop the procedures necessary to capture all financial data needed to produce the CAFR.

Recommendation: We recommend that the Comptroller develop and implement a detailed action plan to convert from the mostly manual process of compiling financial information to an automated process using information maintained on USAS. The plan should identify specific tasks, resources, and time frames.

Management's Response: We agree that a more detailed action plan should be developed for producing the CAFR from USAS. We are currently developing such a plan. We consciously did not choose to produce *the CAFR during the first year of implementation due to outstanding issues that needed to be identified and resolved, so as not to jeopardize the State's fiscal integrity.*

Accounting and Reporting Issue 2:

Ensure Accuracy Of The Financial Reporting Entity

The Financial Reporting Section (FRS) did not establish adequate procedures to provide reasonable assurance that the State's financial reporting entity was properly defined and reported.

FRS did not provide sufficient guidance to state agencies and universities. Consequently, the information gathered by FRS from state agencies and universities was not sufficient to determine if all possible organizations and relationships were considered and if conclusions were reasonable.

An accurate assessment of the State's financial condition is not possible unless the financial reporting entity is properly defined and reported.

Governmental Accounting Standards Board (GASB) Statement No. 14, *The Financial* Reporting *Entity*, establishes standards for defining and reporting on the financial reporting entity. It also establishes standards for reporting participation in joint ventures. FRS has three years to implement GASB 14 from the date of its release. Late consideration of GASB 14 contributed to the problems identified in applying the statement.

Recommendation: We recommend that the FRS develop procedures to review and evaluate the reporting entity and changes in the reporting entity on an ongoing basis to ensure that the State's financial reporting entity is properly defined and reported. We recommend that the supporting documentation of all organizations considered be centrally accumulated and reviewed for reasonableness by the FRS. We also recommend that the FRS annually review changes in generally accepted accounting principles and adjust their instructions as appropriate. In addition, if certain standards require more lead time for agencies to implement, FRS should consider interim notification to agencies to provide sufficient lead time for implementation of new standards.

Management's Response: We agree to implement the recommendations outlined above by the State Auditors. Because of the importance and difficulty in implementing this accounting statement, we will work closely with the State Auditors to ensure all instructions and processes, for identifying these reporting entities, are adequate for that purpose.

Audit Scope

The primary focus of audit work at the Comptroller was the statewide consolidation process and the Comptroller's financial accounts material to the State's comprehensive annual financial report (CAFR). In fiscal year 1994, the Comptroller collected $17 billion in net tax revenues and transferred $10.6 billion from the General Revenue Fund to other funds. At the end of the fiscal year, the State had cash balances of $8.2 billion, and the Comptroller held $500 million for others in its trust and agency funds.

Consolidation work was conducted to determine if the CAFR was accurate and presented in accordance with generally accepted accounting principles. We gained an understanding of the internal control structure for the consolidation process. We also tested the accuracy of the compilation of the annual financial reports for over 280 state agencies, universities, and component units.

For material accounts, we gained an understanding of the internal control structure for the Comptroller's annual financial report, including the general control environment and controls over cash receipts, cash balances, and journal vouchers. Certain financial accounts were also tested, including General Fund tax revenues and operating transfers out, trust and agency fund payables, and cash balances for all funds.