

Office of the Secretary of State

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Secretary of State

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Audits Division

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February 4, 2008

Kris Kautz, Interim Director
Department of Administrative Services
155 Cottage St. NE, U20
Salem, OR 97301-3972

Dear Ms. Kautz:

We have completed the statewide single audit that included selected financial accounts and federal awards at the Department of Administrative Services (department) for the year ended June 30, 2007.

This audit work was not a comprehensive audit of the department. Instead, the audit work performed allowed us, in part, to achieve the following objectives: (1) express an opinion on whether the financial statements contained in the State of Oregon's Comprehensive Annual Financial Report were fairly presented, in all material respects, in conformity with generally accepted accounting principles; (2) determine whether the state's internal controls provided reasonable assurance of proper accounting, financial reporting, and legal compliance of transactions; (3) determine whether the state has complied with applicable legal requirements that may have a direct and material effect on the state's financial statements; and (4) determine whether the state has complied with provisions of contracts or grant agreements that could have a direct and material effect on each major federal program.

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

| <u>SFMA Account</u> | <u>Description</u> | <u>Audit Amount</u> |
|--|---|---------------------|
| <u>GAAP Fund 0001 – General Fund</u> | | |
| 1853 | Transfers Out to Oregon University System | \$380,346,741 |
| 0065 (Agency 999) | Unreconciled Deposit | 8,370,706 |
| 0070 (Agency 999) | Cash on Deposit with State Treasurer | 786,601,627 |
| <u>GAAP Fund 1105 – Educational Support Fund</u> | | |
| 0065 | Unreconciled Deposit | 1,023,067 |
| 0070 | Cash on Deposit with State Treasurer | 232,242,871 |

| | | |
|---|--------------------------------------|---------------|
| <u>GAAP Fund 1107 – Environmental Management Fund</u> | | |
| 1302 | Transfer in Lottery Proceeds | 93,601,906 |
| <u>GAAP Fund 1108 – Health and Social Services Fund</u> | | |
| 0065 | Unreconciled Deposit | 2,205,978 |
| 0070 | Cash on Deposit with State Treasurer | 141,718,991 |
| <u>GAAP Fund 1111 – Public Transportation Fund</u> | | |
| 1405 | Transfer to Counties | 116,050,885 |
| <u>GAAP Fund 1114 – Oregon Rainy Day Fund</u> | | |
| 0586 (Agency 999) | Due From Other Funds | 319,288,3680 |
| 1316 (Agency 999) | Transfer in from Dept of Revenue | 319,288,368 |
| <u>GAAP Fund 5001 – Central Services Fund</u> | | |
| 0852 | Buildings and Building Improvements | 268,545,637 |
| 0816 | Motor Vehicles | 74,178,519 |
| <u>GAAP Fund 8500 – Government Wide Reporting Fund</u> | | |
| 0967 | Net Pension Asset | 1,883,100,000 |
| 1276 | Bonds Payable – Current | 43,547,678 |
| 1714 | Bonds Payable – Noncurrent | 2,590,562,415 |

We also determined whether the department substantially complied with the federal requirements relevant to the following federal program:

| <u>CFDA Number</u> | <u>Program Name</u> | <u>Audit Amount</u> |
|--------------------|---------------------------|---------------------|
| 10.665 and 10.666 | Schools and Roads Cluster | \$149,384,331 |

In planning and performing our audit of the selected financial accounts at the department as of and for the year ended June 30, 2007, in accordance with auditing standards generally accepted in the United States of America, we considered the department’s internal control over financial reporting (internal control) as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements of the State of Oregon, but not for the purpose of expressing an opinion on the effectiveness of the department’s internal control. Accordingly, we do not express an opinion on the effectiveness of the department’s internal control.

Additionally, in planning and performing our audit, we considered the department’s internal control over compliance with the requirements that could have a direct and material effect on the federal program listed above in order to determine our auditing procedures for the purpose of expressing our opinion on compliance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the department’s internal control over compliance.

Our consideration of internal control was for the limited purpose described in the preceding paragraphs and would not necessarily identify all deficiencies in internal control. As discussed below, we identified a deficiency in internal control that we consider to be a significant deficiency.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements, or noncompliance with a type of compliance requirement of a federal program, on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles, such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control. We consider the following deficiency to be significant deficiency in internal control:

Timeliness of Identifying Construction Projects as Completed

During our testing of the Buildings and Building Improvements account, we reviewed transactions posted to the Statewide Financial Reporting Application (SFMA) during fiscal year 2007. In gaining an understanding of the accounting process, we noted that key entries into the accounting records are based upon information provided by the department's Facilities Division (Facilities) to the department's Operations Division (Operations).

In our review, we noted several instances in which final payments to vendors were made years before the project was identified as completed in SFMA. In some instances, final payments were made in May of 2003 and October of 2004, but the projects were not identified as completed in SFMA until fiscal year 2007. As a result, completed projects were misclassified on the state's financial statements as construction in progress rather than reclassified to the appropriate capital asset account.

In addition, accounting standards require that most capital assets, such as buildings and building improvements, be depreciated over their useful lives. The useful life of the asset begins when the project is substantially completed and the asset is placed into service. If projects are not reclassified to capital assets when they are completed, they will not be depreciated over the useful life of the asset, as required by accounting standards.

We recommend department management ensure that the Facilities Division communicates in a timely manner the completion of construction projects with the accounting staff in the Operations Division to assure proper financial reporting for capital assets. To facilitate this communication, the Facilities Division should periodically review the projects identified in SFMA as construction in progress and determine if that classification remains appropriate.

The significant deficiency, along with your response, will be included in our Statewide Single Audit Report for the fiscal year ended June 30, 2007. Including your response 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 be

accomplished only if the response to the significant deficiency includes the information specified by the federal requirement, and only if the response is received in time to be included in the audit report. The following information is required for the response:

- 1 Your agreement or disagreement with the finding. If you do not agree with the 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 significant deficiency, please respond by February 13, 2008.

This communication is intended solely for the information and use of management and others within the organization, and is not intended to be and should not be used by anyone other than the specified parties.

Should you have any questions, please contact Geoff Hill or me at (503) 986-2255.

Sincerely,
OREGON AUDITS DIVISION

Julianne Kennedy, CPA
Audit Manager

JK:brk

cc: Bret West, Operations Division Administrator
Joy Sebastian, Deputy State Controller
Pam Stroebel-Valencia, Internal Audit