

Office of the Secretary of State

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Audits Division

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February 10, 2009

Marvin Brown, State Forester
Oregon Department of Forestry
2600 State Street
Salem, Oregon 97301

Dear Mr. Brown:

We have completed audit work of selected financial accounts at the Oregon Department of Forestry (department) for the year ended June 30, 2008.

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; and (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.

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>Special Revenue Fund – Environmental Management (GAAP Fund 1107)</u>		
0065	Unreconciled Deposit	\$13,804,993
0070	Cash on Deposit with Treasurer	20,849,681
0703	State Forest Lands	83,683,946
1405	Transfers to Counties	51,170,294
3111	Regular Employees	24,305,894
3221	Social Security Taxes	2,625,335
3263	Medical, Dental, Life Insurance	8,179,258
4xxx	Various Services and Supplies	49,757,294

In planning and performing our audit of the selected financial accounts at the department as of and for the year ended June 30, 2008, 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.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control. 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 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 a significant deficiency in internal control:

Inconsistency in Accounting for State Forest Lands Revenue

To communicate effective information, financial reporting must be consistent, including the use of the same reporting method for all similar transactions. The department accounted for State Forest Lands revenue inconsistently during fiscal year 2008.

The timber sales contract amounts are based on the net of gross timber sale value less estimated project work costs. Project work is work needed to be done by the contractor to access the timber for harvesting; this work mostly consists of road construction and road improvements. Historically, the department has reported State Forest Lands revenue from these contracts on a net basis. In June 2007, a legislative bill required transfers to counties during the 2007-09 biennium of additional revenue to offset a portion of project work costs on timber sales. In association with the required transfers, the department recognized the revenue on a gross basis by recognizing the associated project work costs. Consequently, department management reported a portion of the State Forest Lands revenue on a gross basis (total forest sales value), but reported the remaining portion on a net basis (total forest sales value less project work costs). This resulted in total revenue being understated by approximately \$3.1 million.

We recommend department management ensure State Forest Lands revenue be reported consistently for financial statement purposes.

This significant deficiency, along with your response, will be included in our Statewide Single Audit Report For the Fiscal Year Ended June 30, 2008. Including your response satisfies the federal requirement that management prepare a Corrective Action Plan covering all reported audit findings. Satisfying the federal requirement in this manner, however, can only be accomplished 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.

Please respond by February 20, 2009.

Additionally, in the prior fiscal year, two significant deficiencies were reported to you in a letter dated February 6, 2008. The first deficiency related to the department recording services and supplies expenditures for facilities maintenance, totaling approximately \$1.9 million, for which no goods or services were received. This finding can also be found in the Statewide Single Audit Report for the fiscal year ended June 30, 2007, see Secretary of State Audit Report number 2008-03, finding number 07-5. During the current fiscal year, the department again recorded services and supplies expenditures for facilities maintenance, totaling approximately \$772,500, for which no goods or services were received.

The second deficiency related to the department having an incomplete risk assessment process. The department had developed a risk assessment that identified risks throughout the department, including risks that affect financial reporting. However, department management had not developed a plan to manage the risks identified. This finding can also be found in the Statewide Single Audit Report for fiscal year ended June 30, 2007. See Secretary of State Audit Report number 2008-03, finding number 07-6. During the current fiscal year, the department had yet to develop and implement a plan to manage risks identified for financial reporting. Having a complete risk assessment process is fundamental to ensuring management has implemented an adequate system of internal controls over financial reporting.

Both of the prior fiscal year findings will be reported in the Statewide Single Audit Report for the fiscal year ended June 30, 2008, with a status of No Corrective Action Taken.

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This communication is intended solely for the information and use of management, others within the organization, and the Board of Forestry, 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 Diane Farris or me at (503) 986-2255.

Sincerely,
OREGON AUDITS DIVISION

Julianne Kennedy, CPA
Audit Manager

JK:brk

cc: Clark Seely, Associate State Forester, Administrative Services Division
Mark Hubbard, Business Services Director
David Clouse, Quality Assurance Program Director
John Blackwell, Chair, Board of Forestry
Scott Harra, Director, Department of Administrative Services