



Office of Budget and Management Operating Budget Process Audit

Audit Period: July 2017 through June 2018

Results Summary:

Objective	Conclusion
Monitoring the GRF Budget to Avoid a Deficit Position	Well-Controlled with Improvement Needed

* Refer to Appendix A for classification of audit objective conclusions.



Executive Summary

Background

The OBM Budget Planning section monitors the General Revenue Fund (GRF) budget through the GRF framework to avoid deficit positions. Cash balance monitoring includes daily and monthly activities to ensure that a negative cash balance of the GRF does not exceed ten percent of the total revenue of the GRF in the preceding fiscal year to comply with statutory requirements. End of year cash balance monitoring includes daily tracking of the unencumbered GRF balance and estimated outstanding revenues and disbursements to determine the estimated ending unobligated cash balance to ensure it does not exceed 0.5% of the year's GRF revenues, as required by statute. GRF revenues and transfers-in monitoring includes distribution of daily internal reports to compare revenue activity from the previous day and month-to-date and year-to-date revenues against estimates. Monthly and yearly GRF revenue performance is stated in Monthly Financial Reports (MFR). GRF disbursements and transfers-out monitoring includes the Budget Planning section periodically receiving updated disbursement estimates from agencies for Medicaid (from ODM), debt service (from OBM), and property tax disbursements (from OBM) and incorporated into the GRF framework or kept as running lists. The Budget Planning section also re-calculates maximum disbursement amounts throughout the fiscal year. This amount is referred to as the updated control total. Monitoring activities result in updates to the GRF framework throughout the fiscal year to reflect year-to-date performance. During state fiscal year 2018, GRF revenues and transfers-in were \$32,471.3 million and disbursements, transfers out, and encumbrances totaled \$32,178.5 million. The ending unencumbered balance as of June 30, 2018 was \$849.9 million. \$657.5 million was transferred to the Budget Stabilization Fund (BSF) to bring the BSF balance to over \$2.6 billion.

During the audit, OIA identified opportunities for OBM to strengthen internal controls and improve business operations. OIA conforms with the *International Standards for the Professional Practice of Internal Auditing*. OIA would like to thank OBM staff and management for their cooperation and time in support of this audit.

This report is solely intended for the information and use of agency management and the State Audit Committee. It is not intended for anyone other than these specified parties.

Scope and Objectives

OIA staff was engaged to perform an assurance audit related to the controls over the agency's operating budget process. This work was completed September through December 2018. The scope of this audit was GRF budget implementation



The following was the objective of the review: Evaluate the design and effectiveness of processes and controls to monitor the GRF budget to avoid a deficit position.

Audit period: State Fiscal Year 2018.

Detailed Observations and Recommendations

The Observations and Recommendations include only those risks which were deemed high or moderate. There were no low risk observations.

Observation 1 – Lack of Formal Written Policy and Procedures for GRF Monitoring Activities

According to the Ohio Revised Code (ORC) 126.06, the director may establish limits on the negative cash balance of the GRF within the total operating fund, but in no case shall the negative cash balance of the GRF exceed ten percent of the total revenue of the GRF in the preceding fiscal year. ORC 131.44 sets a statutory ending unencumbered GRF cash balance target of 0.5% of a year's GRF revenues.

Formalized GRF monitoring activities with critical and cautionary outlooks is a proactive approach to maintaining and identifying unfavorable performance, negative trends, and potentially recognizing deficits timely to adequately address any issues. Policies and procedures help ensure the actions initiated by management address risks and ensure compliance with laws, rules and regulations. Compliance requirements should be outlined in a policy and the GRF monitoring activities should be outlined in written procedures.

The OBM Budget and Planning Section's GRF monitoring functions include daily, monthly and annual activities. Daily, OBM State Accounting provides the GRF Cash Balance report to OBM Budget and Planning, as well as to the Director for review. Monthly, the planning section documents and the Director approves the month and year-to-date revenue and disbursement performance totals in Tables 1 through 4 of the Governor's Monthly Financial Report. The Tables are the result of monitoring activities throughout the year. At various times throughout the fiscal year, Planning and Budget updates the GRF framework to reflect actual year-to-date performance.

To monitor disbursements, throughout the year, OBM Budget and Planning mostly relies on the agencies to provide status information on current disbursement variances from estimates. Only material variances are reflected in the GRF framework and towards the end of the fiscal year, OBM Budget analysts work with agencies to obtain lapse estimates. Additionally, OBM Planning recalculates maximum disbursement amounts and incorporates the updated control total into the



framework. However, there are no written procedures to ensure a proactive approach and more accurate/timelier update to the framework throughout the year or procedures that outline the frequency required to recalculate maximum disbursements.

Collectively, the controls to monitor the GRF are adequately designed to mitigate risks that the GRF will not maintain and/or have unfavorable performances, possible negative trends, and/or reflect potential financial stress or hardship. However, individually, the controls are not adequately designed to mitigate risks. Specifically, there are no established criteria/thresholds or written policies to ensure adjustments to estimates or completed transfers are appropriately timed and align with the risks. In addition, there is not a policy to outline actions and/or strategies OBM may take to ensure compliance with requirements to achieve strategic goals and favorable performances. Additionally, the specific monitoring activities are not formalized in written procedures to outline roles and responsibilities, timing of activities, information sources, and documentation requirements.

Lack of written policy and procedures may increase the likelihood that monitoring activities may not occur timely or at all or that issues are not detected timely to take needed action to avoid unfavorable performance or noncompliance issues. In addition, without written procedures, there may be interruptions in business processes due to staff turnover and may also result in increased time to train new staff members on GRF monitoring activities.

Recommendation

Develop a policy to set guidelines for GRF monitoring controls to address risks and variance thresholds. Regularly review and update variance thresholds and tolerances to align with changes in the agency's risk appetite.

Develop and implement GRF monitoring procedures to include documenting roles and responsibilities and timelines for completing and documenting each monitoring activity. Consider defining indicators to trigger certain action plans or responses based on critical and cautionary observations over revenues and disbursements detected through the monitoring activities. Include documentation requirements of discussions of material variances with Directors and stakeholders, including their extent, nature, and actions taken to resolve during monthly meetings and/or reviews.

Create policy and procedures to formalize the control total calculation of disbursements and record and maintain records of completed calculations. Formalize the frequency of recalculations of maximum disbursements throughout the year. Include in the calculation actual expenditures, available balance, and allowable percentage before consideration of critical or cautionary action is needed.

Consider creating a deficit resolution policy and procedures that include defining the deficit and the deficit resolution, outlining responsibilities and the budget priorities. Outline appropriate transfers and/or adjustments, what constitutes a transfer or adjustment, who may authorize, and



the situations that require cautionary or critical actions. The procedures should address a budget deficit, identifying potential risks and a plan to mitigate those risks.

Management Response

Before responding to the individual recommendations presented above, we first want to state that our current monitoring activities are thorough and comprehensive. Revenues and key disbursements are monitored on a daily or weekly basis to allow for forecasts of monthly performance and this information is regularly reported to the Director of OBM. Records of our key monitoring activities are maintained and available for our reference when needed. With that being said, we do recognize that some of our monitoring procedures would benefit from additional process documentation.

In response to your first recommendation, we will memorialize, in writing, our current GRF monitoring control practices into a document outlining roles and timelines for completing each activity. While we will regularly review our monitoring practices, variance thresholds or tolerances are not applicable as all variances – regardless of materiality – are tracked and reported to the Director of the Office of Budget and Management.

In response to your second recommendation, we will memorialize, in writing, our current GRF monitoring control practices into a document outlining roles and timelines for completing each activity.

The need to take action as the result of anticipated revenue shortfalls or expense overages is based on situation-specific factors. Since there are so many potential outcomes to a given shortfall or overage event, it would not be appropriate to define indicators which would trigger certain responses and constrain the discretion of the Director of OBM and the Governor. When the Director and Governor determine that action is needed to respond to a situation, these actions are well documented, often through Executive Order or legislation.

In response to your third recommendation, I would first mention that the OAKS Financials system is responsible for tracking and recording appropriations, expenditures, and encumbrances. Regarding the Budget Planning Section's process to calculate a "running" control total, we will memorialize, in writing, our current process. This process already includes use of actual expenditures and available balances, and all records of completed calculations are already maintained. The control total calculation would not appropriately be used to identify whether cautionary action is needed.

In response to your fourth recommendation, we do not feel it would be practical or appropriate to create a deficit resolution policy for two primary reasons. First, as mentioned above, situation-specific factors determine whether action is needed and it would not be practical for a deficit resolution policy to fully account for these factors. Second, were it practical to create a deficit resolution policy, it would still not be appropriate to constrain the discretion of the Director of OBM or the Governor. Instead of a deficit resolution policy, we will develop a document outlining



potential management actions which can be taken by the Director of OBM under existing legal authority to increase transfers in or reduce expenditures or transfers out of the General Revenue Fund.

Risk	Remediation Owner	Estimated Completion Date
Moderate	Budget Planning and Internal Services Section Chief	October 1, 2019



Appendix A – Classification of Conclusions and Observations

Classification of Audit Objective Conclusions

Conclusion	Description of Factors
Well-Controlled	The processes are appropriately designed and/or are operating effectively to manage risks. Control issues may exist, but are minor.
Well-Controlled with Improvement Needed	The processes have design or operating effectiveness deficiencies but do not compromise achievement of important control objectives.
Improvement Needed	Weaknesses are present that compromise achievement of one or more control objectives but do not prevent the process from achieving its overall purpose. While important weaknesses exist, their impact is not widespread.
Major Improvement Needed	Weaknesses are present that could potentially compromise achievement of its overall purpose. The impact of weaknesses on management of risks is widespread due to the number or nature of the weaknesses.

Classification of Audit Observations

Rating	Description of Factors	Reporting Level
Low	Observation poses relatively minor exposure to an agency under review. Represents a process improvement opportunity.	Agency Management; State Audit Committee (Not reported)
Moderate	Observation has moderate impact to the agency. Exposure may be significant to unit within an agency, but not to the agency as a whole. Compensating controls may exist but are not operating as designed. Requires near-term agency attention.	Agency Management and State Audit Committee
High	Observation has broad (state or agency wide) impact and possible or existing material exposure requiring immediate agency attention and remediation.	Agency Management and State Audit Committee