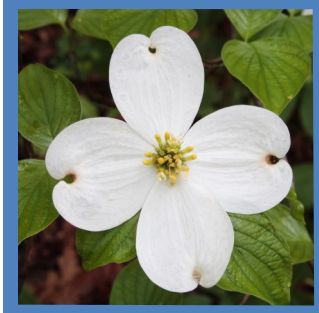


AGENCIES OF THE SECRETARY OF FINANCE

REPORT ON AUDIT
FOR THE YEAR ENDED
JUNE 30, 2020

Auditor of Public Accounts
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AUDIT SUMMARY

This report summarizes our fiscal year 2020 audit results for the following four agencies under the Secretary of Finance (Secretary):

- *Department of Accounts*
- *Department of Planning and Budget*
- *Department of Taxation*
- *Department of the Treasury and the Treasury Board*

Our audits of these agencies for the year ended June 30, 2020, found:

- proper recording and reporting of transactions, in all material respects, in the Commonwealth's accounting and financial reporting system, each agency's financial systems, and in supplemental information and attachments submitted to the Department of Accounts;
- seven prior year findings involving internal control and its operations discussed in the Status of Prior Year Findings and Recommendations section, where corrective action is ongoing;
- five new findings involving internal control and its operations discussed in the Internal Control and Compliance Findings and Recommendations section, necessary to bring to management's attention;
- ten of the twelve findings are considered to be instances of non-compliance with applicable laws and regulations that are required to be reported; and
- adequate corrective action with respect to audit findings reported in the prior year that are not referenced in this report.

This report also includes information on significant initiatives for the Secretary and Department of Accounts, including the status of the Commonwealth's Human Capital Management System development project and upcoming financial reporting changes for leases. In addition, it includes a Risk Alert, which is applicable to the Department of Taxation.

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SIGNIFICANT INITIATIVES

The following section provides an update on two major Commonwealth initiatives affecting Secretary of Finance agencies.

Status of System Development Project

Applicable to: *Secretary of Finance and Department of Accounts*

Commonwealth's Human Capital Management Systems Project

In August 2016, Department of Accounts (Accounts) launched a payroll project to replace the Commonwealth's existing payroll system that has been in place since 1986. Accounts expanded this project in May 2018 to also replace the Commonwealth's human resources; time, attendance, and leave; and benefits administration systems for an all-encompassing Human Capital Management (HCM) project. Accounts will deploy the project, using staggered implementation dates of March and October 2021. It will be essential for Accounts to meet the target implementation dates as the vendor for the Commonwealth's current payroll system will cease providing software support at the end of 2021.

The Human Capital Management project has staggered implementation dates of March and October 2021, with estimated total costs of approximately $131.9 million dollars.

Since April 2020, Accounts has been working through the testing phase of the HCM project. Accounts continues to partner with the Department of Human Resource Management (Human Resource Management) to ensure the new system's specifications are accurate and capture the Commonwealth's standards. The testing phase is set to be complete in February of 2021, and thereafter Accounts has scheduled two release groups of agencies for March 2021 and October 2021 for system implementation. Both groups should have full functionality of all modules within the system by their release date.

Accounts estimates a total cost of $131.9 million for the HCM project. As of November 30, 2020, Accounts spent approximately $92 million and estimates an additional cost of $39.9 million to complete the project. The Governor authorized a working capital advance for the total estimated cost of the project. Accounts spent approximately $74.1 million of the working capital advance to plan, develop, configure, and roll-out new software as of June 30, 2020.

The HCM project scope is set to integrate with the Commonwealth's accounting and financial reporting system, reduce risks by replacing several aging statewide systems, improve performance with all Commonwealth system applications using cloud infrastructure, and meet the majority of the Commonwealth's payroll and human resource requirements. Further, by integrating with the accounting and financial reporting system, the Commonwealth will have a variety of new reporting capabilities and more streamlined processes.

As with all projects, Accounts continues to face risks while implementing the HCM project. For example, although Accounts is familiar with the software product they are implementing, their primary experience with that product has been with the accounting and financial reporting system modules and

not the payroll and human resources modules. Accounts must also adhere to a strict timeline to meet the desired project implementation date, and the COVID-19 pandemic could impact Accounts ability to do so based on scheduling/staffing difficulties and agency training limitations. Furthermore, Accounts faces complexity with data conversion based on the numerous different processes and uses of statewide systems by agencies across the Commonwealth. Accounts, Human Resource Management, and all agencies that use the Commonwealth's payroll and human resource systems will need to continue to devote key personnel, time, and technology resources to mitigate the risks associated with the Human Capital Management project.

New Lease Accounting Standard

Applicable to: *Department of Accounts*

Governmental Accounting Standards Board Statement No. 87 Leases

In 2017, the Governmental Accounting Standards Board (GASB) issued Statement No. 87, Leases. Originally, GASB's effective date for this accounting standard was fiscal year 2021; however, due to the COVID-19 pandemic, GASB issued Statement No. 95, Postponement of the Effective Dates of Certain Authoritative Guidance. This standard delayed implementation of Statement No. 87, Leases, to fiscal year 2022. This new accounting standard will significantly change the way governments account for leases. Under the new model, operating and capital leases no longer exist. Governments will report all leases as financing transactions, which results in recording an intangible asset and a liability for every lease except short term leases (less than 12 months). This will dramatically change the Commonwealth's financial statements by increasing the amount of assets and liabilities.

GASB delayed implementation of Statement No. 87, Leases, to fiscal year 2022. When the new standard becomes effective, most of the Commonwealth's $485.7 million in operating leases will become new lease liabilities in the financial statements.

For fiscal year 2020, the Commonwealth's primary government had $28.4 million in capital lease liabilities and $485.7 million in operating lease commitments, which are not reported as liabilities in the Commonwealth's Comprehensive Annual Financial Report (CAFR). Under the new standard, most of this $485.7 million in operating lease commitments will become new lease liabilities. This could potentially impact the Commonwealth's debt capacity model, resulting in a reduced capacity for debt issuance.

The Commonwealth has two systems that state agencies use to account for leases. The Department of General Services (General Services) manages a system that includes all real estate leases. Accounts manages a system that includes all other leases, such as equipment leases. GASB Statement No. 87 requires that governments recognize and measure existing leases using the facts and circumstances that exist at the beginning of the period of implementation, which is July 1, 2021, not the inception of the lease. With the postponement of the effective date, Accounts and General Services have an additional year to gather data, assess all of their leases, and implement changes to their lease systems no later than July 1, 2021, to successfully implement the new standard for fiscal year 2022.

RISK ALERT

During the course of our audit, we encountered an internal control and compliance issue that is beyond the corrective action of agency management alone and requires the action and cooperation of management and Virginia Information Technologies Agency (VITA). The following issue represented such a risk to the agency and the Commonwealth during fiscal year 2020.

Mitigate Server Vulnerabilities

Repeat: Yes (first issued in fiscal year 2015)
Applicable to: *Department of Taxation*

VITA's contractual partnership with various information technology (IT) service providers to create the Commonwealth's Information Technology Infrastructure Services Program (ITISP) provides agencies with installation, maintenance, operation, and support of IT infrastructure components, such as servers, routers, firewalls, and virtual private networks. The Department of Taxation (Taxation) relies on contractors procured by VITA for the installation of security patches in systems that support Taxation's operations. Additionally, Taxation relies on VITA as the contract administrator to maintain oversight and enforce the contract agreements with the ITISP contractors. While VITA is enforcing the service level agreement, it has not been able to compel the current ITISP contractors to install certain security patches to Taxation's systems to remediate vulnerabilities in a timely manner or taken actions to obtain these required services from another source.

The Commonwealth's Information Security Standard, SEC 501 (Security Standard) requires the installation of security-relevant software updates within 90 days of release. The Security Standard does allow for varying time periods depending on factors such as the criticality of the update, but generally the ITISP uses a 90-day window from the date of release as its standard for determining timely implementation of security patches (*Security Standard section: SI-2 Flaw Remediation*).

As of September 2020, the ITISP contractors had not applied a significant number of critical and highly important security patches to Taxation's server environment, all of which are past the 90-day Security Standard requirement. Missing system security updates cause an increased risk of cyberattack, exploit, and data breach by malicious parties.

Taxation is working with VITA and the ITISP contractors to ensure that all servers have all critical and highly important security patches installed. Additionally, our separate audit of VITA, which is ongoing, will address this issue.

STATUS OF PRIOR YEAR FINDINGS AND RECOMMENDATIONS

This section is organized by agency and reports the status of findings from the prior years' audit where corrective action is ongoing. Each status of prior year finding reported includes information on the type of finding, the severity classification for the finding, and an update on progress made since the issuance of the prior year's audit report. The severity classifications are discussed in more detail in the section titled "Independent Auditor's Report."

Department of Accounts

Continue to Dedicate Resources to Timely Update CAPP Manual Topics

Type: Internal Control and Compliance
Severity: Deficiency
Repeat: Partial (first issued in fiscal year 2019, with significant progress)
Prior Title: Dedicate Resources to Timely Update of CAPP Manual Topics

Accounts' management is not performing timely updates to payroll related topics in the Commonwealth Accounting Policies and Procedures (CAPP) Manual. Accounts updated five out of ten CAPP Manual topics that we identified in 2019 as outdated. The topics that Accounts updated excludes outdated payroll topics. During the fiscal year 2019 audit, we identified that these topics reference the Commonwealth's former accounting system and related processes. Accounts decommissioned the previous accounting system in July 2016. Accounts current plan is to update these sections after completion of the HCM project.

Section 2.2-803 of the Code of Virginia requires Accounts to provide authoritative guidance on the application of accounting policies, procedures, and systems. Further, having up-to-date and relevant policies and procedures is a key component of internal controls and ensures consistent processing of transactions throughout the Commonwealth. Accounts not updating CAPP Manual topics on a timely basis could have a negative impact on consistent transactional processing and financial reporting throughout the Commonwealth. In addition, the lack of up-to-date guidance could contribute to a break down in internal controls at the agency and institution level. Given limited resources and the ongoing project to replace the Commonwealth's current payroll system, Accounts' Payroll Operations plans to update payroll related topics after the implementation of the HCM project is complete. To compensate for having outdated payroll guidance in the CAPP manual, Payroll Operations is currently using an email listserv of agency/institution payroll contacts to communicate changes and updates to specific policies and procedures.

Accounts should dedicate the necessary resources and prioritize updating all outdated payroll CAPP Manual topics after the HCM project is complete. Though Accounts is currently using an email listserv to communicate changes to payroll policies and procedures, this is not a sufficient substitute for having updated and relevant authoritative guidance to which agency personnel can be held accountable.

Department of Planning and Budget

Continue to Improve Database Governance and Security

Type: Internal Control and Compliance
Severity: Significant Deficiency
Repeat: Partial (first issued in fiscal year 2019, with significant progress in all but one area)
Prior Titles: Improve the Budget System Database Governance and Security

The Department of Planning and Budget (Planning and Budget) continues to have inadequate policies and procedures to support its database environment to ensure it consistently secures the database that supports the Commonwealth's budget system in accordance with the Security Standard. While Planning and Budget resolved six of the seven weaknesses identified in the prior year, Planning and Budget continues to lack documented policies and procedures for implementing security controls and supporting the database. We communicated the details of the weaknesses for the system to management in a separate document marked Freedom of Information Act Exempt (FOIAE) under § 2.2-3705.2 of the Code of Virginia due to its sensitivity and description of security controls.

By not having documented policies and procedures, Planning and Budget increases the risk that required security controls and processes are not performed consistently. This also increases the risk for the data within the database to become unreliable, unavailable, or compromised.

Planning and Budget worked with its database administration consultant and VITA to resolve six of the prior year control weaknesses but was delayed in resolving the remaining weakness as it focused on other priorities to address the COVID-19 pandemic.

Planning and Budget should continue working with its database administration consultant and VITA to remediate the remaining weakness communicated in the FOIAE document to align their policies and procedures with the requirements in the Security Standard. These actions will help maintain the confidentiality, integrity, and availability of sensitive and mission critical data.

Department of Taxation

Continue to Improve Controls Over User Access

Type: Internal Control and Compliance
Severity: Significant Deficiency
Repeat: Yes (first issued in fiscal year 2017)
Prior Title: Improve Controls over Role Access

Taxation's management and its Office of Technology (Technology) did not properly restrict the access granted to users in their financial accounting and reporting system (system) based on the principle of least privilege. Although Taxation has various compensating controls in place, we found five of 33 users were provided access to critical access functions in excess of the job duties of the employees

assigned to these roles. Because of this, employees had unnecessary critical access in the financial accounting and reporting system.

Management made significant efforts to improve controls over the system's access, specifically through their recertification process. Management provided training to the various department managers emphasizing the importance of certifying access based on least privilege. Even with the efforts, users continued to have access to critical resources that were not necessary to their job functions. Managers stated that the users had access resources, such as approval and waive, that were not necessary for the employee's job responsibilities. The managers failed to identify these unnecessary access resources during the recertification process.

The Security Standard, Section 8.1 AC-6, requires an organization employ the principle of least privilege when granting access to ensure users only have access that is necessary to accomplish their assigned tasks. Management should ensure least privilege when certifying the access granted to ensure employees have the least amount of access necessary to perform their job duties. Additionally, Technology should ensure proper setup of the access functions to ensure they grant only the stated privileges in the financial accounting and reporting system.

Continue to Improve Disaster Recovery Planning Documentation

Type: Internal Control and Compliance
Severity: Significant Deficiency
Repeat: Yes (first issued in fiscal year 2018)
Prior Title: Improve Disaster Recovery Planning Documentation

Taxation continues to have disaster recovery documentation, specifically its Contingency Plan and IT Disaster Recovery Plan, that is inconsistent with its risk management documentation. Additionally, Taxation does not consistently use disaster recovery plan nomenclature in its contingency planning documentation.

Since the prior year, Taxation did not fully address this finding because it focused its priorities to further revise its Business Impact Analysis and complete risk assessments missing for some of its sensitive systems. We communicated the specific control weaknesses to management in a separate document marked FOIAE under § 2.2-3705.2 of the Code of Virginia due to it containing descriptions of security mechanisms.

Inconsistent recovery expectations and ambiguous language reduces the effectiveness of Taxation's disaster recovery planning documentation. Taxation should make the necessary revisions, as discussed in the separate FOIAE communication, to become compliant with the Security Standard and improve the effectiveness of its plans.

Continue Completing a Risk Assessment for Each Sensitive System

Type: Internal Control and Compliance
Severity: Significant Deficiency
Repeat: Yes (first issued in fiscal year 2019)
Prior Title: Complete a Risk Assessment for Each Sensitive System

Taxation is making satisfactory progress in updating and creating risk assessments for its sensitive systems; however, the following issues remain:

- Eleven of 42 risk assessments are incomplete. Taxation completed four risk assessments since our last review.

- Two of 31 completed risk assessments are more than three years old and have not been updated.

- Taxation did not perform annual self-assessments of the risk assessments.

The Security Standard, Section 6.2 requires Taxation have complete, reviewed, and updated risk assessments for all sensitive systems. Without having complete, reviewed, and updated risk assessments, Taxation increases the risk they will not detect and mitigate existing weaknesses in sensitive systems. By not detecting the weaknesses, it increases the risk of a malicious user compromising confidential data and impacting the system's confidential tax data and its availability.

These issues remain because Taxation focused its priorities on revising its Business Impact Analysis (BIA), sensitive system list, and IT system risk assessment template prior to dedicating its efforts to complete the remaining 11 risk assessments. While Taxation has not completed the risk assessments, it has interviewed key stakeholders for each sensitive system. In addition, Taxation did not complete self-assessments because of focusing on the BIA and missing risk assessments. However, Taxation has an ongoing project to complete, review, and update all risk management and contingency planning documents.

Taxation should continue dedicating the necessary resources to complete and update its risk assessments for each sensitive system. In addition, Taxation should maintain oversight of the IT risk assessments by conducting and documenting annual self-assessments.

Department of the Treasury

Continue to Improve Policies and Procedures over Unclaimed Property Reconciliations

Type: Internal Control
Severity: Significant Deficiency
Repeat: Yes (first issued in fiscal year 2019)
Prior Title: Improve Policies and Procedures over Unclaimed Property Reconciliations

In fiscal year 2019, we recommended that Department of Treasury's (Treasury) Unclaimed Property division (Unclaimed Property) improve its policies and procedures over the reconciliation between the unclaimed property system and the Commonwealth's accounting and financial reporting system. During fiscal year 2020, Unclaimed Property developed policies and procedures; however, they do not adequately resolve the issues noted in the prior year as they do not contain sufficient detail of the actual reconciliation process, nor explanations of how each system's information is used and how to document the reconciling items. In addition, the policies do not include requirements for timeliness of review by the Director of Unclaimed Property. Lastly, Unclaimed Property did not properly implement the newly developed reconciliation policies and procedures.

As a result, we found four of six reconciliations selected for testwork were prepared nine to 19 business days after the close of the fiscal month, which exceeds the five business days included in the Unclaimed Property policies and procedures. However, the reconciliations were completed within timeframes outlined in the CAPP Manual. In addition, we found that while reconciling items were not always clearly presented on the reconciliation, they were included within the supporting documentation.

CAPP Manual Topic 20905 – Cardinal Reconciliation Requirements requires all internally prepared accounting records, data submission logs, and other accounting data to be reconciled to reports produced by the Commonwealth's accounting and financial reporting system by the last business day of the month following the period close. In addition, Topic 20905 prescribes the level of detail at which agency records, accounts, and logs must be reconciled depending on the nature of the transactions. If recorded in multiple systems, transactions should be traced from one system to another, any variance between accounting data should be traced to specific transactions, and all variances should be explained and justified. Policies and procedures should be complete and customized to reflect agency staffing, organization, and operating procedures.

Reconciliations are a key internal control for ensuring financial activity recorded in multiple systems is accurate in each of those systems and for preventing improper payments. In addition, the improper reconciliation of systems increases the risk of material misstatement for account balances related to Unclaimed Property activity. Inadequately detailed policies and procedures over the reconciliation process coupled with untimely start dates and process changes due to COVID-19 pandemic contributed to the issues we noted with the reconciliations reviewed.

Unclaimed Property should continue to improve its existing policies and procedures over the reconciliation between the unclaimed property system and the Commonwealth's accounting and financial reporting system to ensure they are sufficiently detailed to reflect the unique operations of the Unclaimed Property division. Unclaimed Property should better explain reconciling items on the

reconciliation instead of notations within supporting documentation. Further, the reconciliations should be signed and dated by the reviewer and reviewed timely in accordance with the Unclaimed Property policies and procedures as well as the CAPP Manual.

Continue to Improve Process for Payment of Risk Management Invoices

Type: Internal Control and Compliance
Severity: Significant Deficiency
Repeat: Yes (first issued in fiscal year 2019)
Prior Title: Improve Process for Payment of Risk Management Invoices

Treasury's Risk Management Division (Risk Management) is not adequately monitoring or ensuring compliance with the prompt payment provisions in the Code of Virginia. We noted this issue in our fiscal year 2019 report, indicating that improvements are still in process in the current year. Risk Management does not have sufficient oversight in place to ensure all invoices received are being processed and paid according to the prompt payment provisions regardless of whether the invoice is received by Risk Management directly or if the invoice is received via the Office of the Attorney General. We found six of 55 invoices were paid at greater than the 30-day prompt payment limitation. The late invoices were paid an average of five days after the 30-day limit for the selected vouchers from Risk Management's account payables system, and an average of 41 days late for selected vouchers generated outside of the Risk Management's system.

Section 2.2-4347 of the Code of Virginia states that agencies are required to pay invoices no later than 30 calendar days after the receipt of the goods, services, or invoice, whichever is later, or the due date specified in the vendor's contract. Failure to follow prompt pay requirements established by the Commonwealth may harm the Commonwealth's reputation as a buyer, damage relationships with vendors, and result in late fees.

Risk Management had to transition to an electronic work environment due to the effects of the COVID-19 pandemic. Staff and management worked to re-engineer the existing payment process, including setting up a dedicated email inbox for incoming invoices, daily monitoring of the emails, assigning additional staff, and a redistribution of responsibilities to facilitate the workflow balance in the invoice review process. Risk Management indicated that as with any new process, this posed challenges to the timeliness of approving the payments and getting the payments to Treasury's Operations Division (Operations). Operations indicated that Risk Management receives an influx of invoices towards the end of the calendar year, leading to an increased workload.

Risk Management and Operations should strengthen their internal controls and policies and procedures and should further develop and improve procedures, train staff adequately, and maintain sufficient management oversight of the payment process to ensure compliance with prompt payment provisions. Additionally, management should ensure that adequate staffing is available in both Risk Management and Operations to ensure that invoices be paid timely during the high-volume periods anticipated during the year.

INTERNAL CONTROL AND COMPLIANCE FINDINGS AND RECOMMENDATIONS

This section is organized by agency, and each finding reported includes information on the type of finding and the severity classification for the finding. The severity classifications are discussed in more detail in the section titled "Independent Auditor's Report."

Department of Accounts

Ensure Timely Approval of ChartField Changes

Type: Internal Control
Severity: Significant Deficiency
Repeat: No

Accounts' General Accounting division is not timely performing reviews of Statewide ChartField changes in the Commonwealths' accounting and financial reporting system (system). For ten of 20 changes tested, we found Accounts did not perform a timely review of changes made to the chart of accounts within the system during fiscal year 2020. These changes consisted of the creation of new funds, a program, capital projects, and a revenue account.

Pursuant to § 2.2-803 of the Code of Virginia, Accounts is responsible for financial data classification and coding structures for agencies. Further, Accounts must approve changes to any established financial related code or set of codes for agencies. Section 60100 of the CAPP Manual requires Accounts' General Accounting division to enter and approve changes to the Statewide ChartFields within the system. Accounts uses a ChartField Maintenance form to ensure consistency of information reviewed to sufficiently support the reason for the change and required approvals. While Accounts provided forms to support all changes, the General Accounting division did not timely perform the overall review for 50 percent of the ChartField Maintenance forms we reviewed during our test work. Accounts not performing timely reviews of data elements within the system could lead to inaccurate reporting in the Commonwealth's CAFR, financial statements individually issued by state agencies, and other reports used by management and those charged with governance to monitor financial activity.

While the majority of Accounts' untimely review is due to implications of the COVID-19 pandemic, another cause was a delay in Accounts receiving supporting documentation needed to finalize the approval for one ChartField change. Accounts should reexamine existing processes for updating and approving ChartField maintenance changes and dedicate the necessary resources to ensure management is approving ChartField changes in a timely manner.

Department of Planning and Budget

Improve Audit Logging and Monitoring Controls

Type: Internal Control and Compliance
Severity: Significant Deficiency
Repeat: No

Planning and Budget does not implement certain audit logging and monitoring safeguards for the database that supports the Commonwealth's budget system in accordance with the Security Standard. We communicated two control weaknesses to management in a separate document marked FOIAE under § 2.2-3705.2 of the Code of Virginia due to its sensitivity and description of security controls.

The Security Standard requires audit logging and monitoring controls to protect the confidentiality, integrity, and availability of sensitive and mission critical data. Due in part to limited resources, Planning and Budget was not able to implement the necessary safeguards described in the FOIAE document and comply with the Security Standard.

Planning and Budget should dedicate the necessary resources to implement the security controls discussed in the communication marked FOIA Exempt in accordance with the Security Standard. This will help maintain the confidentiality, integrity, and availability of Planning and Budget's sensitive and mission critical data.

Review and Update Baseline Configuration Standards

Type: Internal Control and Compliance
Severity: Significant Deficiency
Repeat: No

Planning and Budget does not review and update its baseline configuration for its database environment. Baseline configurations are essential controls in information technology environments to ensure that systems have appropriate configurations and serve as a basis for implementing or changing existing information systems.

Planning and Budget adopts VITA's baseline configuration for the database environment to secure its information systems, including the Commonwealth's budget system. However, Planning and Budget references a baseline configuration that was last revised in 2017.

The Security Standard requires Planning and Budget review and revise all security configuration standards annually or more frequently as needed (*Security Standard section: CM-2 Baseline Configuration, CM-2-COV*).

Without reviewing and updating its baseline configurations for its environment, Planning and Budget increases the risk that the security hardening configurations are out-of-date or no longer

applicable, potentially compromising the confidentiality, integrity, and availability of its sensitive and mission critical systems that follow the baseline configurations.

Because of limited agency resources to manage its database internally, Planning and Budget outsources database administration to a consultant. While Planning and Budget and the consultant adopted VITA's baseline configurations for the database environment, neither Planning and Budget nor the consultant performed an annual review of the baseline to determine if the minimum requirements outlined are up-to-date or checked for a new release from VITA.

Planning and Budget should work with its consultant to review and revise its baseline configuration on an annual basis to ensure it reflects current security requirements in the Security Standard and industry best practices. Performing annual reviews of the baseline configurations will help protect the confidentiality, integrity, and availability of Planning and Budget's mission critical data.

Department of Taxation

Improve Patching to Mitigate Vulnerabilities

Type: Internal Control and Compliance
Severity: Significant Deficiency
Repeat: No

Taxation failed to apply a small percentage of patches to software running on its systems in a timely manner. Taxation's patching process missed some specific software patches and is therefore not in compliance with the Security Standard.

While Taxation relies on the contractors procured by VITA to install security patches to its IT infrastructure components, Taxation remains responsible for applying patches to certain agency-specific software. We communicated the specific control weaknesses to management in a separate document marked FOIAE under § 2.2-3705.2 of the Code of Virginia due to its sensitivity and description of security controls.

The Security Standard requires Taxation to install security-relevant software and firmware updates within 90-days of the release of the updates. Software vulnerabilities are common flaws that potentially malicious actors use to infiltrate a network and initiate an attack, which can lead to financial, legal, and reputational damages for Taxation. Without appropriate software patching and vulnerability management controls, Taxation increases the risk of unauthorized access to sensitive and mission critical systems.

Taxation should dedicate the necessary resources to apply security patches to mitigate the outstanding vulnerabilities within its IT environment. This will help maintain the confidentiality, integrity, and availability of sensitive and mission critical data.

Ensure Employees Complete Required Conflict of Interest Training

Type: Internal Control and Compliance
Severity: Significant Deficiency
Repeat: No

Taxation did not ensure employees completed the required conflict of interest training within the timeframe outlined in the Code of Virginia. Specifically, 21 of 25 Statement of Economic Interest (SOEI) Form Taxation filers tested did not complete the conflict-of-interest training within the required timeframe.

Pursuant to § 2.2-3128 through 2.2-3131 of the Code of Virginia, each state filer shall attend the orientation course within two months after he or she becomes a state filer and at least once during each consecutive period of two calendar years commencing on the first odd-numbered year thereafter. In addition, § 2.2-3129 of the Code of Virginia requires agencies to keep a record of attendance that includes the specific attendees, each attendee's job title, and the dates of attendance for a period of not less than five years after each course is given.

Taxation did not provide documentation of employee's compliance with SOEI training requirements. Not completing the training may result in Taxation not being able to rely on its employees to effectively recognize, disclose, and resolve conflicts of interest. Taxation could be susceptible to actual or perceived conflicts of interest that would impair or appear to impair the objectivity of certain decisions made by employees in positions of trust. Additionally, not completing the conflict-of-interest orientation course may prevent Taxation employees from recognizing or properly disclosing a conflict of interest.

Taxation should ensure compliance with the Code of Virginia by monitoring all employees designated in a position of trust to ensure they complete the required conflict of interest training within two months of becoming a filer and once within each consecutive period of two calendar years thereafter. In addition, Taxation should maintain a record of such attendance.

FINANCE SECRETARIAT OVERVIEW

The Secretary assists the Governor in the management and direction of the finance agencies and performs program coordination, policy planning, and budget formulation activities. To accomplish this, the Secretary oversees four agencies which perform critical functions in the Commonwealth's statewide financial management system. These agencies are the Departments of Accounts, Planning and Budget, Taxation, the Treasury and the Treasury Board. The individual audits of these agencies primarily support the audit of the CAFR for the fiscal year ended June 30, 2020, and this report is intended to report on the results of this work.

The Secretary also oversees the Virginia Board of Accountancy (Accountancy) which is not material to the Commonwealth's CAFR and not included in the scope of this audit. In accordance with § 54.1-4420 of the Code of Virginia, we perform an annual audit over Accountancy. The results of our review of Accountancy can be found at www.apa.virginia.gov.

Accounts, Planning and Budget, Taxation, and Treasury and work closely together in the budgeting, managing, and reporting of the Commonwealth's financial resources. They handle all of the financial transactions of the Commonwealth, from collecting taxes to paying bills to distributing aid to localities. Their primary responsibilities include:

- forecasting and collecting revenues;
- preparing and executing the Commonwealth's budget;
- managing the Commonwealth's cash and investments;
- issuing bonds on behalf of various boards and authorities;
- administering the Commonwealth's statewide accounting and payroll systems;
- overseeing the Commonwealth's financial reporting processes; and
- making strategic financial plans.

These agencies primarily serve other agencies within the Commonwealth in a central support capacity. General fund dollars are the primary funding source for their operations. Table 1 summarizes the original and final operating budgets, as well as expenses for all finance agencies except the Treasury Board. The Treasury Board's financial activity is not included since its activities consist primarily of the payment of debt service on general obligation and appropriation-supported debt rather than administrative expenses. In addition, Table 1 excludes funds that do not pertain to the administrative duties of Taxation and Accountancy's financial activity.

Summary of Budget and Expenses for Fiscal Year 2020

Table 1

	Original Budget	Final Budget	Expenses
Secretary of Finance	$ 667,595	$ 797,138	$ 737,545
Department of Accounts	42,354,357	73,496,965	68,279,440
Department of Planning and Budget	8,015,465	8,591,672	6,290,738
Department of Taxation	113,105,467	116,822,251	110,054,857
Department of the Treasury	47,938,950	55,225,695	50,734,042
Total	**$212,081,834**	**$254,933,721**	**$236,096,622**

Source: Commonwealth's accounting and financial reporting system

The most significant budgetary changes within the Finance agencies took place in Accounts. The $31.1 million increase in Accounts' final budget primarily relates to additional funding for the Commonwealth's Human Capital Management System.

RETAIL SALES AND USE TAX COLLECTION AND DISTRIBUTION

In accordance with § 30-133.2 of the Code of Virginia, we perform work related to retail sales and use tax distributions as part of our annual audit of Taxation. Our review covers retail sales and use tax with a focus on the collection and distribution of local sales and use taxes. As part of our initial review, we reviewed activity for fiscal years 2009 through 2012 and established a benchmark by which to evaluate errors in the process.

In fiscal year 2020 Taxation collected approximately $7 billion in retail sales and use taxes, with $1.4 billion of these revenues being distributed to localities as a one percent local option tax. Taxation collects the tax and determines the local portion, which is distributed to the locality where the sale or activity occurred.

The sales and use tax distribution process requires a joint effort between Taxation, localities, and businesses. There are a number of controls and processes in place to help ensure that locality distributions are accurate and made to the correct locality. When Taxation detects an error, they process an adjustment to correct the distribution and transfers the funds to the correct locality. Errors most frequently occur because a taxpayer does not allocate the proper amounts to the locality or a taxpayer has a liability in more than one locality.

Table 2 shows the local distribution amount for retail sales and use tax, as well as the amount and rate of distribution errors identified and corrected by Taxation in each of the last three fiscal years.

Error Rate for Local Sales Tax Distributions

Table 2

	2018	2019	2020
Local distribution amount	$1,243,480,343	$1,292,803,736	$1,358,988,341
Errors identified and corrected	4,716,646	4,979,795	6,286,195
Error rate	0.38%	0.39%	0.46%

Source: Taxation's financial accounting and reporting system

As shown above, the error rate for fiscal year 2020 was 0.46 percent. This is within the one percent benchmark established and an increase from the fiscal year 2019 error rate of 0.39 percent. Based on these results, it appears that the error rate is within the established benchmark, and Taxation is properly distributing the local portion of the retail sales and use tax. We do not recommend any changes in the established benchmark.

Commonwealth of Virginia

Auditor of Public Accounts

Staci A. Henshaw, CPA
Auditor of Public Accounts

P.O. Box 1295
Richmond, Virginia 23218

December 15, 2020

The Honorable Ralph S. Northam
Governor of Virginia

The Honorable Kenneth R. Plum
Chairman, Joint Legislative Audit
and Review Commission

We have audited the financial records, operations, and federal compliance of the **Agencies of the Secretary of Finance** for the year ended June 30, 2020. We conducted this audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States, in support of the Commonwealth's Annual Financial Report and Single Audit. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Audit Objectives

Our primary audit objectives for the audit of the Departments of Accounts, Planning and Budget, Taxation, and the Treasury for the fiscal year ended June 30, 2020, include the following:

- to evaluate the accuracy of financial transactions related to tax collections, including accounts receivable, unearned revenues and taxes, accounts payable and other liabilities, tax abatements, and tax and interest revenue as reported in the Commonwealth's accounting and financial reporting system and Taxation's accounting and financial reporting system and in supplemental information prepared by Taxation;

- to evaluate the accuracy of financial transactions related to cash and cash equivalents, investments, debt, risk management, and unclaimed property activity, which is controlled by Treasury as reported in the Commonwealth's accounting and financial reporting system, Treasury's internal systems and accounting records, and in supplemental information prepared by Treasury (including the activity of the Treasury Board, the Local Government Investment Pool, the Virginia College Building Authority, the Virginia Public School Authority, and the Virginia Public Building Authority);

- to evaluate whether the budget approved by the General Assembly is appropriately recorded in the Commonwealth's accounting and financial reporting system and controls in this system are adequate to ensure program expenses do not exceed appropriations;

- to determine whether management has established and maintained internal controls over the Commonwealth's financial reporting and other central processes and the centralized services provided to agencies and institutions in support of the preparation of the financial statements as indicated in the Audit Scope and Methodology section of this report;

- to determine whether management has established and maintained adequate operating and application system controls over the Commonwealth's accounting and financial reporting, payroll, budget, capital asset, and lease accounting systems and other internal systems as referenced in the Audit Scope and Methodology section;

- to determine whether the agencies have complied with applicable laws, regulations, contracts, and grant agreements;

- test federal compliance in support of the Commonwealth's Single Audit; and

- to review corrective actions related to audit findings from the prior year report.

Audit Scope and Methodology

Management has responsibility for establishing and maintaining internal control and complying with applicable laws, regulations, contracts, and grant agreements. 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, regulations, contracts, and grant agreements.

We gained an understanding of the overall internal controls, both automated and manual, sufficient to plan the audit. We considered materiality and risk in determining the nature and extent of our audit procedures. Our review encompassed controls over the following processes and systems.

Department of Accounts

Financial reporting*
Commonwealth's accounting and financial reporting system
Commonwealth's payroll system
Commonwealth's capital asset system
Commonwealth's lease accounting system
Administrative activities
Coronavirus Relief Fund - Catalog of Federal Domestic Assistance 21.019

*Including preparation of the Comprehensive Annual Financial Report and Schedule of Expenditures of Federal Awards.

Department of Planning and Budget

Budget execution
Commonwealth's budgeting system

Department of Taxation

Financial reporting
Tax return processing
Tax revenue collections
Taxation's accounting and financial reporting system
Administrative activities

Department of the Treasury (including Treasury Board operations)

Financial reporting*
Bond issuance
Debt service expenses
Investment trading
Investment accounting
Investment accounting systems
Bank reconciliation system
Trust accounting
Check processing
Risk management claim processing
Management of unclaimed property
Access controls
System change controls

*Including preparation of financial statements of the Local Government Investment Pool Program, the Virginia College Building Authority, the Virginia Public Building Authority, and the Virginia Public School Authority.

The Virginia Board of Accountancy falls under the control of the Secretary of Finance; however, is not material to the Comprehensive Annual Financial Report for the Commonwealth of Virginia. As a result, this agency is not included in the scope of this audit.

We performed audit tests to determine whether the controls were adequate, had been placed in operation, and were being followed. Our audit also included tests of compliance with provisions of applicable laws, regulations, contracts, and grant agreements. Our audit procedures included inquiries of appropriate personnel, inspection of documents, records, and contracts, and observation of the agencies' operations. We performed analytical procedures, including budgetary and trend analyses. We confirmed cash, investments, and loan balances with outside parties. We also tested details of transactions to achieve our objectives.

A nonstatistical sampling approach was used. Our samples of transactions were designed to support conclusions about our audit objectives. An appropriate sampling methodology was used to ensure the samples selected were representative of the population and provided sufficient, appropriate evidence. We identified specific attributes for testing each of the samples and when appropriate, we projected our results to the population.

Our consideration of internal control over financial reporting (internal control) was for the limited purpose described in the section "Audit Objectives" and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and, therefore, material

weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. We did identify certain deficiencies in internal control as described in the sections entitled "Status of Prior Year Findings and Recommendations" and "Internal Control and Compliance Findings and Recommendations," that we consider to be significant deficiencies.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial information will not be prevented or detected and corrected on a timely basis. A significant deficiency is a deficiency or a combination of deficiencies in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We have explicitly identified 11 findings in the sections titled "Status of Prior Year Findings and Recommendations," and "Internal Control and Compliance Findings and Recommendations," as significant deficiencies for the Commonwealth.

In addition to the significant deficiencies, we detected a deficiency in internal control that is not significant to the Commonwealth's Comprehensive Annual Financial Report and Single Audit but is of sufficient importance to warrant the attention of those charged with governance. We have explicitly identified one finding in the section titled "Status of Prior Year Findings and Recommendations" as a deficiency.

Conclusions

We found that Taxation properly stated, in all material respects, the financial records reviewed in support of the tax collections activity detailed in the audit objectives as reported in the Commonwealth's accounting and financial reporting system, Taxation's accounting and financial reporting system, and supplemental information.

We found that Treasury properly stated, in all material respects, the financial records reviewed in support of the cash and cash equivalents, investments, debt, risk management, and unclaimed property activity reported in Commonwealth's accounting and financial reporting system, Treasury's internal systems and accounting records, and supplemental information.

We found that the budget approved by the General Assembly is appropriately recorded in the Commonwealth's accounting and financial reporting system, and controls in this system were adequate to ensure program expenses did not exceed appropriations.

We noted certain matters at Accounts, Planning and Budget, Taxation, and Treasury involving internal control and its operation and compliance with applicable laws and regulations that require management's attention and corrective action. These matters are described in the sections titled "Status of Prior Year Findings and Recommendations," and "Internal Control and Compliance Findings and Recommendations."

The agencies of the Secretary of Finance have taken adequate corrective action with respect to audit findings reported in the prior year that are not referenced in this report.

Since the findings noted above include those that have been identified as significant deficiencies, they will be reported as such in the "Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of the Financial Statements Performed in Accordance with Government Auditing Standards," which is included in the Commonwealth of Virginia's Single Audit Report for the year ended June 30, 2020. The Single Audit Report will be available at www.apa.virginia.gov in February 2021.

Exit Conference and Report Distribution

We discussed this report with management of the respective agencies of the Secretary of Finance and have included their responses at the end of this report in the section titled "Agency Responses." We did not audit management's responses and, accordingly, we express no opinion on them. Additionally, on January 7, 2021 we provided management of the VITA with a copy of the Risk Alert titled "Mitigate Server Vulnerabilities" for their response. VITA's management elected not to provide a response for inclusion in the audit report and intends to provide a response for inclusion in its audit report to be issued at a later date.

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.

Staci A. Henshaw
AUDITOR OF PUBLIC ACCOUNTS

AVC/clj

COMMONWEALTH of VIRGINIA

DAVID A. VON MOLL, CPA
COMPTROLLER

Office of the Comptroller

P. O. BOX 1971
RICHMOND, VIRGINIA 23218-1971

January 22, 2021

Ms. Staci A. Henshaw
Auditor of Public Accounts
James Monroe Building
101 N. 14th Street
Richmond, Virginia 23219

Dear Ms. Henshaw:

The Department of Accounts (Accounts) appreciates the opportunity to respond to the *Status of Prior Year Recommendations* and *Internal Control and Compliance Findings and Recommendations* contained in your 2020 Secretary of Finance Audit Report. We give your comments the highest level of importance and consideration as we continue to review and improve our current practices.

Status of Prior Year Recommendations

Continue to Dedicate Resources to Timely Update CAPP Manual Topics

Accounts acknowledges the importance of updating the Commonwealth Accounting Policies and Procedures (CAPP) Manual. Accounts appreciates the acknowledgement of the progress made to update five of the ten topics identified in the 2019 report and the compensating efforts taken to promptly communicate cricital changes and updates to users related to the other topics. Accounts will update job aids within the Cardinal Human Capital Resource module and related CAPP topics during calendar year 2021.

Internal Control and Compliance Recommendations

Ensure Timely Approval of ChartField Changes

Accounts acknowledges the importance of prompt review and approval of Statewide ChartField changes in the Commonweatlh's accounting and financial reporting system, Cardinal. Accounts agrees that the documentation is not being reviewed timely. Further, Accounts appreciates the acknowledgement that the COVID-19 pandemic contributed to this lack of timely review since resources were required to prioritize and establish new funds and address numerous COVID-19 requirements. Additionally, while the documentation was not reviewed timely, Accounts believes that Cardinal data was correct. This is due, in part, to compensating controls. Cardinal user agencies would notify Accounts of any errors. Also, routine reviews of Cardinal data by Accounts identifies needed revisions to fund descriptions.

(804) 225-2109 FAX (804) 786-3356 TDD (804) 371-8588

Accounts plans to develop more robust procedures for the Chartfield Maintenance process. This will result in streamlining the process and should allow for timely ChartField Maintenance documentation approval. Accounts plans to complete this process in calendar year 2021.

Sincerely,

David A. Von Moll

Copy: The Honorable Aubrey L. Layne, Jr., Secretary of Finance
Lewis R. McCabe, Jr., Deputy State Comptroller

COMMONWEALTH *of* VIRGINIA
Department of Planning and Budget

DANIEL S. TIMBERLAKE
Director

1111 E. Broad
Street Room 5040
Richmond, VA 23219-1922

February 2, 2021

Ms. Staci A. Henshaw
Auditor of Public Accounts
James Monroe Building
101 N. 14th Street
Richmond, Virginia 23219

Dear Ms. Henshaw:

The Department of Planning and Budget (DPB) appreciates the opportunity to respond to the findings and recommendations contained in the 2020 Secretary of Finance Report. DPB has reviewed the findings and recommendations provided by the Auditor of Public Accounts (APA) as part of its audit of financial records and operations for the fiscal year that ended on June 30, 2020. I offer the following response to the internal control and compliance findings and recommendations for DPB.

Status of Prior Year Recommendations

Improve the Budget System Database Governance and Security

DPB acknowledges the importance of having adequate policies and procedures to support its database environment in accordance with the Security Standard. DPB appreciates the acknowledgement that it has worked to correct six of the seven weaknesses identified in fiscal year 2019 and is currently working with its external vendors and with the Virginia Information Technologies Agency (VITA) to put in place the remaining policies and procedures needed to resolve this finding.

FAX (804) 225-3291 (804) 786-7455 TDD (804) 786-7578

Internal Control and Compliance Findings and Recommendations

Improve Audit Logging and Monitoring Controls

DPB acknowledges the importance of implementing certain audit logging and monitoring safeguards for its database that supports the Commonwealth's budget system in accordance with the Security Standard. DPB agrees that it needs to develop a policy to put proper controls in place. In response to this finding, DPB is currently working with its external vendors and the Virginia Information Technologies Agency (VITA) to address the safeguards needed to resolve this finding.

Review and Update Baseline Configuration Standards

DPB acknowledges the importance of implementing a schedule for reviewing its baseline configuration in accordance with the Security Standard. In response to this finding, DPB is currently working with external vendors to institute a formal review process to ensure that its database reflects requirements in the Security Standard and industry best practices. This review began in January of 2021 and will be performed annually or more frequently if deemed necessary.

DPB will use your findings and recommendations as it works to review and continually improve its existing practices and policies. Thank you again for the opportunity to respond to your report.

Sincerely,

Daniel S. Timberlake

c: The Honorable Aubrey L. Layne, Jr.

COMMONWEALTH of VIRGINIA

Department of Taxation

January 29, 2021

Ms. Staci A. Henshaw
Auditor of Public Accounts
James Monroe Building
101 N. 14th Street
Richmond, VA 23219

Dear Ms. Henshaw:

The Department of Taxation ("Virginia Tax") has reviewed the findings and recommendations provided by the Auditor of Public Accounts as part of your audit of the agency's financial records and operations for the year ended June 30, 2020. I appreciate both the effort and professionalism of your staff in the performance of the audit and the opportunity to provide the following responses to address the report findings.

Risk Alert-Mitigate Server Vulnerabilities

It should be noted that Virginia Tax leadership formally communicates the status of this issue with VITA executive management each quarter. In addition, our agency technology staff meet routinely with VITA staff on other issues, including patching. Virginia Tax will continue to work with VITA to ensure server patches are being applied in a timely manner. The correction of this control is beyond the control of Virginia Tax.

Continue to Improve Controls over User Access

Virginia Tax has corrected the specific identified issues noted in the report and reviewed the proper procedures for least privilege with those supervisors responsible. Considering the thousands of accesses reviewed and approved annually that are accurate and consistent with the least privilege expectations; Virginia Tax has made substantial progress over the past few years in this area and is largely succeeding in addressing this issue.

Virginia Tax will continue to train and educate all staff in supervisory positions about the importance of least privilege and their role in ensuring our full compliance. Virginia Tax will provide global reminders to all existing and especially new supervisors

by providing local area training and education. Clear and concise expectations will be set for the next system access recertification scheduled for completion on July 31, 2021.

Continue to Improve Disaster Recovery Planning Documentation

The revised Business Impact Analysis document was completed January 1, 2021. The Disaster Recovery Plan and the Continuity Plan (CP) documents will be updated by June 30, 2021.

Continue Completing a Risk Assessment for Each Sensitive System

Virginia Tax will complete a risk assessment plan that will assess and report risks of sensitive systems as required by SEC501 by August 30, 2021.

Improve Patching to Mitigate Vulnerabilities

Virginia Tax Technology personnel will apply the missing patches and comply with the requirements noted in SEC 501 on a go-forward basis by September 30, 2021.

Comply with Conflicts of Interest Act Training

The training documented in your report was completed on November 20, 2020.

Thank you for the opportunity to respond to your report. The Department strives to maintain strong internal controls and business processes that ensure high standards of integrity, efficiency, and control.

Sincerely,

Craig M. Burns
Tax Commissioner

Cc: The Honorable Aubrey L. Layne, Jr., Secretary of Finance

COMMONWEALTH of VIRGINIA

MANJU S. GANERIWALA
TREASURER OF VIRGINIA

Department of the Treasury

P.O. BOX 1879
RICHMOND, VIRGINIA 23218-1879
(804) 225-2142
FAX (804) 225-3187

January 22, 2021

Ms. Staci Henshaw
Auditor of Public Accounts
101 N. 14th Street, 8th Floor
Richmond, VA 23219

Dear Ms. Henshaw,

The Department of the Treasury (Treasury) welcomes the opportunity to respond to the recommendations in your Report on the Audit of the Agencies of the Secretary of Finance for the fiscal year ended June 30, 2020. Treasury appreciates the recognition of our progress in addressing previous concerns as noted in the report. Additionally, your comments and recommendations are appreciated and given the highest level of consideration by Treasury as we continually strive to improve our processes.

Comments to Management

Improve Policies and Procedures over Unclaimed Property Reconciliations

The Unclaimed Property Division (UCP) will continue to improve the monthly reconciliation policy and procedures and ensure compliance with all requirements. Treasury will continue to follow the guidance provided in the Commonwealth Accounting Policies and Procedures Manual (CAPP) in the updated reconciliation policy and procedures.

Improve Process for Payment of Risk Management Invoices

The Risk Management Division will continue to work with the Operations division to streamline the payment process and strengthen internal controls to ensure payments are made in compliance with the Prompt Pay Act, Code of Virginia § 2.2-4347.

Sincerely,

Manju S. Ganeriwala

cc: The Honorable Aubrey L. Layne Jr., Secretary of Finance

SECRETARY OF FINANCE AGENCY OFFICIALS

As of June 30, 2020

Aubrey L. Layne, Jr.
Secretary of Finance

David A. Von Moll
Comptroller

Daniel S. Timberlake
Director of the Department of Planning and Budget

Craig M. Burns
Tax Commissioner

Manju S. Ganeriwala
Treasurer