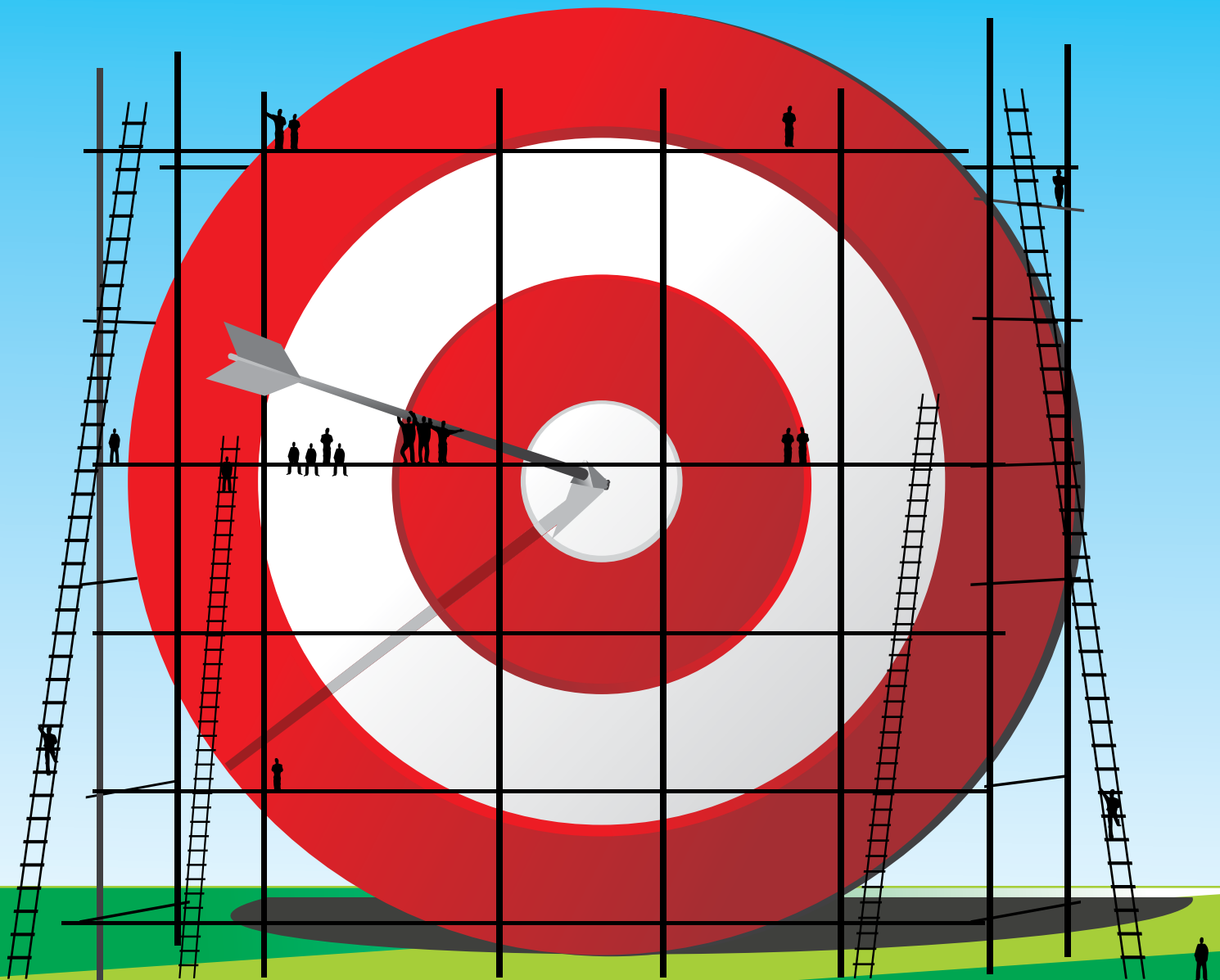


RISK MANAGEMENT:

By: Clifton A. Williams, CGFM, CPA

Highlights of the 2011 CFO Survey



Risk Management in the 2011 Government Chief Financial Officer Surveys

Risk management was an important topic in several spring 2011 surveys of government financial professionals. AGA sponsored an in-person survey of federal chief financial officers (CFOs) and other financial executives (152 respondents) and an online survey of its federal, state and local government members (1,157 respondents, see *Figure 1* for a breakdown by government level). At the same time, AGA and the National Association of State Auditors, Comptrollers and Treasurers (NASACT) conducted a separate online survey of a targeted group of state financial executives (40 respondents from 28 states). Grant Thornton LLP funded and carried out all surveys. We report on the risk management portion of the surveys here.

Note: Throughout this article, “executive” refers to a respondent to the federal and state executive level surveys while “manager” refers to a respondent of the online survey of AGA members.

Assessing Government and Risk Management

Whether a government entity makes benefit payments, issues bonds, manages reserves or fights wars, it faces and must manage risk. Financial management leaders are intimately involved in managing many financial risks, but are usually absent from the operations or mission risk arenas. This is unfortunate because operations risks tend to cause financial problems and vice versa. In addition, financial professionals have risk assessment and management skills that operations professionals need.

Figure 2 shows that most respondents at all levels of government think their organizations are doing an adequate job of managing risk for the entities’ top three or four goals.

Some comments from the Yes, Mixed and No answer categories in *Figure 2* include:

Yes: “Strategic planning using the balanced scorecard method, emergency business plan and business continuity plans are in place and actively reviewed,” says a manager. According to an executive, “We implemented a living strategic plan that is updated based on changes to or new risks identified through our ongoing operations.”

Mixed: “Borderline. There is standard segregation of duties across the state to manage risk, but broader risk management is up to individual agencies within their operating budgets,” says a manager. Another says, “Risk management is important and I would rate it in our top 10 concerns, so as director of finance, I keep it on the back burner with town management.”

No: “No, goals are set but risks are not always managed,” says a manager. “Intergovernmental dependency and revenue fluctuation responses are not adequately managed. We have limited input into those risk areas,” says an executive. “I am one of two CPAs working in a local school district and top management is not interested in risk management,” says another manager.

Role of Financial Executives and Managers in Risk Management

Reviewing all responses from all levels of government, we get the sense that most financial executives and managers confine themselves to the financial aspects of risk assessment and management. Some, however, do play an active role in managing nonfinancial risks to mission and their entities. When asked what role their financial management offices play in assessing and managing risks for the three or four top goal areas in their entities, executives and managers reported the following activities:

- Carry out internal audits and activities related to them.
- Develop, plan, update and enforce internal controls.
- Act as an information source and adviser on risk management and internal control.
- Document and review completion of risk management and internal control tasks by their own and other government entities; this includes reviewing other risk assessments.

FIGURE 1: GOVERNMENT AFFILIATION OF AGA MEMBERS RESPONDING TO 2011 ONLINE SURVEY

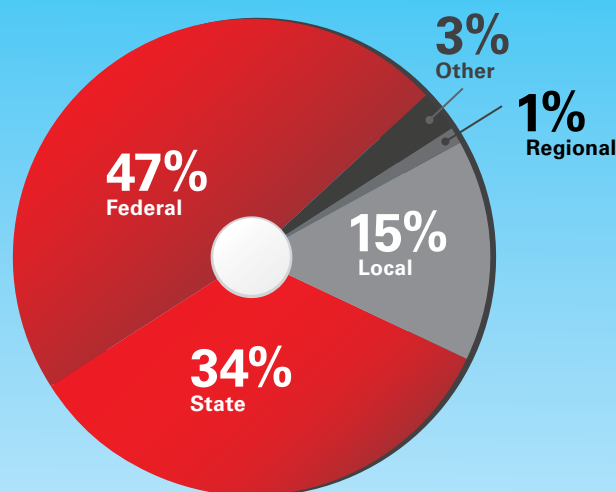


FIGURE 2: SURVEY RESPONDENTS’ OPINIONS OF THE ADEQUACY OF RISK MANAGEMENT FOR THEIR ORGANIZATIONS’ TOP THREE OR FOUR GOALS

Survey respondents	Yes	Mixed	No	Don’t know
Federal executives	50%	16%	28%	6%
Federal managers	68%	6%	18%	7%
State executives	71%	4%	25%	0%
State managers	67%	3%	16%	14%
Local managers ¹	59%	3%	31%	6%

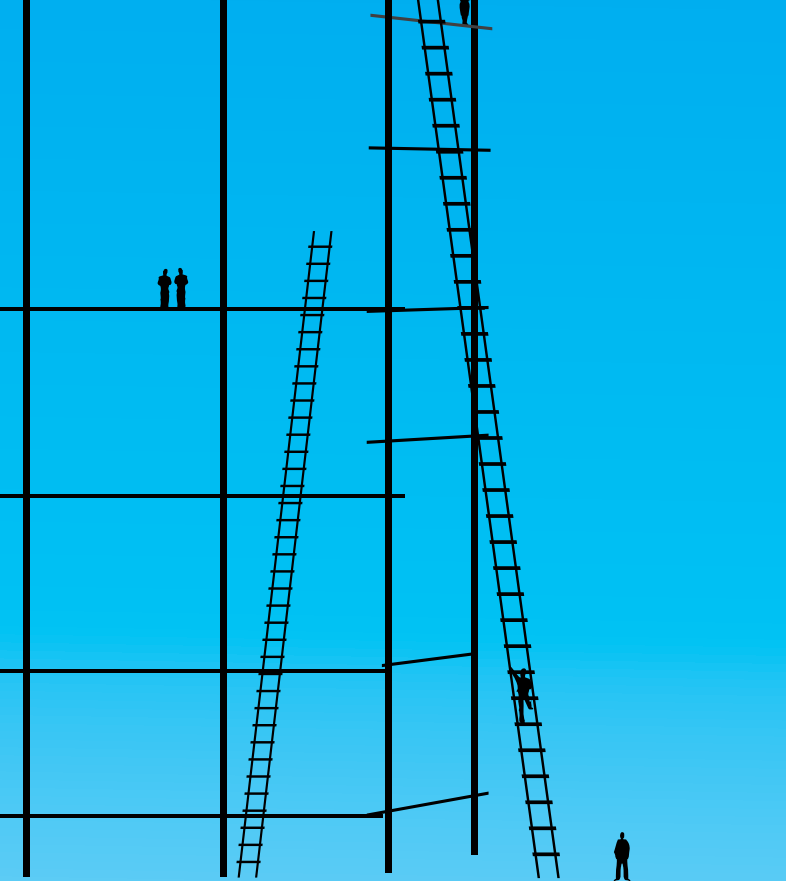


FIGURE 3: RESPONDENTS' SATISFACTION WITH INTEGRATION OF RISK MANAGEMENT WITH INTERNAL CONTROLS

Government level	Mean satisfaction score on 1 to 5 scale*
Federal executives	3.1
Federal managers	3.5
State executives	3.5
State managers	3.6
Local managers	3.5

*1 = very dissatisfied, 5 = very satisfied

FIGURE 4: EXECUTIVES' SATISFACTION WITH THEIR FINANCIAL STAFF'S RISK MANAGEMENT SKILLS

Government level	Mean satisfaction score on 1 to 5 scale*
Federal	2.7
State	4.0

*1 = very dissatisfied, 5 = very satisfied

FIGURE 5: MANAGERS' OPINION ON WHETHER THEY ARE SATISFIED WITH THEIR SKILLS IN RISK MANAGEMENT TRAINING

Government level	Satisfied with skills and training		
	Yes	No	Do not know
Federal	59%	22%	19%
State	62%	16%	22%
Local	60%	21%	19%

- Coordinate agencies' reviews of risk management relative to objectives in strategic plans, which may lead to changes to the plans and their related activities.
- (For auditors) Consider risks that affect financial audits and recommend improvements to relevant risk assessment activities.
- Provide input through budget reviews and audits.

Integration of Internal Controls and Risk Management

An entity's internal control activities should be integrated in its enterprise risk management (ERM)² activities, but this is not always the case. Risk mitigation strategies on the program or operations side of an entity are rarely informed by the internal control work done on the financial side. This may reflect the siloed nature of many public sector organizations or simply a lack of understanding that financial and nonfinancial risks go together.

For example, of executives who commented on the topic, most said their primary contribution to ERM is through internal controls over financial transactions. We asked respondents how satisfied they were with how their entity integrates risk management in general with its internal controls. *Figure 3* shows passing grades, but nothing stellar.

Here are comments from the respondents for the different scoring levels shown in *Figure 3*:

Level 1. "The entity has not implemented an ongoing risk management process," says one manager. Says another, "Management is not concerned with internal controls or lack of staffing. We are woefully understaffed, so many areas just are not monitored properly."

Level 2. "There is a disconnect between risks and controls; controls are often thought of in a traditional way," says a manager. "We have a very difficult time convincing program managers that internal controls are as much or more their responsibility as they are of the state- and department-level controllers," says an executive. "Only financial controls are assessed. And though attempts are made to perform entity-wide controls and risk assessments, they are not prepared and used properly."

Level 3. "We usually establish internal controls reactively, not proactively," says a manager. According to an executive, "We are a combination of a centralized accounting system with decentralized agencies. Many of the internal controls are built into the accounting system but may be subject to agency override because of the decentralized structure. With the changes in audit standards, the legislative auditor's office no longer performs much of an internal audit function and there has been little support for adding internal auditors to fill this gap."

Level 4. "Internal controls are assessed within the risk management process," says a manager. "We have good coordination between the state auditor and the state accounting officer," says an executive.

Level 5. "We have a comprehensive internal control policy as well as a policy for those outside of our agency using services we provide," says a manager. Says an executive, "We passed an act that requires an entity-wide risk management approach similar to COSO 1 and 2. This is an entity-wide and activity/program risk assessment process

and includes annual self-assessment. We start looking at our strategic plan's mission, goals and objectives. We then identify risks by magnitude and likelihood that they could prevent us from achieving goals and objectives. For those risks that cannot be prevented, we identify and implement internal controls to mitigate them."

Training for Risk Assessment

We asked federal and state executives to rate their satisfaction with their financial staffs' training in risk assessment on a scale of one to five. We also asked the staffs whether they thought they had the proper skills.

On average, federal executives give their financial staffs a low score on having the skills needed to apply risk management methods, while state financial executives give their staffs a relatively high score. However, the state scores may be somewhat higher because a higher percentage of auditors responded.

Although a majority of managers in this survey are satisfied with their risk management skills and training, we should take into account that they are AGA members and thus more likely to be better educated than nonmembers who are government accounting and financial management professionals. Here are some comments from the managers on skills and training:

"Professional training and certifications are part of the risk management program on a continuing basis as long as funds are available."

"My training and educational background and experience give me adequate ability in this area. However, risk management is an evolving area that will always require a financial career to continue and maintain education and training to stay abreast."

"I would like to have more tools for assessing the risk assessments themselves so that they are more meaningful and easy to understand."

Many executives in the survey are dissatisfied with the risk management training of nonfinancial managers. Says one executive, "My state's career development programs for executives and managers do not include risk management. Further, risk management is not [considered] a core competency for these leadership positions." Several managers noted the importance of having nonfinancial managers take risk assessment training; this includes training offered in connection with obtaining the Project Management Professional (PMP) certification.

How Financial Management Professionals Can Play a Greater Role in ERM

Says an executive, "The role of the CFO is keeping risks at the forefront of discussions in administrative, information technology, capital investment, human capital and other related issues." For CFOs or other financial executives, perhaps the best place to start or get on board a balanced ERM initiative is within their office.

Says an executive, "The first circle has to be close to home—it should be the basic CFO responsibilities, fundamentals like internal control over basic accounting. Deal with things inside your shop first, and then go outside. Next, look for where your entity is hemorrhaging money or having other problems that could be mitigated by financial management approaches, skills and tools."



Financial professionals have good entry points to non-financial risk management, say many respondents. These include anything having to do with internal controls, financial audits, budgets and strategic plans, which touch virtually every activity in an entity. Financial executives and managers have legitimate reasons to sit on risk management committees because they understand financial risk, but once on such teams they should not confine themselves to fiscal matters.

One thing is for sure: Governments are going to be paying much more attention to risk management in the future. This is an opportunity for the financial professional who takes an active role in ERM, especially in helping integrate internal controls and other risk management activities. ■

End Notes

1. We did not do a separate survey of local government executives.
2. Enterprise risk management: "A process, effected by an entity's board of directors, management and other personnel, applied in strategy setting and across the enterprise, designed to identify potential events that may affect the entity, and manage risk to be within its risk appetite, to provide reasonable assurance regarding the achievement of entity objectives." —Committee of Sponsoring Organizations of the Treadway Commission (COSO), "Executive Summary," *Enterprise Risk Management—Integrated Framework*, September 2004, p. 2.



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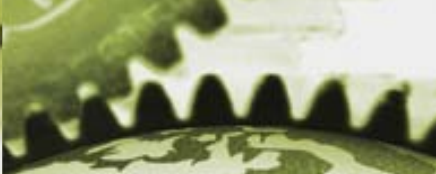
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Don't Delay—The Time Has Come to Use the Full Potential of Enterprise Risk Management to Reduce Costs and Enhance Program Delivery



By: Jeffrey C. Steinhoff, CGFM, CPA, CFE, and Geoffrey L. Weber, MBA, CISA, CISM

All levels of government are grappling with budget constraints and long-term fiscal paths that are widely recognized to be unsustainable. Governments are challenged to be more effective to meet the expectations of the public while addressing stark fiscal realities. Finding ways of doing more with less is of utmost importance.



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Enhancing Transparency and Reducing Risk by Means of Accounting Standards at the Federal Reserve



By: Charles F. Beauchamp, Ph.D., and William F. Ford, Ph.D.

The Federal Reserve's financial crisis response initiatives added major credit and interest rate risks to its balance sheet. Replacing its traditional non-GAAP accounting protocol with GAAP standards would further enhance the transparency of those risks. In doing so, the Fed would reduce its greatest risk, which is reputational risk.

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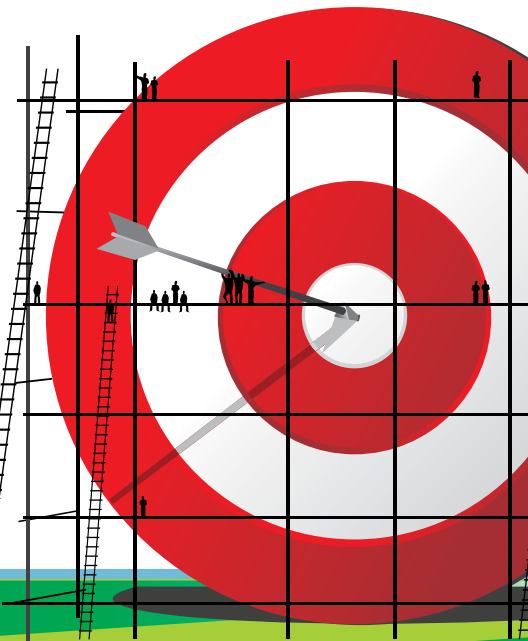
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Much of government exists to detect, assess and mitigate risk in areas such as defense, public safety, food supplies, health, disasters, the environment and, in the broad sense of the word, the welfare of the people. Despite this, many government entities have not yet incorporated effective risk management in their organizations. This article reports government financial executives' and managers' opinions on risk management as it applies to financial and nonfinancial activities. It is based on the 2011 AGA surveys of financial executives and managers.



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