OFFICE OF THE
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Auditing for a Better Oregon

January 14, 2005

Marvin Brown, State Forester
Oregon Department of Forestry
2600 State Street
Salem, Oregon 97310

Dear Mr. Brown:

The statewide single audit that included selected financial accounts at the Oregon Department of Forestry (department) for the year ended June 30, 2004, has been completed.

This statewide single audit work is not a comprehensive audit of your agency. Instead, this audit permits us to give an opinion on the statewide financial statements contained in the State of Oregon's *Comprehensive Annual Financial Report* and to report on internal control and the state's compliance with laws and regulations. Regular audits of the department will continue on a periodic basis.

The following department accounts and transactions were audited to determine their fair presentation in accordance with generally accepted accounting principles in relation to the statewide financial statements.

SFMA Account	Description	Audit Amount
Special Revenue Fund – Environmental Management (GAAP Fund 1107)		
0065	Unreconciled Deposit	$ 9,673,760
0070	Cash on Deposit with Treasurer	24,245,031
0075	Cash on Deposit—Suspense Account at Treasury	199,875
0501	Accounts Receivable—Other Billed	3,259,569
503	Accounts Receivable—Other Unbilled	17,480,951
0703	State Forest Lands	75,495,987
1303	Transfer in from General Fund	7,244,700
1315	Transfer in from Division of State Lands	5,022,973
1316	Transfer in from Department of Revenue	5,736,391
1405	Transfer to Counties	47,918,084
1810	Transfer to Division of State Lands	15,062,909
3111	Regular Employees	20,022,041
3130	Seasonal Positions	4,736,729
3171	Overtime Payments	2,711,969
3210	Public Employees Retirement Contribution	3,177,223

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SFMA Account	Description	Audit Amount
3221	Social Security Taxes	2,198,699
3263	Medical, Dental, Life Insurance	3,684,723
4202	Equipment Rental	5,203,970
4500	Professional Services	6,505,795
4505	Professional Services > $75K	16,788,326
4600	State Government Service Charges	8,450,363
4976	Agency Program Related Supplies	2,227,187

Based on our audit, we identified six reportable conditions needing corrective action. Our findings and recommendations are presented in the enclosed Audit Findings and Recommendations Summary accompanying this letter.

The reportable conditions, along with your responses, will be included in our statewide audit report. Including your responses with responses from other state agencies satisfies the federal requirement that management prepare a Corrective Action Plan (CAP) covering all reported audit findings. Satisfying the federal requirement in this manner, however, can only be accomplished if the response to each reportable finding includes the information specified by the federal requirement, and only if the responses are received in time to be included in the audit report. The following information is required for each response:

1. Your agreement or disagreement with the finding. If you do not agree with an audit finding or believe corrective action is not required, include in your response an explanation and specific reasons for your position.

2. The corrective action planned.

3. The anticipated completion date.

4. The name(s) of the contact person(s) responsible for corrective action.

For the reportable conditions, please respond by January 31, 2005.

Should you have any questions, feel free to contact Margaret Wert or me at (503) 986-2255.

Sincerely,
OREGON AUDITS DIVISION

Nancy L. Young, CPA, CISA, CFE
Audit Manager

cc: Clark Seely, Assistant State Forester, Administrative Services Division
Marti-Lea Graham, Business Services Director
Pam Stroebel, Quality Assurance Director
Laurie Warner, Acting Director, Department of Administrative Services

Audit Findings and Recommendations Summary
Oregon Department of Forestry
State Fiscal Year 2004

REPORTABLE CONDITIONS

Controls Over Financial Accounting
During our audit, we found that the Department of Forestry (department) has not established adequate controls over key financial accounting functions. Without an adequate system of controls, the department is less able to effectively meet its business purpose.

For example, the department did not timely comply with Oregon Revised Statute (ORS) 530.115, which states that a portion of timber revenues will be paid to counties on or before the last day of each month following the end of the calendar quarter. During fiscal year 2004, approximately $48 million in timber revenues were owed to counties. Of this amount, the department did not transfer approximately $5.9 million to 9 of 12 counties timely. This situation existed because the department experienced a cash flow shortage and was forced to temporarily delay payments until the department was approved to take out a line of credit.

Significant weaknesses also exist in the department's cash handling, payroll, and accounts receivable processes. Details are in the following sections.

We recommend the State Forester make it a priority to establish a complete system of controls over the financial accounting functions by assigning the authority and responsibility to an individual or unit whose mission it is to align the department's financial activities. Those activities should include establishing and implementing policies and procedures department wide, and reporting and verification mechanisms to ensure policies and procedures are adhered to.

Internal Controls over Cash Handling
The department could improve its internal controls over cash. Specifically, we noted that some policies and procedures over cash and check stock were not implemented and desk manuals were limited in detail. The department did not have a process in place to replenish its petty cash or for making change. Furthermore, some assets were not protected (for example, checks were not restrictively endorsed and one check sent to the mailroom in the amount of $2,103 was lost), and checks were prepared without supporting documentation. We also noted inadequate segregation of duties over the request, approval and signing of checks. Finally, the department was unable to account for some missing cash receipts (A-receipts) and deposit slips used by the field offices.

The *Oregon Accounting Manual* (OAM 10.20.00.PR.101) states departments that collect state moneys should design and document internal controls for cash and the OAM (10.20.00.PR.123) states the department should have in place controls over cash receipts that include restrictively endorsing checks immediately upon receipt. Without an adequate system of controls over cash, the department is less able to meet its business objectives and is less able to identify and correct errors and omissions.

We recommend that department management:
1. Further develop, finalize, and implement policies and procedures over cash handling (i.e., check stock, petty cash, and change funds).
2. Update desk manuals on a regular basis and ensure they contain complete information.
3. Ensure checks are secured at all times.
4. Provide adequate segregation over the request, approval and signing of checks.
5. Ensure adequate supporting documentation is provided with each check preparation request.
6. Maintain a complete inventory on controlled items such as A-receipts and deposit slips.

Internal Controls over the Payroll Process

The department has significant weaknesses in its payroll processes. The OAM (45.07.00.PO.102) states that agencies must ensure the review and approval of the data that becomes the basis for and the documentation of payroll expenditures. Agency administration is responsible for ensuring that the policy is followed throughout the agency and alternate reviewers are designated for when supervisors are absent from work.

We reviewed internal controls over payroll and tested payroll transactions for regular and seasonal employees, as well as overtime payments, and identified the following:
- Life insurance codes for 99 employees did not correspond to the employee's correct age range. Per discussion with a Public Employees Benefit Board representative, since the correct premium was not deducted, in the event of a loss of life, the employee would not be insured.
- Public Employees Retirement System (PERS) contributions were made to employees that were ineligible as PERS members. Some of these employees were eligible for a 6 percent differential in lieu of the PERS contribution; however, the department paid both the differential and the contribution to 37 of these employees.
- Timesheets contained numerous manual corrections that were not supported.
- The department did not adequately document its reasons for providing additional compensation for employees who did not take the allowed 15-minute breaks.
- Units utilize different payroll timesheet formats.
- The department overpaid seasonal employees a total of $291 due to various errors.
- Some timesheets were not approved by a supervisor.
- The department did not pay a total of $354 in overtime payments due to various errors.
- One employee with unlimited payroll system update access also receives and distributes payroll checks to field office employees. This situation increases the opportunity for misappropriation of assets.
- One employee enters his own payroll data into the system without supervisory review.
- The department units were unable to demonstrate review of some system generated overtime exception reports.

As a result, the department is less able to ensure that payroll is complete, accurate and supported. As such, the department runs the risk that errors could go undetected and uncorrected in a timely manner resulting in a loss of state funds.

We recommend the department immediately correct:
1. Life insurance codes to ensure they correspond to the correct age range.

2. Payroll errors to ensure employees do not receive both the PERS contribution and a 6 percent differential.
3. Overpayments and underpayments identified during the audit.

We also recommend the department modify its payroll processes to ensure:

1. Codes for payroll deductions and contributions are correct and updated on a routine basis.
2. Management review and approval of timesheets.
3. Adequate documentation exists to substantiate the expenditure.
4. Adequate segregation of duties over payroll responsibilities
5. Unit managers review exception reports in a timely manner.

The department should also consider using standardized timesheets in all payroll units to help reduce errors.

Internal Controls over Accounts Receivable

During the audit, we noted that the department did not collect its accounts receivable in a timely manner nor did it charge interest on past-due accounts. The amount of interest that could have been collected for past-due accounts was approximately $67,000 as of June 30, 2004. We also identified one invoice in the amount of $5,810 that was approximately two years past due that agency staff were not seeking payment. Furthermore, many invoices reviewed required corrections and adjustments due to preparation errors, some of which were several months past due and have yet to be rebilled. Of $6.8 million in receivables for firefighting costs owed by individuals and owner-operators, the department collected less than $300,000 (less than 5 percent of the total due). The majority of these receivables have been outstanding between 2000 and 2004.

The OAM (35.20.20.PO.102) states that it is state policy to collect all receivables due to state agencies and to establish procedures to effect the timely collection of all amounts owed. The OAM (35.20.20.PR.102) states that the first step an agency must take to effectively collect its receivables is to have clear, written, top management supported internal procedures that will be used to bill and collect accounts receivable.

W**e recommend** the department:

1. Develop and implement clear, written, top management supported internal procedures governing accounts receivable that include:
   a. Management review of invoice preparation to better identify and correct errors timely.
   b. Follow up procedures when revenue is not received timely or when adjustments are needed to invoices.
   c. Ensure outstanding receivables are reviewed for uncollectibility and are written-off, if applicable.
2. Provide training for personnel for the timely collection of past due amounts.

Next Day Deposit Testing

Department management should improve controls over miscellaneous deposits to ensure compliance with the next day deposit exemption or state statute. During the fiscal year 2002 and 2003 audits, the department was out of compliance with the statute or exemption in 50 percent of sample items tested. During the fiscal year 2004 audit, the department was out of compliance with the statute or exemption in 40 percent of the sample items tested. We identified one field office that did not collect or deposit money for campground fees for a two-week period and also found that the Salem central office did not make timely deposits.

ORS 293.265 states that funds are to be deposited within one business day of receipt, although provisions exist to authorize exceptions for legitimate business reasons. The department requested an exemption to the next day deposit requirement for multiple district and field offices, which allows them to deposit funds within the time frame or dollar amount documented in the request. Districts that have not requested an exemption are required to follow the next business day timeline.

We recommend that management ensure all department offices are in compliance with the state statute and any exemption filed.

Inappropriate Use of State Funds

The department inappropriately used state funds when paying for moving expenses and for employee recognition or retirement parties.

According to state policy (HRSD 40.055.10) when the department relocates an employee to a new official workstation, the department will reimburse the employee for normal, reasonable moving and related expenses. In addition, the policy states that the new workstation must be at least 50 miles farther from the employee's former residence than the old workstation was from the same residence. For example, if the old workstation was three miles from the former residence, the new workstation must be at least 53 miles from the former residence in order for the employee to be reimbursed for moving and related expenses. The department's policy mirrors the state policy except for reimbursement rates.

According to the department's bargaining agreement, the department will reimburse for expenses related to packing, crating, and unpacking not to exceed $1,000 per move and will reimburse miscellaneous relocation expenses up to $5,000 whereas state policy only allows for reimbursement of $750 and $1,110, respectively.

During fiscal year 2004, the department paid $79,405 in moving expenses to 25 employees. Of those 25 employees, seven received more than $5,000, two of which received more than $10,000.

For example, we reviewed moving expenses for the following employees and question why the reimbursements described below were normal and reasonable:

- One employee was paid moving expenses totaling $6,872 to move 3 times during a 3-year period. In the first move, the employee was paid $1,130. Reimbursement included a washer, dryer and curtains and moved the individual approximately 23 miles closer to the new workstation. Five months later, although the employee did not qualify for moving expenses, the department paid this employee $742 in order to move an additional 21 miles closer to the same workstation. This amount included a new stove. Approximately 32 months later, the employee received moving expenses in the amount of $5,000 for realtor fees in order to move back near the original workstation. In each instance, the move did not meet the 50-mile distance requirement.

- A second employee was paid $7,232 to move to a new workstation. Included in this amount was $3,166 for closing costs.

We also identified numerous instances in which state funds were used to purchase items such as cakes, refreshments, decorations, and gift certificates for retirement parties. During the audit we noted at least two instances in which employee recognition or retirement parties were held during work hours and scheduled to last two or more hours. During fiscal year 2004, the department spent at least $5,428 that it recognized as employee recognition that included retirement gift certificates, decorations, and refreshments.

According to the OAM (10.40.10.PO.109), state funds must not be used to provide refreshments for voluntary social events such as agency sponsored retirement celebrations. The policy further restricts state funds from being used to provide retirement invitations, cards, gifts, and party favors. However, department policy states, for retirements the department will pay up to $200 for food and supplies for the function such as non-alcoholic beverages, cookies, cakes, hors d'oeuvres, invitations, decorations, plates, cups, and utensils. For a resignation the department will pay up to $100.

We recommend the department ensure state funds are spent for appropriate uses by:

1. Aligning the department relocation policy with the dollar amounts allowed in state policy.
2. Documenting how employee moving expenses paid by the department are normal and reasonable.
3. Considering voluntary employee contributions for retirement parties, decorations, and gifts.