

**OFFICE OF THE ATTORNEY GENERAL
AND
DEPARTMENT OF LAW**

**REPORT ON AUDIT
FOR THE YEAR ENDED
JUNE 30, 2006**



AUDIT SUMMARY

Our audit of the Office of the Attorney General and the Department of Law for the year ended June 30, 2006 found:

- proper recording and reporting of all transactions, in all material respects, in the Commonwealth Accounting and Reporting System; and
- adequate internal controls; and
- two instances of noncompliance with applicable laws and regulations over information technology and small purchase charge card that also require management's attention and corrective action.

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AUDIT FINDINGS AND RECOMMENDATIONS

Complete an Information Security Program

The Office of the Attorney General (Office) does not have a complete or current information security program; therefore, they are not in compliance with Virginia's Information Technology security standard, ITRM Standard SEC 2001-01.1. Although the Office does have procedures in place, these procedures are not in writing; therefore, the plan's documentation requires completion. The Office should have a security program that includes policies and procedures to provide reasonable assurance that appropriate levels of confidentiality, integrity, and availability exist over data in their possession. In addition, the Commonwealth of Virginia (Commonwealth) recently issued a more comprehensive standard, ITRM Standard SEC 501-01, which will supersede SEC 2001-01.1 on July 1, 2007. The Information Technology Security Standard 501-01 provides that a well developed security program should include documented policies and procedures consisting of the following components:

- Information Security Responsibilities and Separation of duties
- Information Security Officer Role
- Risk Management
- IT Contingency Planning
- It Systems Security
- Logical Access Control
- Data Protection
- Facilities Security
- Personnel Security
- Threat Management
- IT Asset Management

A comprehensive information security program provides the essential framework to protect the data on information systems and the data handled by employees. The lack of a comprehensive information security program prevents the Office's management from assessing the current or potential risks to their data, and enabling them to adequately prevent or minimize those risks. The Office should allocate the time and resources necessary to complete a comprehensive information security program that will meet industry best practices.

Strengthen Controls over Small Purchase Card Program

Internal control practices surrounding purchase cards normally require written policies and procedures that set out supervisory oversight, purchasing limits, and other criteria, which the Office has not documented and distributed to all users, cardholders, and supervisors. In addition, an individual has a purchase charge card, but is not a designated authorized cardholder, and certain of this individual's job duties appear inconsistent with someone who should be a cardholder. Internal control practices recommend that the holder and user a of purchasing card be the person whose name appears on the face of the card; and that individuals should not loan the card to others, or have both authorization and purchase authority. Internal control and Commonwealth practices recommend that agencies have written policies and procedures outlining the supervisory oversight, cardholder duties and responsibilities, recordkeeping requirements, purchasing limitations and restrictions, and actions that management will take if individuals do not comply with the policies and procedures.

The Office should develop and implement policies and procedures that address the internal control practices discussed above, and may wish to model those practices on the information in the State Comptroller's Commonwealth Accounting Policies and Procedures Manual. The Office should also review the duties and responsibilities of individual cardholders to ensure an adequate separation of duties.

AGENCY HIGHLIGHTS

The Attorney General is the chief executive officer of the Commonwealth of Virginia's Department of Law. A new Attorney General took office effective January 14, 2006. The Attorney General and staff represent the interest of the Commonwealth in all civil cases naming the Commonwealth, or any of its agencies or officials as a party, and in criminal cases on appeal to the Court of Appeals of Virginia and the Supreme Court of Virginia. In cases involving federal law, the Attorney General represents the Commonwealth's interests in federal court. The Department of Law also enforces consumer protection laws and investigates Medicaid fraud.

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

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

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

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

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

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

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

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

Attorney General's Office

The Office receives most of its funding from General Fund appropriations, but also collects some special revenue and federal funds. The special revenue funds include collections from agencies and universities for legal services provided by the Office, while the federal funds are primarily grants supporting Medicaid fraud control activities and programs to fight domestic violence and violent teen gangs. The following schedule compares the Office's original and adjusted budgets by program with actual expenses for fiscal year 2006.

2006 Budgeted and Actual Expenses

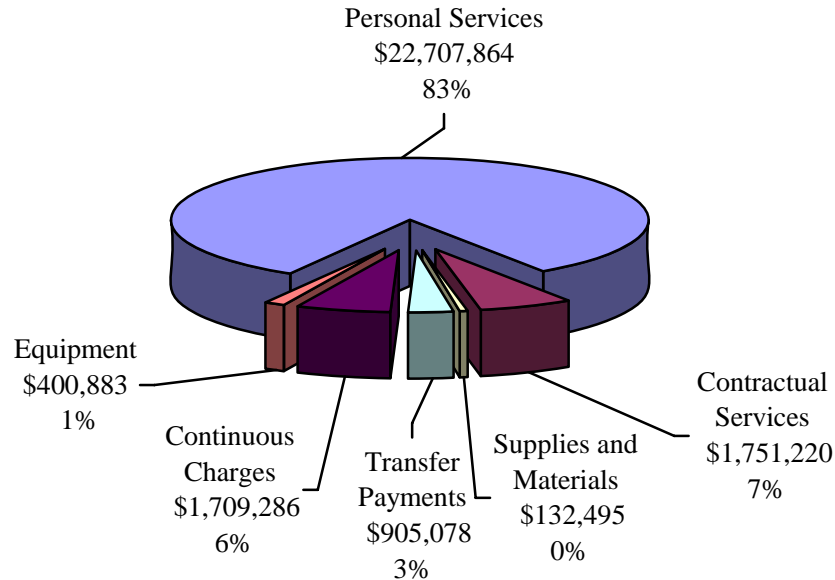
<u>Program</u>	<u>Original Budget</u>	<u>Final Budget</u>	<u>Expenses</u>
Legal advice	\$19,954,342	\$23,870,167	\$22,608,006
Medical assistance services	3,895,890	3,635,912	3,219,507
Regulation of business practices	<u>2,038,429</u>	<u>2,367,076</u>	<u>1,779,316</u>
Total	<u>\$25,888,661</u>	<u>\$29,873,155</u>	<u>\$27,606,829</u>

Overall, the Office's budget increased during the year by almost \$4 million, most of which occurred in the Legal Advice program. The change in this program was primarily due to increases for additional federal funds that were not included in the original budget. In addition, the Office received a budget increase at the end of the year of almost \$1 million for an additional payroll as a result of a statewide change to move one payroll period from fiscal year 2007 to fiscal year 2006.

The Office also collects and deposits directly into the General Fund of the Commonwealth proceeds from fines, forfeitures, court awards, and settlements. In 2006, these funds totaled approximately \$317,000, of which, over 75 percent was the result of a multi-state antitrust settlement. These funds are not included in the above table because they are not available to the Office to fund its operations.

The Office's payroll expenses of \$22,707,864 account for over 82 percent of total expenses. The Office employs 280 full-time and ten part-time employees. The following chart shows fiscal year 2006 expenses broken down by type.

2006 Expenses by Type



Medicaid Fraud Control Unit

The Virginia Medicaid Fraud Control Unit (MFCU), a unit within the Public Safety & Enforcement Division, investigates and prosecutes insurance fraud against the federally funded Medicaid program. The Virginia MFCU consists of criminal investigators, auditors and several Assistant Attorneys General with experience in commercial and financial investigations and has existed since 1982. The Virginia MFCU works with all federal and state law enforcement agencies, as well as private insurance companies operating within Virginia.

In fiscal year 2000, the Virginia MFCU re-organized its operations in order to better fight fraud by networking with various state and federal agencies. This initiative increased the investigative team from eight MFCU investigators to a multi-jurisdictional investigative force of approximately 25 investigators. As a result of successful prosecutions of criminal and civil cases, Virginia can realize financial recoveries, including cash settlements and asset forfeiture. The table below shows the total amount of MFCU recoveries as ordered by the courts (fines, penalties, or restitutions). Because the Virginia Medicaid program is 50 percent federally-funded and 50 percent state-funded, Virginia receives only half of the recoveries. All recoveries go into the Virginia Health Care Fund established by the General Assembly in 2004 and must support health care services. The total amount of Virginia MFCU recoveries deposited into the Virginia Health Care Fund in fiscal year 2006 was \$3,223,827.

<u>Fiscal Year</u>	<u>Total Recoveries</u>
2000	\$ 1,480,345
2001	37,612
2002	12,081,532
2003	11,848,871
2004	14,358,790
2005	10,578,111
2006	9,071,737

Source: Medicaid Fraud Case Tracking System

Division of Debt Collection

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

The 2004 General Assembly passed legislation requiring agencies to forward past due accounts over \$3,000 and 60 days old to the Division. This legislation also mandated the following allocation of collections: 30 percent to the state agency or institution, 30 percent to the Division to fund operations, and 40 percent to the General Fund of the Commonwealth. The Secretary of Finance can grant exception to this allocation for some agencies and universities. Over the last several years, the Division has received budget and staffing level increases in an effort to increase collections and keep up with the growing caseload. The following table shows selected operating statistics for the last five years for the Division.

Operating Statistics 2002-2006

	<u>2002</u>	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>
Employment level approved by the General Assembly	15	17	21	23	23
Division budget approved by the General Assembly	\$953,457	\$1,126,706	\$1,361,076	\$1,516,385	\$1,578,689
Number of accounts	6,207	6,322	8,312	11,140	9,689
Dollar value of accounts	\$87 million	\$91 million	\$100 million	\$159 million	\$157 million
Gross collections	\$11 million	\$13 million	\$13 million	\$10 million	\$12.5 million
Amount returned to the General Fund	\$ -	\$ -	\$1.5 million	\$1.4 million	\$1.1 million

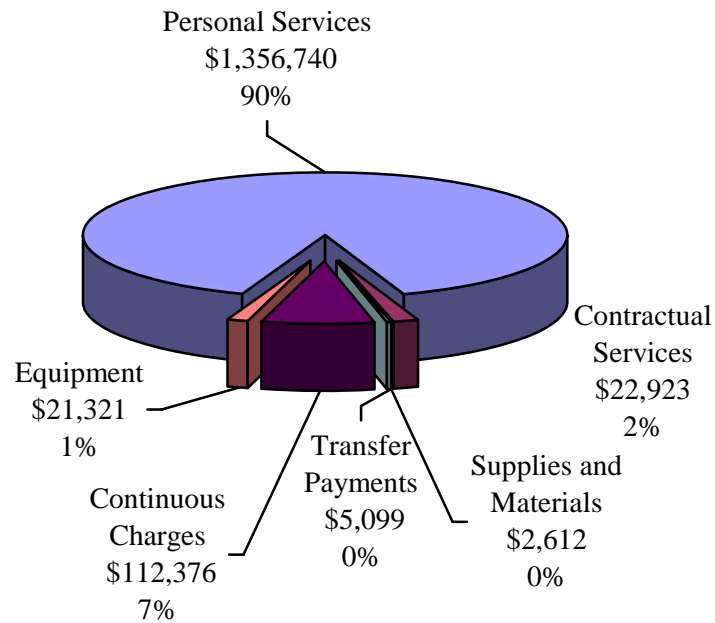
Source: Commonwealth Accounting and Reporting System and the Division of Debt Collection

The Division funds operations with a portion of fees retained from their collections. Currently, the Appropriation Act allows the Division to retain 30 percent of collections, not to exceed \$1.8 million in any fiscal year. Over the last several years, the Division has retained fees in excess of their operating expenses, resulting in an accumulated cash balance in their operating fund that totals \$2.7 million. This amount equates to almost two year's worth of operating expenses. We discussed this issue in our prior year's report and subsequently the General Assembly amended the Appropriation Act to address cash balance in this fund. The following table details the Division's operating revenues and expenses for the last five fiscal years.

	<u>2002</u>	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>
Beginning balance	\$ 604,984	\$ 876,937	\$1,352,947	\$2,278,366	\$2,689,193
Collection fee revenue	1,322,606	1,579,304	1,964,690	1,705,269	1,555,866
Expenses	(1,050,653)	(1,056,470)	(1,024,534)	(1,285,932)	(1,521,073)
Transfers	-	(46,824)	(14,737)	(8,510)	(8,668)
Ending balance	<u>\$ 876,937</u>	<u>\$1,352,947</u>	<u>\$2,278,366</u>	<u>\$2,689,193</u>	<u>\$2,715,317</u>

The major operating expense for the Division is personal services, which make up over 89 percent of total expenses, as shown in the following chart. The following table and chart show 2005 funding and expense information.

2006 Expenses by Type





Commonwealth of Virginia

Walter J. Kucharski, Auditor

**Auditor of Public Accounts
P.O. Box 1295
Richmond, Virginia 23218**

September 25, 2006

The Honorable Timothy M. Kaine
Governor of Virginia
State Capitol
Richmond, Virginia

The Honorable Thomas K. Norment, Jr.
Chairman, Joint Legislative Audit
and Review Commission
General Assembly Building
Richmond, Virginia

We have audited the financial records and operations of the **Office of the Attorney General and the Department of Law** for the year ended June 30, 2006. We conducted our audit in accordance with Government Auditing Standards, issued by the Comptroller General of the United States.

Audit Objectives

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

Audit Scope and Methodology

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

We gained an understanding of the overall internal controls, both automated and manual, sufficient to plan the audit. We considered materiality and control risk in determining the nature and extent of our audit procedures. Our review encompassed controls over the following significant cycles, classes of transactions, and account balances.

- Expenditures
- Payroll Expenditures
- Small Purchase Charge Card
- Revenue Collections and Distributions
- Appropriations
- General Controls over Information Systems

We performed audit tests to determine whether the Office's controls were adequate, had been placed in operation, and were being followed. Our audit also included tests of compliance with provisions of applicable laws and regulations. Our audit procedures included inquiries of appropriate personnel and observation of the Office's operations. We inspected documents including vouchers, reconciliations, timesheets, deposit certificates, and fraud case files. We reviewed the applicable sections of the Code of Virginia and the 2006 Virginia Acts of Assembly. We tested transactions and performed analytical procedures, including budgetary and trend analyses.

Conclusions

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

We noted certain matters involving internal control and its operation and compliance with applicable laws and regulations that require management's attention and corrective action. These matters are described in the section entitled "Audit Findings and Recommendations."

The Office has taken adequate corrective action with respect to audit findings reported in the prior year that are not repeated in this letter.

EXIT CONFERENCE AND REPORT DISTRIBUTION

We discussed this report with management on October 25, 2006. Management's response has been included at the end of this report.

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

AUDITOR OF PUBLIC ACCOUNTS

LCW:sks
sks: 26



COMMONWEALTH of VIRGINIA

Office of the Attorney General

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November 1, 2006

Mr. Walter Kucharski
Auditor of Public Accounts
101 N. 14th Street
Richmond, VA 23219

Mr. Kucharski,

Thank you for providing the Office of the Attorney General with the opportunity to respond to the recommendations in your recent audit. We were especially pleased that all audit points from last year's audit have been successfully remedied.

Since last year's audit, the Finance Division has undertaken a review of operational processes to streamline workflow and improve internal controls. The Director of Finance continues to stress the importance of proper documentation when recording transactions and continues to educate our staff about the need to ensure compliance with the Commonwealth Accounting Policies and Procedures Manual and the Commonwealth's procurement laws and policies.

As you also will recall, the Office recently extended a hiring offer to a new CIO who will start work on November 1, 2006. This individual will play a pivotal role in developing a more stringent systems security assessment for the office. The OAG recognizes the importance of strong control measures and has aggressively started a program to achieve compliance with the new ITRM Standard SEC 501-01 when it takes effect on July 1, 2007. This will include the appointment of a Chief Security Officer.

While the OAG meets the internal control standards governing the financial operations of the office, we will continue to look for the most cost-effective methods to ensure the proper level of controls.

The Attorney General is appreciative of the Auditor of Public Accounts bringing these matters to our attention. We fully intend to take the actions necessary to improve each area mentioned.

Sincerely,

A handwritten signature in black ink that reads "Janet Polarek".
Janet Polarek
Director of Administration

OFFICE OF THE ATTORNEY GENERAL

As of June 30, 2006

Robert F. McDonnell
Attorney General

William C. Mims
Chief Deputy Attorney General

Janet Polarek
Director of Administration

Thomas A. Gelozin
Director of Finance