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Secretary of State

State of Oregon

**DEPARTMENT OF FORESTRY**



Audits Division

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*Auditing for a Better Oregon*

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Attached is our report on the Oregon Department of Forestry. We performed preliminary risk assessments of the department's operations to identify areas of risk the department faces. Our report includes audit results in three areas: financial-related, information technology, and performance-related.

In this report, we make recommendations to improve specific financial-related areas in which the department should strengthen its internal controls. We also noted information technology areas where controls could be improved.

The department generally agreed with our recommendations and has taken action to improve procedures to address a number of issues raised in this report.

OREGON AUDITS DIVISION

John N. Lattimer  
Director

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## EXECUTIVE SUMMARY

### BACKGROUND AND PURPOSE

The Oregon Department of Forestry's activities include fire protection for 16 million acres of private, state and federal forests (more than half of the forest land in Oregon); the detection and control of harmful forest insect pests and forest tree diseases and the administration of the Oregon Forest Practices Act on 12 million acres of private and state lands; the management of 780,000 acres of state-owned forest lands; forest resource planning and policy development; forestry assistance to Oregon's 166,000 non-industrial private woodland owners; and operation of a nursery which produces seedlings for reforestation.

The purpose of this audit was to perform financial-related, information technology, and performance-related preliminary risk assessments of the department's operations to determine whether there are risks that should be communicated to the department. Information from the risk assessments may also be used to identify future audits at the department. We also reviewed the department's efforts to implement recommendations from our audit report 95-30, *State Forest Management Program Cost Allocation Processes*, issued in 1995.

### RESULTS IN BRIEF

The audit identified financial-related areas in which the department should strengthen its internal controls. We found that the department:

- Could improve its internal controls for revenue accounting and cash handling for seedling sales from the D. L. Phipps Forest Nursery and the sale of permits to harvest special forest products (e.g. mushrooms, tree boughs, moss) at the district office we visited;
- Needs to address issues regarding its revolving fund. We found checks written for over \$5,000 without the pre-approval by the Fiscal Section required by department policy. There were also many outstanding checks over two years old that the department should cancel and determine the appropriate disposition; and
- Did not prepare required fixed asset reconciliations in a timely manner.

The audit also identified areas in which the department should strengthen its information technology controls. We found that the department:

- Has weaknesses in its access controls, which provide protection against unauthorized access to its systems and data;
- Did not regularly update its virus protection software at some of the department's workstations;
- Located some of its network hardware in highly visible areas that are generally accessible to unauthorized employees or the general public;
- Did not always retain sufficient documentation to ensure that computer program changes are appropriately authorized, tested, and approved;
- Did not store backup tapes in appropriate off-site locations;
- Has not fully developed its disaster recovery and contingency plans; and
- Did not maintain the software licensing records required by department directive for some of the department's programs.

We also provide information about the department's management of timber sales from state-owned forest lands. Information provided includes the timber sales process; various risks we identified; and the department's control procedures to reduce those risks.

Finally, we reviewed the department's efforts to implement the recommendations from our 1995 audit report, *State Forest Management Program Cost Allocation Processes* (report number 95-30). We found that the department has partially or fully implemented all of our recommendations.

**AGENCY'S RESPONSE**

The Oregon Department of Forestry concurs with the findings of the audit, and generally agrees with the recommendations.

## INTRODUCTION

The Oregon Department of Forestry (department), authorized by *Oregon Revised Statutes* (ORS) 526.008 and established in 1911, is under the direction of the state forester, who is appointed by the seven-member State Board of Forestry. The statutes direct the state forester to act on all matters pertaining to forestry, the protection of forest lands and the conservation of forest resources.

The department's activities include fire protection for 16 million acres of private, state and federal forests (more than half of the forest land in Oregon); the detection and control of harmful forest insect pests and forest tree diseases and the administration of the Oregon Forest Practices Act on 12 million acres of private and state lands; the management of 780,000 acres of state-owned forest lands; forest resource planning and policy development; forestry assistance to Oregon's 166,000 non-industrial private woodland owners; and operation of a nursery which produces seedlings for reforestation. The department also operates a motor pool with more than 500 pieces of equipment and a communications pool with more than 2,500 major pieces of radio communications equipment.

The department's 1997-1999 budget was \$171 million. This amount was funded by \$27 million from the General Fund, \$3 million from federal funds, and \$141 million from timber sales revenue, landowner assessments for fire protection, timber harvest taxes, burning fees, and the sale of nursery grown seedlings and other forest products.

## SCOPE AND METHODOLOGY

The purpose of this audit was to perform financial, information technology, and performance-related preliminary risk assessments of the department's operations to determine whether there are risks that should be communicated to the department. Information from the risk assessments also may be used to identify future audits at the department.

To accomplish the audit work for the financial-related portion of the audit we gained an understanding of the agency's operating and support programs and their controls and associated risks by interviewing staff at the department, the Legislative Fiscal Office, and the Department of Administrative Services. We also reviewed applicable laws, rules, and policies and procedures. In addition, we reviewed the department's organizational structure, budget documents, and previous audits done by the Audits Division. Furthermore, we

analyzed transactions for the period July 1, 1997, through December 31, 1998. We then evaluated the department's controls over disbursements, receipting, and fixed assets by performing additional interviews, inspecting documents, performing limited testing, and making observations at the department's Fiscal Section in Salem, the D. L. Phipps Forest Nursery, and one of the district offices.

For the information technology portion of the audit, we reviewed the department's Information Technology Section's information systems general controls. This work included a review of the control procedures for the following information technology processes: organizational structure; managing operations; managing problems and incidents; ensuring continuous service; managing facilities; system security; and ensuring compliance with external requirements. Our audit work included inquiries of the section's staff, examination of documents supporting controls and procedures, and observation of the section's processes and operations. We evaluated compliance with applicable laws, rules, and regulations pertaining to internal controls and the operation of the section. During our audit we used the Information Systems Audit and Control Foundation's (ISACF) *Control Objectives for Information and Related Technology* (COBIT) to identify generally accepted and applicable internal control objectives and practices for information systems. ISACF is a worldwide organization dedicated to research, develop, and publicize generally accepted information technology control objectives and audit guidelines.

For the performance-related (efficiency and effectiveness issues) portion of the audit, we restricted our risk assessment to the department's management of timber sales from state-owned forest lands. To accomplish our risk assessment, we gained an understanding of the timber sale process and the associated risks and controls by interviewing staff at the department, the Legislative Fiscal Office, and the Department of Administrative Services. We also interviewed staff of the United States General Accounting Office (GAO) specializing in forest resource issues. In addition, we reviewed applicable laws, rules, and policies and procedures. We also read pertinent audit reports prepared by the Audits Division, other states and the GAO. Furthermore, we read the report *Evaluation of*

*the Management of State-Owned Forest Land in Oregon*, published in 1998 by a consultant hired by the department to perform an evaluation of its management of the state-owned forest lands. We evaluated selected controls by observing the opening of competitive bids for timber sales at a district office, and reviewing various documents, including files for completed timber sale contracts. We also reviewed the department's efforts to implement recommendations from our audit report 95-30, *State Forest Management Program Cost Allocation Processes* issued in 1995. The audit covered the department's processes of allocating costs to the state forests program and, within the program, the allocating of costs between the Board of Forestry and Common School Fund lands.

We discussed the results our risk assessment with the department, which agreed with our conclusions.

We conducted this audit from April to September 1999 in accordance with generally accepted government auditing standards.



## FINANCIAL-RELATED AUDIT RESULTS

### REVENUE ACCOUNTING AND CASH HANDLING

One of our audit objectives was to gain an understanding of the Oregon Department of Forestry's (department) policies and procedures for processing and recording its receipts. Our audit determined that the department can improve its internal controls for seedling sales at the D.L. Phipps Forest Nursery and the sale of permits at the district office we visited.

The department's D. L. Phipps Forest Nursery (nursery), located near Elkton, provides quality, genetically-adapted tree seedlings for public and private reforestation. Sales of these seedlings total approximately \$5.5 million per biennium. Most of these payments are checks sent directly to a bank lockbox for deposit. The nursery processes telephone, mail-in, and walk-in credit card payments. The nursery also receipts and deposits walk-in cash payments that total less than \$5,000 a year. The orders and payments for the nursery's seedlings are entered by nursery staff into a subsidiary accounts receivable system maintained at the nursery.

We noted the following weaknesses in the nursery's internal controls for seedling sales:

- There is an inadequate segregation of duties for the revenue accounting, receipting, and depositing activities at the nursery. As a result, errors or theft may not be detected or prevented in a timely manner. One employee is responsible for producing billings and recording payments in the nursery's accounts receivable system, and is authorized to enter orders into the system, receipt walk-in cash payments, and prepare and make deposits. Cash handling should be separated from record keeping. Another individual is authorized to receipt walk-in cash payments, and prepare and make deposits. Where feasible, cash receipting and depositing activities should be performed by separate individuals.

**We recommend** that the department, to the extent feasible with the limited staff at the nursery, assign the duties of maintaining the accounts receivable subsidiary, cash receipting, and preparing and making deposits, to different individuals.

**AGENCY RESPONSE:**

*We agree with the recommendation. We recognize the importance of segregation of duties, and the Nursery Manager has reassigned duties of personnel to ensure our compliance with this recommendation. Position descriptions have been updated to reflect the job task changes, and oversight roles with managers have been clearly defined.*

- Nursery staff do not always deposit cash in a timely manner. The department's policy is that cash be deposited at least once per week, but any amounts over \$10 must be deposited daily. An example of an untimely deposit by the nursery is a deposit for \$633.00 made on March 31, 1999. The deposit consisted of seven cash receipts; the earliest was received on March 12, 1999. Six of the seven receipts were greater than \$10. Delays in depositing cash receipts increase the risk of loss.

**We recommend** that the nursery deposit its cash receipts in accordance with the department's policy.

**AGENCY RESPONSE:**

*We agree with the recommendation. The nursery staff have corrected their procedures for cash deposits to adhere to agency policy. On a broader level, we are also revisiting our overall cash deposit procedures in accordance with the Oregon Accounting Manual requirements to accommodate current business needs, and will make revisions as appropriate that will be implemented on a statewide basis.*

- The nursery does not restrictively endorse or list checks it receives by mail. Seedling purchasers paying by check are expected to mail their payment to a bank lockbox. The bank prepares the deposit and forwards the orders and deposit listing to the nursery. We were informed that four or five checks might be received in the mail daily at the nursery from December through April. The nursery staff reseals these envelopes and forwards them to the bank lockbox. These checks are not listed or restrictively endorsed. In addition, occasional walk-in customers pay by check. These checks are restrictively endorsed but are not listed prior to being forwarded to the bank lockbox.

Receipts should be recorded as soon as they come within an agency's control. The listed checks should then be compared with the bank lockbox deposit listings to verify that the checks were properly deposited. Restrictive endorsements on checks reduce the risk of misappropriation.

The nursery can decrease the number of checks it receives in the mail by revising the order form in the seedling catalog. The reverse side of the order form, which is in an envelope format, has the nursery's address. The result is that checks to pay the required deposit on a seedling order are mailed to the nursery rather than the bank lockbox.

**We recommend** that the nursery staff list all checks received at the nursery prior to forwarding them to the bank lockbox. They should also verify that all forwarded checks were subsequently deposited. Checks also should be restrictively endorsed when received. In addition, the nursery should consider revising the order form in the seedling catalog by removing the nursery's address from the reverse side. If the reverse side was left blank, the purchaser could write the applicable address, depending on the method of payment (credit card payments to the nursery and checks to the bank lockbox).

**AGENCY RESPONSE:**

*We agree with the recommendation. The nursery staff have changed and reinforced their procedures for recording checks prior to forwarding to the lockbox, and the nursery is currently in compliance with this recommendation.*

*The order form has been revised as recommended to enable purchasers to mail their checks directly to the lockbox.*

- The nursery's accounts receivable system does not have adequate access controls. The nursery uses a database system, separate from the Statewide Financial Management System (SFMS), to record seedling orders, produce billings and record payments from customers. Six employees are authorized to enter orders into the system, and one of these employees has the authority to produce billings and record payments. We found that all six employees, using their assigned password, can access all parts of the system. These employees have access to the ordering, billing and payment screens. The nursery's accounts receivable system should have access controls that restrict users to the system functions needed to perform their job responsibilities. In the absence of these controls, all six employees can change billing and payment information in the system, although only one employee has been given the authority to do so.

**We recommend** that the department's Information Technology Section work with nursery staff to determine whether it is

feasible to set up access controls for the nursery's accounts receivable system. The department also should consider having its Finance Section in Salem be responsible for the accounting functions involved with seedling sales; the nursery staff would be responsible for growing seedlings and filling orders.

**AGENCY RESPONSE:**

*We agree with the recommendation concerning improved access controls for the accounting system. The nursery information technology staff has been in the process of rewriting the accounts receivable system and order entry system, and is approximately 90% complete with this effort, with final completion planned for this spring. This revision will provide better management and control of access by staff.*

*We continue to believe that decentralization of our nursery accounting activities is the best fit for our operations. However, we will more closely align our accounting work between the nursery and our central fiscal services, and we believe that a number of factors will help us build better internal controls and greatly improve compliance with them. For example, some positions in the business services unit of the nursery organization have been reclassified, and some duties reassigned to accommodate appropriate segregation of job duties. In addition, Salem Finance staff will be more actively involved in developing internal controls and looking at system problems when they arise. Also, our proprietary fund accountant in Salem Finance will be playing a more active oversight role for the broad spectrum of the accounting process at the nursery. Finally, our intent is to pursue formal creation of an internal audit function within the agency, which will help review and monitor many business functions across all agency programs, including nursery operations.*

In addition to our review of the accounting and cash handling for seedling sales at the nursery, we selected one of the department's field offices (Forest Grove) for a review of its cash receipting process. The department has 14 field offices that, among other tasks, issue permits and deposit the receipts for woodcutting and special forest products (e.g. mushrooms, tree boughs, and moss). The district offices determine the permit prices and whether checks are accepted. The Forest Grove office accepts only cash for the permits. We were told that this policy is the result of the office receiving many insufficient funds checks in the past.

Our review of cash receipting at the Forest Grove district office revealed the following internal control issues:

- Deposits are not made in a timely manner as prescribed by department policy. Deposits are generally made once a week unless there is over \$400 to \$500 in cash on hand.

The department's policy requires that any cash amounts over \$10 be deposited immediately (daily).

**We recommend** that the Forest Grove district office adhere to the department's policy for depositing cash. The department should communicate to its district offices the importance of adhering to this policy.

**AGENCY RESPONSE:**

*As with the similar recommendation for the nursery operation, we agree with this recommendation. The District staff has corrected their procedures for cash deposits to adhere to agency policy. Again, though, on a broader level, we are also revisiting our overall cash deposit procedures in accordance with the Oregon Accounting Manual requirements to accommodate current business needs, and will make revisions as appropriate that will be implemented on a statewide basis.*

*As a decentralized organization, we will visit with all our office locations to provide consistent emphasis on this recommendation.*

- Too many employees have physical access to the district office's cash receipts. Five employees have access to the safe in which the cash receipts are held until they are deposited. The greater the number of employees with access to the cash receipts, the greater is the risk of misappropriation.

**We recommend** that access to the safe be limited to the minimum number of employees considered prudent under good business practices.

**AGENCY RESPONSE:**

*We agree with the recommendation. We will visit with all of our field offices on this issue to assess their current situation, and to provide information about best practices for access to office safes.*

- The district office's cash controls are weakened because the special forest products permits are not pre-numbered. While pre-numbered receipts are supposed to be issued every time a permit is sold, the lack of pre-numbered permits increases the risk that permits are issued and the cash received is not reported. Requiring the use of pre-numbered permits would strengthen cash controls because cash received, and the permits and receipts issued could be linked. The district office does use pre-numbered woodcutting permits.

**We recommend** that the district office use pre-numbered permits, and account for those permits in conjunction with cash received and receipts issued, for its special forest products.

*AGENCY RESPONSE:*

*We agree with the recommendation. The permit development process is a centralized function of the State Forest program of the agency. We will change our permit forms to be pre-numbered, and will work with our field offices to ensure that adequate internal controls are developed and adhered to for better accounting results in this area.*

Many of the above-noted items, when considered alone, do not pose a significant risk to cash. When taken together, however, we believe that the risk of loss or theft is greatly increased. **We also recommend** that the Forest Grove district office reconsider its policy of not accepting checks for permits. The risk of misappropriation is much greater for cash than it is for checks.

*AGENCY RESPONSE:*

*We do not concur with this recommendation due to a local history of NSF checks. However, as noted in other responses, we will take steps agency-wide to strengthen and comply with better cash handling controls to minimize the risk in this area.*

**STATE FORESTRY  
DEPARTMENT REVOLVING  
FUND**

As part of our audit, we reviewed the department's policies and procedures for various types of disbursements. Our review determined that there are issues the department needs to address regarding its revolving fund. The department's revolving fund, authorized by law in the amount of \$750,000, is used to pay for emergency fire-fighting obligations and miscellaneous special purchases at the department's field offices. The department has a policy that requires pre-approval by the Finance Section in Salem for payments greater than \$5,000.

We noted the following weaknesses associated with the department's revolving fund:

- The department's D. L. Phipps Forest Nursery (nursery) did not obtain pre-approval from the Finance Section for payments that exceeded \$5,000. Our review determined

that the nursery wrote six revolving fund checks that exceeded \$5,000 during fiscal years 1997 and 1998. These checks totaled \$52,760 and were refunds to customers whose orders could not be completely filled. The nursery did not obtain pre-approval from the Finance Section for these payments as required by department policy.

**We recommend** that the department take steps to ensure that its policy requiring pre-approval for revolving fund checks exceeding \$5,000 is followed. As recommended above, the department should consider having the Finance Section assume the accounting duties involved with the nursery's seedling sales.

**AGENCY RESPONSE:**

*We agree with the recommendation regarding adherence to agency policy for approval for revolving fund checks exceeding \$5,000. Nursery staff has already taken procedural steps to ensure compliance with this policy and the requirements needed to meet it. We will also visit with other field offices to ensure understanding of the policy. As noted above, we continue to believe that decentralization of our nursery accounting activities is the best fit for our operations, but we will more closely align our accounting work between the nursery and our central fiscal services.*

- There are many outstanding checks listed on the monthly revolving fund reconciliation that are considerably older than the two year limit for canceling checks. We reviewed the department's March 1999 reconciliation and noted that there were numerous outstanding checks over two years old (there were 18 checks written in 1994, 12 written in 1995, and 20 written in 1996 included in the outstanding check listing). State agencies are required to report annually, as of August 1, to the Department of Administrative Services and the State Treasurer checks that have been outstanding for a period of more than two years as of July 1. These checks are subsequently cancelled. The amounts should then be credited to the agency's fund(s) that provided cash for the revolving fund or in some circumstances be transferred to the Department of State Lands for deposit in the Unclaimed Property Revolving Fund within the Common School Fund Account.

**We recommend** that the department take the required steps to cancel the outstanding revolving fund checks older than two years and determine the appropriate disposition for those amounts.

**AGENCY RESPONSE:**

*We agree with the recommendation. We have already implemented this recommendation and taken corrective steps to bring our records current. Our procedures have been reviewed and employees have received additional training to understand this process, including our reporting obligations.*

**FIXED ASSETS**

One of our audit objectives was to gain an understanding of the department's policies and procedures pertaining to its fixed assets. The department had \$32.3 million in recorded fixed assets at June 30, 1998. This amount consisted of \$18.2 million for equipment and machinery, \$11.5 million for buildings and \$2.6 million for land. The department uses an enterprise fund (the D. L. Phipps Forest Nursery), two internal service funds (motor pool and communications pool) and the general fixed-assets account group (for the department's other fixed assets) to account for its fixed assets. Accumulated depreciation also is recorded in the enterprise fund and the two internal service funds. The department values approximately 657,000 acres of its state forest lands at one dollar per acre.

Our review determined that the following internal controls for fixed assets can be strengthened:

- Required reconciliations are not being prepared in a timely manner. In addition, the titles to vehicles should be held by the department's Finance Section instead of the Fleet Manager. As of May 1999, the department's latest completed quarterly fixed asset reconciliations were March 31, 1997, for the general fixed assets account group; June 30, 1998, for the two internal service funds (motor pool and communications pool); and December 31, 1998, for the enterprise fund (nursery). The Department of Administrative Services (DAS) requires state agencies to reconcile expenditures for non-expendable property (capital outlay) with the property recorded in the property ledger(s) each quarter. DAS also requires a reconciliation of the property ledger(s) with the general ledger's control accounts at least every quarter. These reconciliations are an important control activity, they help ensure accountability and proper financial reporting for the department's fixed assets. The absence of timely reconciliations can result in acquired assets not being recorded in the property ledgers and undetected differences between the property ledgers and

general ledger control accounts. The risk of loss or misappropriation of assets is increased. Unrecorded assets also result in misstated asset balances and depreciation expense.

**We recommend** that the department prepare the backlogged fixed asset reconciliations as soon as is practical and thereafter prepare the quarterly reconciliations in a timely manner.

*AGENCY RESPONSE:*

*We agree with the recommendation. We brought our fixed asset reconciliations current immediately upon being identified during this audit. We continue to be current and are able to comply with the quarterly reconciliation process.*

**We also recommend** that titles to vehicles be held by the department's Finance Section instead of the Fleet Manager.

*AGENCY RESPONSE:*

*We agree with the recommendation. We will take steps necessary to transfer current vehicle titles to the Finance Section, and establish procedures for assignment of future titles to the Finance Section.*



## INFORMATION TECHNOLOGY AUDIT RESULTS

The Oregon Department of Forestry (department) computer system consists of approximately 750 personal computers attached to 31 local area networks (LANs), which are at various locations throughout the state. These networks are linked to the Department of Administrative Services General Government Data Center, as well as the Department of Transportation mainframe computer. Department employees from the various district offices maintain many of these networks. In addition, the department provides central computer support services through its Applications and Technical Support Units. These services include planning, database administration, software development, network management, training, and computer security.

The department's computer software platform includes standard off-the-shelf software for word processing, creating spreadsheets, and electronic mail (e-mail). In addition, the department's employees use several custom applications to accomplish more specific tasks, such as timber revenue accounting, billing and payroll.

### ACCESS CONTROLS

The department relies on password protection software to safeguard information against unauthorized use, disclosure, modification, damage or loss. Effectiveness of these access controls depends on whether the password protection software is properly maintained. For example, users should be assigned access privileges based on their need to view, add, change, or delete data. To ensure that this mechanism remains effective, system owners should regularly review and confirm users' access privileges and make necessary changes in a timely manner. The department's access controls should be improved to provide better protection for systems and data. Weaknesses in the department's access controls include the following:

- Technical support employees have access privileges beyond what is required to perform their duties.
- Some employees are authorized to share a single user ID, making it difficult to monitor and control employee access and activity.
- Security policies do not require users to create unique passwords, and users are not required to periodically change their passwords.

- Access privileges are not always revoked promptly for employees no longer requiring access. For example, some terminated employees' access privileges remained unchanged for as long as 30 days after they left the department.

These conditions exist because the department has not developed sufficient policies and procedures to effectively govern access to its systems and data. As a result, the risk increases that unauthorized transactions may occur or the agency's computer resources may be compromised.

**We recommend** that the department further develop and implement computer security policies and procedures to provide better control over access to information systems and data. These policies and procedures should ensure that:

- Technical support employees are provided only those access privileges needed to perform their assigned duties.
- Employees are prohibited from sharing user IDs and passwords.
- Users create and use effective passwords. These passwords should be five to eight characters in length, difficult for others to guess, and easy for the user to remember. In addition, require users to periodically change their passwords to lessen the risk that passwords may be compromised.
- Prompt revocation of access privileges when employees terminate employment or when their level of access is no longer needed.

*(See agency response on page 17.)*

## **VIRUS PROTECTION**

The department utilizes virus protection software to protect its systems and data from damage resulting from malicious software attacks. To ensure protection against new viruses, this software must be regularly updated. Although the department's virus protection software is

designed to automatically update necessary files, we noted that some technical support staff workstations were not updated with the most recent versions of those files.

**We recommend** that the Technical Support unit implement procedures to periodically ensure that all virus protection software is being updated as intended.

*(See agency response below.)*

## **PHYSICAL SECURITY**

The department is responsible for protecting its computer equipment against man-made and natural hazards. These responsibilities include limiting physical access to computer equipment and providing an appropriate operating environment. Generally accepted computer control standards recommend that critical equipment such as network servers be placed in secure, low-visibility areas.

In some instances, we found that the department's network hardware was located in highly visible areas and was generally accessible to unauthorized employees or the general public. This condition exists because the department lacks policies and procedures to ensure that computer systems are adequately secured and housed. As a result, the department has increased risk that some computer systems could be stolen, damaged or changed.

**We recommend** that the department establish written policies and procedures to safeguard its computer systems. These policies and procedures should require all critical network components be located in locked areas accessible only to authorized employees. The locked areas should provide the recommended operating environment for the equipment and be in less visible locations.

### **AGENCY RESPONSE:**

*We agree with these recommendations. During the past several months, we have been developing a new agency information technology security policy and plan. The policy has been developed in concert with Information Resources Management Division (IRMD) guidelines, and with discussions with the audit team itself as the audit has*

*progressed. The new policy is in draft form, and we will proceed with both agency leadership review and input as well as IRMD review, and we will implement the policy and plan in the second half of this calendar year.*

*In addition, we are currently reviewing interim policy and procedures regarding system access controls, password protection, and automatic updating of virus protection at both the server and workstation level. As a result of this review, we will implement actions necessary to address the recommendations.*

## **MANAGING CHANGES**

To provide adequate control over changes to computer applications and systems, the department's Applications Unit should have processes to ensure that the work it does is adequately documented. These mechanisms should ensure that computer program changes are appropriately authorized, tested, and approved.

The department's managers currently e-mail their program or system change requests and authorizations to the Applications Unit. The unit, however, does not always retain these requests. In addition, of the five application changes reviewed, only one had adequate documentation of the changes made. The Applications Unit did not retain sufficient documentation for the remaining four applications we tested.

Lack of program change documentation increases the risk that inappropriate or unauthorized changes may occur. In addition, it increases the risk that programs may be put into production before they are adequately tested and approved. These conditions exist because the department lacks system development policies and procedures requiring preparation and retention of program-change documentation.

**We recommend** that the Applications Unit more fully develop and implement formal system development policies and procedures. These policies and procedures should require staff to prepare and retain sufficient documentation of computer program or system changes.

**AGENCY RESPONSE:**

*We agree with the recommendation. Systems development and change policies and procedures will be developed and implemented which take into consideration the criticality and scope of system projects. These will be prepared for addition to the department's Information Technology directive. Interim policies and procedures will be circulated to appropriate staff and internal customer representatives. The policies and procedures will provide for system by system documentation of development or change requests, authorization, testing, and approvals, and monitoring of such documentation. We will use the COBIT framework as the basis for this policy and procedure development.*

**BACKUP AND RECOVERY**

The department currently has policies requiring regular backups of systems and data. To provide adequate protection of data, backup tapes should be stored in an offsite facility far enough away from the computer site to ensure that it is not affected by the same event. In addition, the offsite storage facility should be adequately secured.

Many of the department's backup tapes are not stored in an offsite location; they are stored in the same building as the original systems. As a result, the department is at risk of losing both the system and its backup should a destructive natural or manmade event occur.

**We recommend** that forestry management modify its current policy to require backup tapes be regularly stored in appropriate offsite locations.

*(See agency response on page 20.)*

**ENSURING CONTINUOUS SERVICE**

Disaster recovery and contingency planning are necessary to ensure that information technology services will be provided in the event of a significant disruption of service. The effectiveness of these plans depends on whether they are tested and all necessary parties are trained regarding their roles and responsibilities. Although the department prepared a contingency plan, it

has not sufficiently addressed the following disaster recovery elements necessary to restore its computer operations:

- A list of key resources including data files, equipment and supply needs, operation manuals and sufficient documentation to expedite the data restoration process.
- A disaster recovery training plan that includes employee awareness of their roles and responsibilities.
- A testing plan to provide positive assurance that the recovery plan will be reliable and to ensure that the necessary resources will be available to restore data.

As a result, the department is less prepared to promptly recover its systems and data should a significant disruption in service occur.

**We recommend** that department management fully develop its disaster recovery and contingency plans to include provisions for recovering information systems and data, adequate training of employees assigned to recovery teams, and provisions to periodically test its plans. Further, we recommend that the department provide for continuing review and updates of its disaster recovery and contingency plans to ensure that they remain current.

**AGENCY RESPONSE:**

*We agree with these recommendations. As with the agency security policy and plan, an Information Systems Backup and Disaster Recovery Plan is in development. We are utilizing the framework of our Y2K Business Continuation Plan as the basis for this draft. Our backup and recovery plan will address these recommendations, and again, will be developed with agency leadership review and input from IRMD, particularly as related to the utilization of the Burns Data Center.*

**SOFTWARE LICENSES**

Department management issued a department-wide directive requiring units to maintain records of software licenses. The policy further states that the Information Technology Director will be responsible for monitoring compliance with this directive.

Some department programs, however, do not maintain the required software licensing records. In addition, the last review performed by the Information Technology Section was conducted in 1996. Thus, the department has less assurance that it will remain compliant with software licensing requirements.

**We recommend** that department managers comply with current policies regarding maintenance of software records, and that the Information Technology Director provide for the regular software license reviews as directed.

*AGENCY RESPONSE:*

*We agree with the recommendation. We will visit with field and staff managers and system administrators within the next four months, and conduct the required reviews.*

**MONITORING**

Management should monitor and assess the effectiveness of internal controls intended to protect computing resources. The department currently does not have a central internal audit function to provide assurance that information technology controls are working as intended. In addition, its organizational structure is primarily decentralized and relies on area managers and program directors to ensure that each unit is complying with most policies and procedures.

This condition increases the risk that intended operational security and other internal controls may be ineffective. In addition, lack of monitoring increases the risk that internal control errors, inconsistencies, and exceptions may not be systematically documented and reported to management.

**We recommend** that department management develop and implement processes for regularly monitoring and assessing the effectiveness of key information technology controls. Individuals who are independent of the controls being monitored should perform these procedures. In addition, the results of these reviews should be provided to the agency director, or to a senior manager who is

independent of the information technology function, for follow-up action if needed.

**AGENCY RESPONSE:**

*We agree with the recommendation. We are in the development stages of establishing a broad internal audit function for the agency, to address the types of issues raised with this finding and recommendation. Given current staffing levels, we anticipate proposing additional positions as an agency request during the upcoming 2001-03 biennial budget development process. We believe that this is a critical business function that will benefit all agency programs, including information technology, and are anxious to formalize this function within the Department.*

## PERFORMANCE-RELATED RISK SURVEY RESULTS

The department manages about 780,000 acres of state-owned forest lands. There are five major state forests:

- Clatsop, about 138,000 acres in northwest Oregon near the coast,
- Elliott, about 98,000 acres near Coos Bay and Reedsport on the central coast,
- Santiam, about 48,000 acres in the Willamette Valley,
- Sun Pass, about 34,000 acres near Crater Lake, and
- Tillamook, about 380,000 acres in northwest Oregon near the coast.

The department also manages a number of small tracts scattered across the state. State forests consist chiefly of second-growth conifer forests. The department's 780,000 acres of managed forest lands include about 657,000 acres of formerly county-owned lands, designated as Board of Forestry (BOF) lands, while the remaining 123,000 acres are Common School Fund (CSF) lands.

**BOF LANDS:** (657,000 acres) Oregon law requires that 63.75 percent of the timber sale revenues from these lands be distributed to the counties and local taxing districts where the timber is harvested; the remaining 36.25 percent of the revenues are distributed to the department for management of the lands.

**CSF LANDS:** (123,000 acres) are primarily located in the Elliott State Forest, and managed by the department under contract with the Division of State Lands. Revenues from the CSF lands go to the Common School Fund. The department bills the Division of State Lands for reimbursement of its costs (direct and indirect) to manage the CSF lands.

Oregon law requires that BOF lands be managed to achieve the "greatest permanent value." The board has determined that "greatest permanent value" means healthy, productive, and sustainable forest ecosystems that over time and across the landscape provide a full range of social, economic, and environmental benefits to the people of Oregon. Sustainable and predictable timber production is only one of the values; other values include habitats for wildlife, productive soil, clean air and water, protection against floods and erosion, and recreation. All five major state forests are covered in forest management plans on which the department is now working. In addition, the U.S. Fish and Wildlife Service approved a Habitat Conservation Plan for the Elliott State Forest in 1995. This plan allows incidental "take" of endangered species as long as the plan is complied with.

CSF lands are supposed to be managed to maximize long-term revenue for the schools. For practical purposes, the requirements to comply with various federal regulations (Endangered Species Act, Clean Air and Clean Water Acts) and the Habitat Conservation Plan for the Elliott State Forest, results in management of the CSF lands in a manner similar to the BOF lands ("greatest permanent value").

Table 1 provides information on timber sale receipts and the amounts transferred by the department to the “counties” (counties, school districts, and other local taxing districts) for the BOF lands. It includes timber sale receipts, transfers to, and the department’s management expenses billed to the Division of State Lands for the CSF lands. There were 245 active sales during this period; 150 were commercial thinning harvests, while the remaining 95 were clear-cuts.

**Table 1**  
**1997-99 Timber Receipts and Distributions<sup>1</sup>**

	Board of Forestry Lands	Common School Fund Lands
Timber Receipts	\$101,395,135	\$33,844,845
Transfers to Counties	64,295,096 <sup>2</sup>	–
Transfers to DSL	–	33,241,546 <sup>3</sup>
ODF Expenses billed to DSL	–	9,959,999

## TIMBER SALES PROCESS

The major components of the timber sale process are sale planning, sale preparation, awarding the contract, and contract monitoring.

### Sales Planning

The department plans its timber sales to achieve a relatively stable supply of timber in consideration of the local jobs affected and expected revenue for the counties, local taxing districts, Common School Fund and the department. The nine department districts that have state forest lands prepare annual operating plans covering their planned timber sales. There are two types of sales: clear-cuts, in which the contractor pays a lump sum for all timber within the sale boundary; and commercial thinning, in which the contractor thins the timber within the sale boundary.

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<sup>1</sup> Information was provided by the department and is for July 1, 1997, through June 30, 1999.

<sup>2</sup> The total transferred is less than 63.75 percent because some revenue came from lands that were rejuvenated using state bond funding; 12.75 percent of net revenues from those lands go to the state general fund until the bonds are repaid.

<sup>3</sup> The amount transferred to the Division of State Lands differs from the timber receipts because of a timing difference in the transfer process.

## Sales Preparation

Sales in the districts' annual operating plans must be prepared for bid. Determining the minimum bid involves several steps:

1. Projects (road building, reforestation, etc.) to be completed by the contractor are determined with the estimated cost to perform the work;
2. The site is "cruised"<sup>4</sup> to determine the number of trees by species, size, and grade;
3. Quarterly surveys of local mills are used to determine the market value of the on-site timber; and
4. The contractor's costs of felling and hauling the timber are estimated.

The department uses this information to determine the minimum bid. An auction booklet of proposed sales is compiled monthly by the department and mailed to companies that do business with the department. Contract specifications for the sale are available for review. Potential bidders are expected to inspect the sale site and not rely solely on the department's descriptions and estimates when deciding whether and how much to bid.

## Awarding Sales Contracts

All sales of \$25,000 and over are awarded by competitive sealed bid, subject to a minimum bid amount set by the department. The winning bidder must submit proof of insurance, a performance bond, an operations plan, and a first-installment payment. The contractor is required to attend a pre-operations meeting with the department's contract administrator for the sale. The meeting is used to convey the department's contract expectations and answer contractor questions. When these requirements are satisfied, including approval by the department of the contractor's operations plan (which is incorporated into the contract), operations can begin.

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<sup>4</sup> A "cruise" is to estimate the volume and quality of a timber stand by visual examination of test plots or strips in the stand. A cruiser usually examines from 10 to 20 percent of the total stand.

### **Contract Monitoring**

Department inspectors are assigned for each sale contract and make onsite visits throughout the project and harvest activity. The inspectors monitor the contractor's operations to verify that the contractor is adhering to the contract requirements and making satisfactory progress. The department bills the contractor as specified in the contract as the harvest proceeds. When operations are completed, the department performs a final inspection. If no deficiencies are noted, the department releases the contractor's performance bond.

### **TIMBER SALES RISKS AND CONTROLS**

#### **Some Risks are Unique for Clear-Cut Sales**

Clear-cut and commercial thinning sales represent different risks for the department. In a clear-cut sale, the department sells all of the timber on the sale site (other than specified trees left for wildlife, stream buffers, etc.) to the contractor for a lump sum. A significant risk is that the timber is sold for less than market value. To counter this risk, the department uses well-trained employees to perform the timber cruise. Quarterly mill surveys keep the department current regarding the market value for timber. The timber cruise information, coupled with the mill survey data and the department's estimates of the contractor's harvest costs, are used to establish a minimum bid amount. Sealed competitive bidding with a minimum bid established by the department should minimize the department's risk of receiving less than the fair market value for its timber.

Another risk for a clear-cut sale is the contractor's harvesting timber outside the sale site boundaries. The department attempts to use natural boundaries and roads for the boundaries when feasible; otherwise, boundary trees are marked. The department relies on onsite monitoring by its inspectors to ensure that the contractor's operations remain within the boundaries. The sale contract provides for double or triple (if the violation was intentional) damages for boundary violations.

**Other Risks are Unique for  
Commercial Thinning Sales**

Unlike clear-cut sales, which involve a lump-sum amount, commercial thinning sales are awarded based on the price bid per unit of timber removed by the contractor. The department uses independent scaling bureaus to measure and record the volume of timber removed. The most significant risk for commercial thinning sales is that timber is harvested and not recorded (or recorded at a lower volume or grade than actual) by the scaling bureau. The department appears to have good controls in these areas:

1. Harvesting and scaling are allowed only during specified times, and a specific scaling site must be used;
2. Logs must be branded with a specific brand issued by the department for the sale;
3. Log load receipt booklets with serially-numbered, multi-part receipts are issued to the contractor and accounted for by the department (the department matches the receipt portion from the scaling bureau with the receipt from the contractor and all booklets must be returned to the department); and
4. The last scaled load must be held at the scaling site for surprise checks by department inspectors.

Another risk for commercial thinning sales is timber left on the ground by the contractor because it was damaged when it was felled or deteriorated from being left on the ground too long. The department's onsite inspections, including the final inspection, are the primary control over this risk. When the department detects timber improperly left on the ground, it scales the timber and charges the amount to the contractor.

**Risks Pertinent to Both  
Types of Sales**

There are other risks applicable to both types of sales. One risk is that the sale site is damaged by the contractor's operations. The department can require the contractor to use a specified logging method (helicopter or cable yarding) and to log only during a certain portion

of the year to minimize site damage. The department relies on its onsite monitoring to detect unacceptable site damage. Damages can be recovered from the contractor's performance bond. Another risk is the failure of the contractor to make required installment payments as the harvest progresses. In such cases, the department can order a work stoppage. If the contractor does not make the required payment, the contract would be defaulted and the department has various remedies including using the contractor's performance bond, reselling the contract, and suing the contractor.

A final risk is the department's liability to the contractor when the department suspends or cancels a contract. The contract provisions and the department's administrative rules limit this risk. Contracts may be suspended or cancelled when in the best interest of the state. The department's liability to the contractor is limited to specified contractor out-of-pocket costs.

We found that the department's controls for the risks we identified related to its management of timber sales from state-owned forest lands appear to provide reasonable assurance against a significant occurrence of those risks.

**AGENCY RESPONSE:**

*As we discussed with the Audit Team at the outset of this review, we appreciated the opportunity to receive a thorough review of our timber sale program and processes during this audit. We concur with your findings and assessment of our current situation for the program, and are pleased to learn that our risk is appropriately managed.*

## PRIOR AUDIT FOLLOW UP

As part of the comprehensive audit of the department, we followed up on our audit report number 95-30, *State Forest Management Program Cost Allocation Processes* issued in 1995. The report concluded that the department needed to improve its system of cost accounting for the State Forests Program to ensure that the costs charged to the Board of Forestry (BOF) and Common School Fund (CSF) lands are reasonable and accurate.

In 1995, we reported that the department lacked cost detail on program activities because management did not require that such detail be recorded in the accounting records. Furthermore, the department's process (budget-based) to allocate administrative costs to its programs resulted in a greater percentage of such costs being allocated to the State Forests Program than would have been allocated under a usage-based model. Also, the performance measures information reported by the department was not obtained from or reconciled to the department's accounting system records and was incomplete and potentially misleading. In addition, the Division of State Lands (the administrative arm of the State Land Board) indicated that they were not satisfied with the content of the department's annual report to the State Land Board.

Our audit made five recommendations that, if implemented, would enable the department to better account for programs and track and report costs by activity. Overall, the department has implemented most of our recommendations. Following are the recommendations and the department's actions to implement the recommendations:

- 1. Restructure the processes used to allocate central and program administrative costs to department activities on bases that are reflective of how much the administrative activities are used. Once implemented, these processes should be periodically reassessed to ensure that they continue to result in an equitable distribution of costs. The department should then fix authority and responsibility to monitor the process.**

*Fully implemented.* The department no longer allocates its central administrative costs (overhead) among all programs based on a formula that computes each program's budget as a percentage of the total budget for the department. The department conducted a units of measurement study in 1995 in which it measured various activities (e.g. time spent on tasks, transactions processed) performed by the department's central support units (personnel, finance, computer services, graphics, etc.) for the department's programs, including the State Forests Program. The study included activities for the BOF and CSF lands. The resulting percentages are used to allocate the central administrative costs to the programs (and BOF and CSF lands within the State Forests Program).

The costs of the central State Forest Management Program staff located in Salem are allocated between the BOF and CSF lands based on their statewide acreage ratio.

District costs are directly charged when activities pertain to specific BOF or CSF acreage. Otherwise, the costs, including district overhead, are charged based on the acreage ratio of BOF and CSF land in the district.

The department has assigned the responsibility of monitoring and managing the cost allocation process to the Finance Director and the Assistant State Forester, Agency Administration Division.

It appears that the current process of allocating central and program administrative costs to the department's programs, and to the BOF and CSF lands within the State Forests Program, results in an equitable distribution of costs.

**2. Fully utilize the accounting system to track actual costs of significant program activities.**

*Partially implemented.* The department uses the Statewide Financial Management System (SFMS) to track its actual costs by activity for the State Forests Program. SFMS coding was revised for the 1999-2001 biennium to record expenditures in six major categories: administration, forest management, forest products, information systems, engineering, and social. These categories will be used for budgeting, expenditure monitoring and reporting. The department intends to also perform time and motion studies for selected subcategories (for example, timber sale preparation within the category of forest products) each year to attempt to identify activities that can be performed more efficiently.

**3. Use the accounting system as the primary source for reporting program results of a financial nature. The department's fiscal section should be involved in the process of accumulating financial information that is to be included in the reporting of program results to ensure that the information reported is an accurate representation of what is reflected in the accounting records.**

*Fully implemented.* The department uses SFMS as the primary source to report program results of a financial nature. Prior to implementing SFMS in 1997, the department's Timber Revenue Accounting System (TRAS) was the primary source for reporting the program results of the State Forests Program. Using TRAS to report program results was unsatisfactory because it did not include some major cost components, including personal services. This issue was resolved when the department began using SFMS as the primary source for reporting the program's results. The department does use information from TRAS to supplement SFMS for reporting the program's results.

**4. Establish central policies and procedures to ensure uniform application in allocating and tracking costs, and fix authority and responsibility to monitor and manage the process.**

*Fully implemented.* The department has established central policies and procedures regarding the allocation and tracking of costs. The Finance Director and the Assistant

State Forester, Agency Administration Division are responsible for monitoring and managing the process.

**5. Meet with the State Land Board to clarify reporting and communication requirements. Modify the management agreement to accommodate desired changes.**

*Partially implemented.* The department met with Division of State Lands to agree on significant activities and costs to include in reports to the State Land Board. The department and the Division of State Lands are currently negotiating revisions to the management agreement.

*AGENCY RESPONSE:*

*We concur with your findings and assessment of our implementation progress in response to the 1995 audit report (95-30). We believe that we have made significant strides and improvements in cost allocation and tracking in response to that audit.*

*We would note that we believe that we are now in a “fully implemented” status with regard to recommendation #2, but understand that since this did not occur until July of 1999 at the beginning of this biennium, your assessment may not consider full implementation until the 1999-01 biennial cycle is complete.*

*With respect to recommendation #5, we would concur that the recommendation is partially implemented due to current negotiating efforts with the Division of State Lands regarding revisions to the management agreement.*

## **COMMENDATION**

The courtesies and cooperation extended by officials and employees of the Oregon Department of Forestry during the course of this review were commendable and sincerely appreciated.

## **AUDIT TEAM**

Andrew Bromeland, CPA, Audit Administrator  
Drummond Kahn, MS, CGFM, Audit Administrator  
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Ann Takamura, MPA  
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**AGENCY'S RESPONSE TO THE AUDIT REPORT**





# Oregon

John A. Kitzhaber, M.D., Governor

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January 26, 2000

John N. Lattimer, Director  
Audits Division, Office of the Secretary of State  
255 Capitol Street NE, Suite 500  
Salem, OR 97310

Dear Mr. Lattimer:

Subject: 1999 Department of Forestry Audit



"STEWARDSHIP IN FORESTRY"

On January 18, 2000, we received from Audit Administrator Drummond E. Kahn the draft report of the recent financial, information technology, and performance-related risk assessment of the Department of Forestry. As requested, enclosed is our response to the findings and draft recommendations. In summary, we concur with the findings of the audit, and generally agree with the recommendations. As we conclude this phase of the process with your staff, we will be preparing a specific agency action plan with our leadership team to implement and monitor our own response efforts. When that action plan is completed, we will share the plan with you as well.

This audit process, and the subsequent results, have been very productive for the Department of Forestry, and I believe will serve us very well in the years to come. On behalf of the agency staff who worked directly with your audit team, I would like to thank you for the professional approach that was taken by the team, and the genuine interest that they demonstrated in making this a very positive, collaborative process that will truly assist us in making improvements to our business and agency management practices. We recognize that performance auditing is a valuable tool, and your audit team's approach and attitude during this process has been helpful and supportive in creating possibilities for practical improvements for the Department.

We will look forward to our final exit conference with the audit team, and continuing to move ahead on implementation efforts.

Sincerely,

James E. Brown  
State Forester

JEB:CWS

enclosure

cc: Jon Yunker, Director, Department of Administrative Services  
Agency Leadership Team



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### **DIRECTORY OF KEY OFFICIALS**

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*Deputy Director*

*Deputy Director*

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