

**DEPARTMENT OF ENVIRONMENTAL QUALITY
RICHMOND, VIRGINIA**

**REPORT ON AUDIT
FOR THE YEAR ENDED
JUNE 30, 1999**

***AUDITOR OF
PUBLIC
ACCOUNTS***



COMMONWEALTH OF VIRGINIA

AUDIT SUMMARY

Our audit of the Department of Environmental Quality for the year ended June 30, 1999, found:

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

no material weaknesses in the internal control structure; and

no instances of noncompliance with applicable laws and regulations tested that are
required to be reported.

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May 8, 2000

The Honorable James S. Gilmore, III
Governor of Virginia
State Capitol
Richmond, Virginia

The Honorable Vincent F. Callahan, Jr.
Chairman, Joint Legislative Audit
and Review Commission
General Assembly Building
Richmond, Virginia

INDEPENDENT AUDITOR'S REPORT

We have audited the financial records and operations of the **Department of Environmental Quality** for the year ended June 30, 1999. We conducted our audit in accordance with Government Auditing Standards, issued by the Comptroller General of the United States.

AUDIT OBJECTIVES, SCOPE, AND METHODOLOGY

Our audit's primary objectives were to evaluate the accuracy of recording financial transactions on the Commonwealth Accounting and Reporting System, adequacy of the Department's internal control, and test compliance with applicable laws and regulations.

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

| | |
|-------------------|--------------|
| Revenues | Payroll |
| Expenditures | Fixed Assets |
| Grants Management | |

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

The Department's management has responsibility for establishing and maintaining internal control and complying with applicable laws and regulations. Internal control is a process designed to provide reasonable, but not absolute, assurance regarding the reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations.

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

AUDIT CONCLUSIONS

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

We noted no matters involving internal control and its operation that we considered to be material weaknesses. Our consideration of internal control would not necessarily disclose all matters in internal control that might be material weaknesses. A material weakness is a condition in which the design or operation of the specific internal control components does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material to financial operations may occur and not be detected promptly by employees in the normal course of performing their duties.

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

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

EXIT CONFERENCE

We discussed this report with management at an exit conference held on April 23, 2000.

AUDITOR OF PUBLIC ACCOUNTS

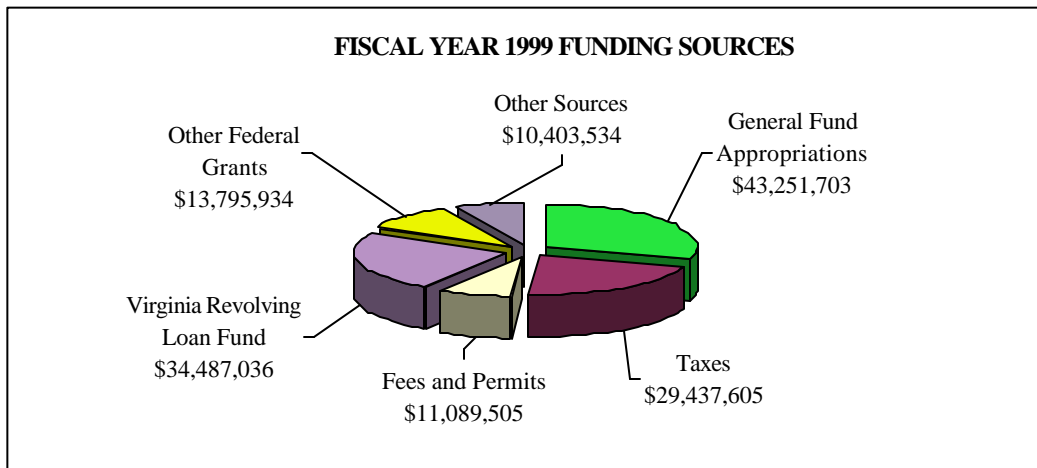
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SELECTED AGENCY INFORMATION

General Overview

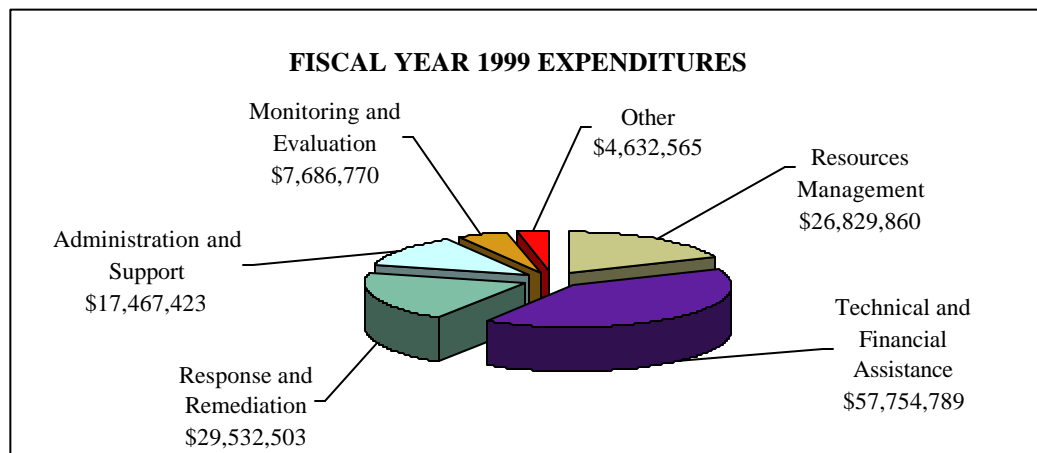
The Department of Environmental Quality protects the Commonwealth's natural resources by administering state and federal environmental programs, issuing permits, monitoring water and air quality, and inspecting waste facilities. Additionally, the Department enforces regulations promulgated by the State Water Control Board, the Board of Waste Management, and the Air Pollution Control Board.

The following chart illustrates the Department's funding sources for fiscal year 1999:



Taxes represent funds collected by other agencies and transferred to the Department for activities such as litter control, vehicle emissions inspection, or waste tire disposal. Other sources include recovery of indirect costs (\$3,976,088), civil penalties and charges (\$1,162,108), interest (\$4,164,234), and miscellaneous revenue (\$1,101,104).

The following chart shows the spending levels for the Department's various programs during fiscal year 1999:



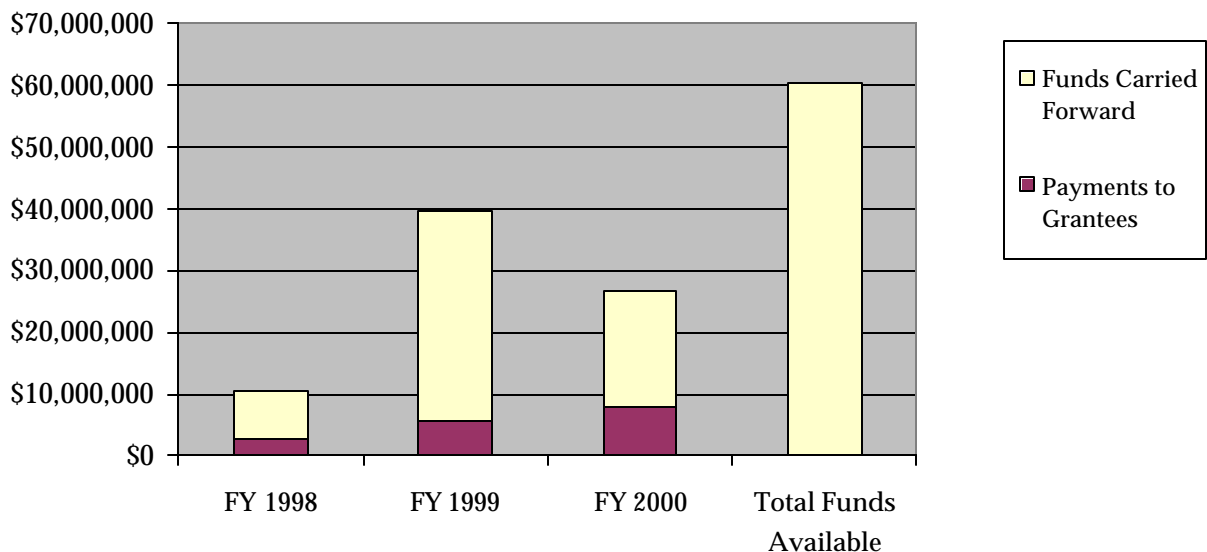
Other programs include Research and Planning (\$2,696,240), Policy and Program Development (\$595,914), and Information and Education Assistance (\$1,340,411).

Virginia Water Quality Improvement Fund

The Water Quality Improvement Act of 1997 established the Water Quality Improvement Fund, which provides grants to local governments, soil and water conservation districts, and individuals for point and nonpoint-source pollution prevention, reduction, and control programs. The Department administers the point source pollution control portion of the program. As of March 31, 2000, the Department has awarded \$59.9 million in reimbursement-basis grants for water quality improvement projects under 16 grant agreements. To date, reimbursements total approximately \$16.2 million (or 27 percent of grants awarded). The following chart exhibits Water Quality Improvement Fund financial activity.

| | <u>1998</u> | <u>1999</u> | <u>2000*</u> | <u>Total</u> |
|-----------------------|---------------------|---------------------|---------------------|----------------------|
| Revenues | | | | |
| General funds | \$10,000,000 | \$37,100,000 | \$25,150,000 | \$72,250,000 |
| Interest | <u>434,358</u> | <u>2,463,445</u> | <u>1,486,936</u> | <u>4,384,739</u> |
| Total revenues | 10,434,358 | 39,563,445 | 26,636,936 | 76,634,739 |
| Payments to grantees | <u>(2,688,177)</u> | <u>(5,673,418)</u> | <u>(7,810,742)</u> | <u>(16,172,337)</u> |
| Funds carried forward | <u>\$ 7,746,181</u> | <u>\$33,890,027</u> | <u>\$18,826,194</u> | <u>\$ 60,462,402</u> |

* As of March 31, 2000.



As shown in the above chart, at March 31, 2000, approximately \$60.5 million is available to support point source program objectives. Although there are no signed agreements to obligate any of the FY 2000 appropriation, the Department has received 19 applications seeking approximately \$94.6 million in grant funds. Additionally, the Department has additional potential obligations of approximately \$15.1 million under grant increase requests for the 16 agreements already signed and approximately \$1.5 million for new agreements pending approval.

Title V Air Permitting Program

Title V of the Clean Air Act requires that each state develop an operating permit program to apply state and federal requirements to stationary air pollution sources and be self-supporting. The Environmental Protection Agency (EPA), which prescribes state program development requirements, granted interim approval for the Commonwealth's Title V program effective March 12, 1998. EPA's interim approval would have expired on June 30, 1999 but EPA has extended the approval to July 1, 2002 because they have not yet presented final guidelines to Virginia. The Department is drafting and issuing permits under Title V and collecting annual fees on emissions to support the program. As of June 30, 1999, the agency had drafted 80 permits. According to the Department, this compares to the Title V permit issuance rate in other states. In fiscal year 1999, Title V revenue and expenses totaled \$9,413,215 and \$7,845,007 respectively. This resulted in a year-end carry forward of \$1,568,208.

The Department maintains Title V program funds separately to ensure that any funds carried over are used to offset future expenses.

Status of the Systems Development Projects

Prompted by its Year 2000 initiatives, the Department has progressed in its system development efforts. The following is a listing of the Department's significant system development projects.

Comprehensive Environmental Data System 2000 (CEDS 2000)

CEDS 2000 will provide database management, permit application and issuance tracking, and permittee compliance for the Department's permitting programs. When fully implemented, the system will run on Oracle and replace approximately 180 systems that run on various platforms. System development has reached the Final Release Development and Design Phase, which consists of three versions. Version 1 included all components essential for Y2K compliance and finished in December 1999. Current efforts focus on Version 2, with scheduled completion in the fall/winter of 2000. The enhancements for Version 2 include electronic submittal of permit applications, discharge monitoring reports, and improvements to the Air Permit Generation System. Version 3 will be Web-enabled and interface with federal and other state systems. The Department plans to complete Version 3 in late 2000 or early 2001. As of March 31, 2000, the Department has spent \$4,316,909 on this project.

Oracle Financials

The Department acquired Oracle Financials to replace its legacy systems. The Department contracted with Pricewaterhousecoopers for implementation support services for six modules: General Ledger, Accounts Payable, Purchasing, Fixed Assets, Accounts Receivable, and Oracle Projects, a time reporting module. The Department also installed the Oracle Human Resources Management System (HRMS) module. The Department is developing a process to fully automate the Oracle financial system's reconciliation to the Commonwealth Accounting and Reporting System (CARS). All modules are operational and the Department expects to fully use the system for financial reporting on July 1, 2000. Total costs for Oracle implementation through March 31, 2000 were \$2,006,630.

DEPARTMENT OF ENVIRONMENTAL QUALITY
Richmond, Virginia

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Director

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