



Applying Risk Management and Avoiding Risk Assessment Deficiencies

Divon Crutchfield, CPA
January 25, 2017

Introduction

- My Background
- Objectives:
 - To explain how we can all use risk management to help us achieve our objectives
 - To provide a brief overview of the Financial Integrity Act
 - To provide an introduction to the Department of Finance and Administration's new guidance and tools



Introduction

- Objectives (cont.):
 - To help risk assessment preparers improve the usefulness of assessments by
 - Sharing some common deficiencies we've identified in assessments over the years
 - Discussing some techniques that could help improve the quality of assessments

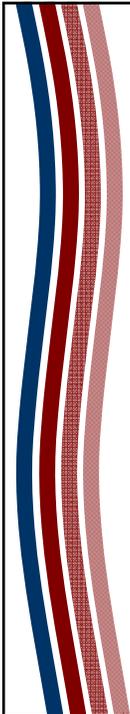


How Is Risk Management Relevant To You?

AKA . . .

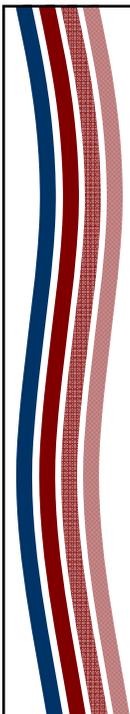
Why should I care about this?





Why should you care?

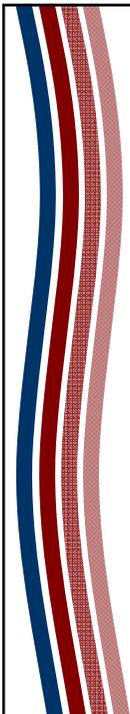
Anyone that cares about achieving objectives should care about risk management



Whose Objectives?

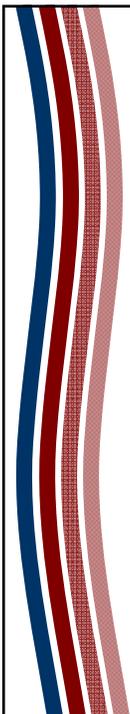
1. Your organization's,
2. Your division's,
3. Your unit's / team's,
4. Your own objectives in the workplace,
5. Your personal objectives outside work.





Why Should You Care?

We all have objectives, and Risk Management is simply a set of strategies for helping people achieve those objectives

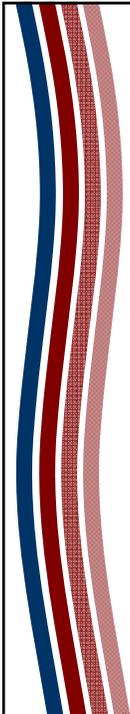


Applying Risk Management Every Day

5 steps in any context:

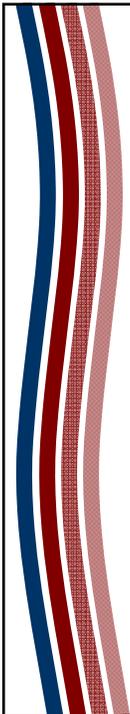
- What are your objectives?
- What are the risks related to those?
- How will you address those risks?
- How will you get information about your progress?
- How will you monitor your progress?





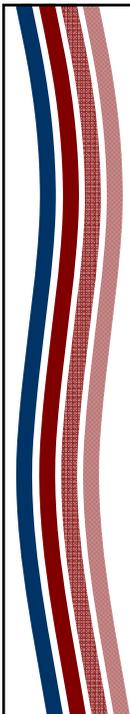
Applying this to common situations

- Waking up on time
- Managing entertainment / social media
- Preparing financial statements
- Complying with program requirements



A Brief Overview of the Financial Integrity Act

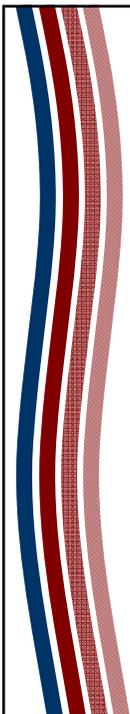




Sections 9-18-101 through 9-18-104, *Tennessee Code Annotated*

Each agency of state government and institution of higher education along with each county, municipal, and metropolitan government shall establish and maintain internal controls, which shall provide reasonable assurance that:

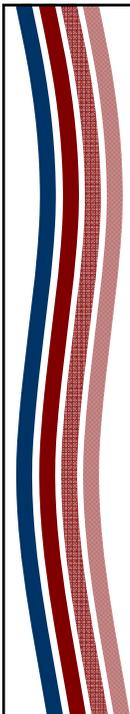
- Obligations and costs are in compliance with applicable law,
- Assets are safeguarded, and
- Revenues and expenditures are properly recorded and accounted for



Sections 9-18-101 through 9-18-104, *Tennessee Code Annotated*

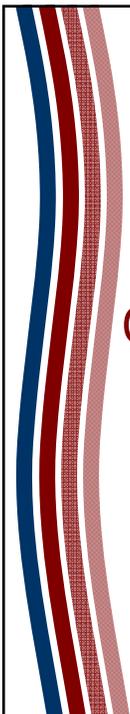
- To document compliance with these requirements, each agency of state government and institution of higher education shall annually perform a management assessment of risk;
- The objectives of the annual risk assessment include providing reasonable assurance of accountability for meeting program objectives and promoting operational efficiency and effectiveness.
- The commissioner of finance and administration (F&A), in consultation with the comptroller of the treasury, shall establish guidelines for the assessment of the risks and systems of internal control to determine compliance with these requirements





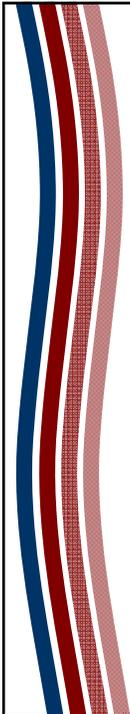
Sections 9-18-101 through 9-18-104, *Tennessee Code Annotated*

- Each year, the head of each state agency and higher education institution is required to file an annual assurances report based on the evaluations of risks and internal controls performed in accordance with F&A's guidelines.
- Includes a statement of assurance representing the agency head's informed judgement as to the overall adequacy and effectiveness of internal controls



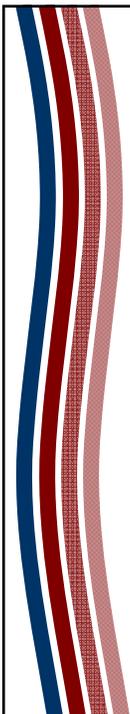
Introduction to F&A's New Guidance and Optional Toolsets





New Guidance and Optional Toolset

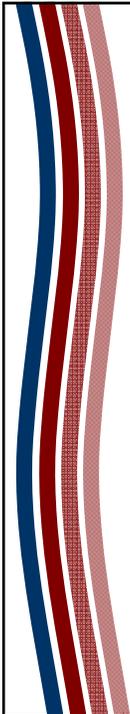
1. Available online at <https://www.tn.gov/finance/article/fa-accfin-risk-management>
2. Guidance itself is only 7 pages
3. Also issued a host of optional tools and instructions for completing those tools



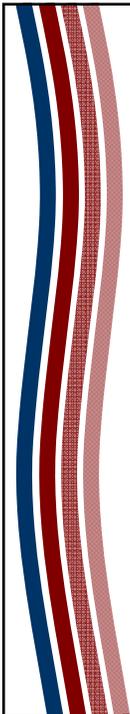
New Guidance and Optional Toolset

1. Guidance
 - a) More flexible – includes fewer requirements.
 - b) Does incorporate the Green Book's documentation requirements
2. Optional Tools
 - a) No standard risks identified
 - b) Enhancements in the design of the templates
 - c) Very helpful set of instructions





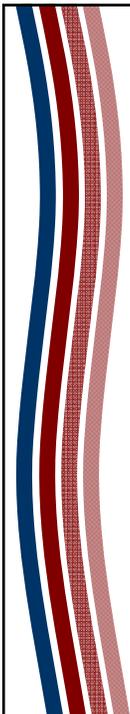
Avoiding Common Risk Assessment Deficiencies



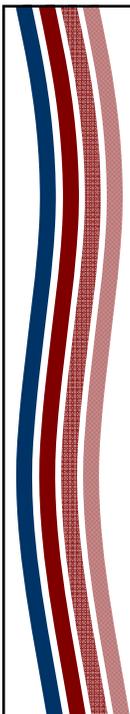
Primary Areas of Concern

1. Lack of agency-specific risks and business unit / division-specific risks
2. Understating the impact of risks and likelihood of occurrence
3. Concluding that controls are operating effectively without testing them
4. Completing the risk assessment forms incorrectly





Lack of agency-specific risks and business unit / division- specific risks

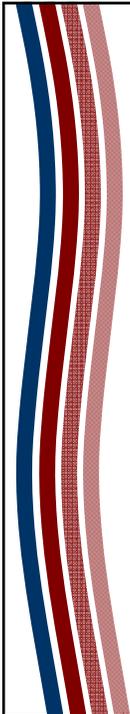


Lack of Agency, Business Unit / Division – Specific Risks

Assessments I reviewed fell into three categories:

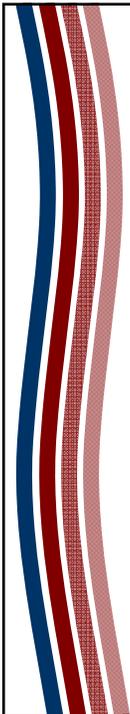
- About 1/3 included only standard risks in the template without identifying any agency-specific risks.
- About 1/3 identified at least one agency-specific risk, but only had a handful of agency-specific risks overall.
- About 1/3 identified numerous agency-specific risks.





Lack of Agency, Business Unit / Division – Specific Risks

- Templates were designed for agencies to add their own unique risks
- Virtually no way that standard template could adequately address the needs of numerous agencies
- Each agency probably has numerous agency-specific risks to consider; it is unlikely that none are significant

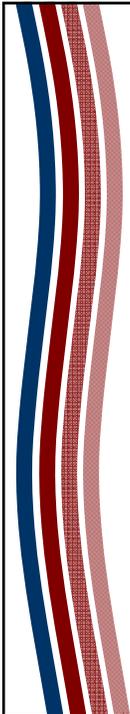


Potential Solutions

Provide specific brainstorming techniques to preparers of assessments. Consider reviewing

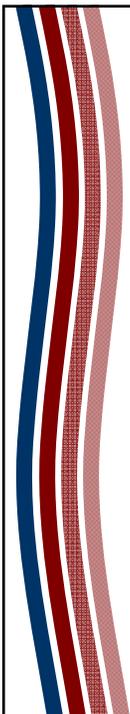
- Existing state statutes
- Recently issued state and federal legislation, regulatory provisions, accounting standards
- Your agency's / business unit's primary objectives and activities
- Recent audit findings / monitoring reports for your agency / business unit
- Recent audit findings / monitoring reports for counterparts in other states





Potential Solutions

Specific brainstorming techniques could be documented in instructions in Excel spreadsheets used to prepare the assessment or in other written instructions provided to preparers.

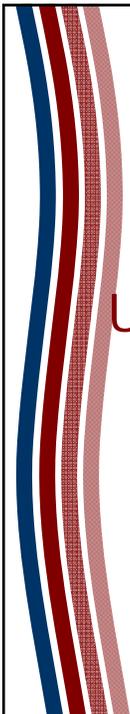


Potential Solutions

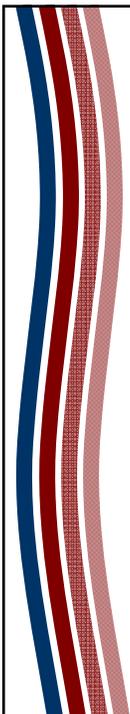
Inform preparers that higher scrutiny will be placed on division-specific or agency-wide assessments that have no unique risks.

- Presumption that an assessment with no unique risks is generally inadequate
- If the assessment has none, ask them to continue brainstorming





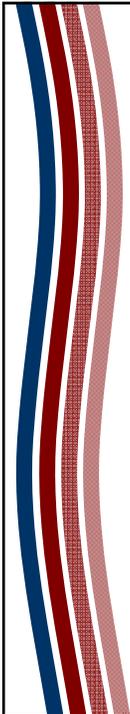
Understating the impact of risks and likelihood of occurrence



Understating the impact of risks and likelihood of occurrence

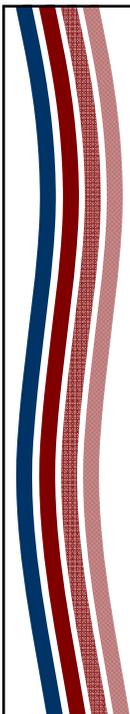
- Impact often assessed as low
- Presumption that risks related to federal compliance requirements should likely be assessed at a higher level if the unit completing the assessment is primarily federally funded





Understating the impact of risks and likelihood of occurrence

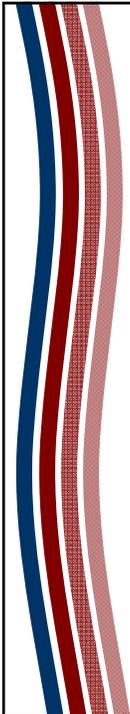
- Likelihood often assessed as low
- Not clear that preparers are assessing likelihood based on inherent risk instead of residual risk



Understating the impact of risks and likelihood of occurrence

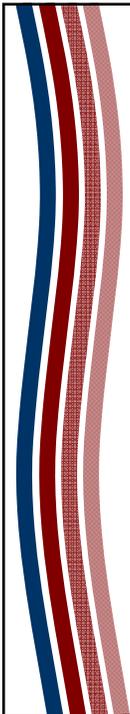
- Inherent risk is risk absent any management activity or controls to prevent an event from happening
- Residual risk is risk that remains after management's response to the risk





Understating the impact of risks and likelihood of occurrence

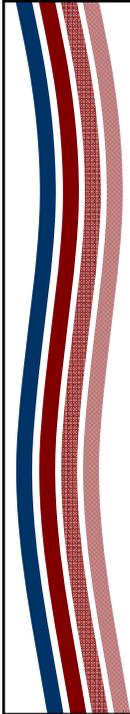
- Examples for each section of the template where likelihood should likely be assessed higher
 - Strategic, Operational, and Reporting (Revenue records vs. amounts received)
 - Compliance (Allowable Costs/Cost Principles)
 - Fraud (Petty Cash)



Potential Solutions

- Add a column to the right of the control operating effectively column that clearly is for assessing residual risk.*
- Add an “Inherent risk” label for likelihood and impact*
- Remind preparers that inherent risk assessment is based on assuming that no controls are in place





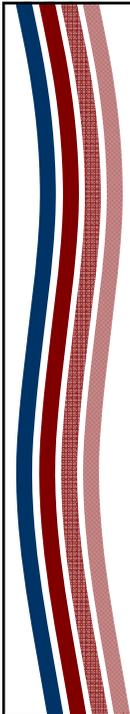
Concluding that controls
are operating effectively
without testing them



Not Testing Controls

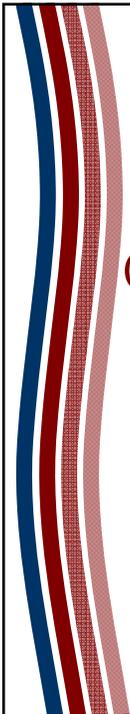
- Some managers are assuming that controls are operating effectively without testing* the controls
- The guide states documentation should meet documentation requirements in OV4.08 of the Green Book
- “Management evaluates and documents the results of ongoing monitoring and separate evaluations to identify internal control issues.”





Potential Solutions

- Inform assessment preparers of requirements in written instructions
- Assist them in brainstorming how to document ongoing evaluations, perform tests, and how to document those tests
- Consider requesting the documentation and completing a cursory review to ensure the evaluation of the control is supported



Completing the risk assessment forms incorrectly



Completing the risk assessment forms incorrectly

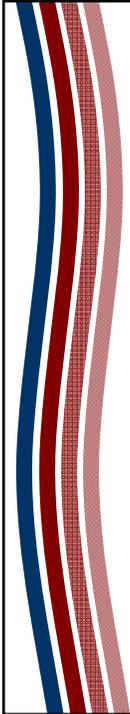
- Controls documented as operating effectively, but no control identified in the Control Activities column
- Control activities not identified when impact and likelihood are other than low*
- Risk assessment instructions not followed due to other issues



Potential Solutions

- Develop Excel spreadsheet template with built-in controls that flag preparers (for example, highlights the cell yellow) if any of these issues are present.
- In written instructions, ask preparers to enter explanations for any remaining flags, and follow-up with preparers about any unexplained flags.





Thank You

My Contact Information:

- Divon.Crutchfield@cot.tn.gov
- 615-747-5239

