

Office of the Secretary of State

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February 4, 2010

Susan Castillo, Superintendent of Public Instruction
Department of Education
255 Capitol St. NE, Suite 200
Salem, OR 97310

Dear Ms. Castillo:

We have completed audit work of selected financial accounts at the Department of Education (department) for the year ended June 30, 2009.

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.

In planning and performing our audit of the selected financial accounts at the department as of and for the year ended June 30, 2009, 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.

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

SFMA Account	Description	Audit Amount Debit (Credit)
<u>GAAP Fund 0001 – General Fund</u>		
6200	General Fund/Other Fund Transfer	\$2,523,985,594
<u>GAAP Fund 1105 – Educational Support Fund</u>		
0300	Federal Revenue	(392,802,699)
6600	Distribution to Local School Districts	3,251,427,755
1306	Transfers in from Department of Administrative Services	(352,410,681)
1211	Vouchers Payable	(53,751,877)
<u>GAAP Fund 1109 – Nutritional Support Fund</u>		
0300	Federal Revenue	(145,447,294)

Our consideration of internal control was for the limited purpose described above 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 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.

Year End Accruals

Generally accepted accounting principles require that revenues be recognized when the underlying expenditures have occurred. The Oregon Accounting Manual clarifies that revenues received within 90 days of fiscal year-end for expenditures that occurred during the year should be recognized in the year in which the expenditures occurred.

While the department continues to improve its process for accruing revenues and expenditures, our testing of the fiscal year 2009 accruals found that the department’s estimates were still significantly different from actual revenues and expenditures for the accrual period. In addition, some revenue accruals were posted to an incorrect fund. As a result, revenue for fiscal year 2009 was understated by approximately \$10 million in the Educational Support Fund and overstated by \$5 million in the Nutritional Support Fund. Expenditures were understated by approximately

\$11 million in the Educational Support Fund and by \$3 million in the Nutritional Support Fund. We reported a similar finding for the prior two audit periods.

We Recommend department management ensure that year-end accruals are reasonably estimated in conformance with generally accepted accounting principles and posted to the proper fund.

Prior Audit Findings

In the prior two fiscal years, significant deficiencies related to year-end accruals were reported to you in letters dated February 7, 2008, and February 9, 2009. Those findings were also included in the Statewide Single Audit Reports for the Fiscal Years Ended June 30, 2007, and 2008; See Secretary of State Audit Report number 2008-03 (finding number 07-20) and 2009-07 (finding numbers 07-20 and 08-9). During the current fiscal year, the department made progress in correcting these findings. The prior findings will be reported in the Statewide Single Audit Report for the Fiscal Year Ended June 30, 2009, with a status of partial corrective action taken.

Last year we also reported a significant deficiency related to employee fraud at the department (finding 08-8). During the current fiscal year, the department made progress in implementing procedures to address this deficiency. This prior finding will be reported in the Statewide Single Audit Report for the Fiscal Year Ended June 30, 2009, with a status of partial corrective action taken.

The significant deficiency, along with your response, will be included in our Statewide Single Audit Report for the Fiscal Year Ended June 30, 2009. 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 of the contact person responsible for corrective action.

Please respond by February 19, 2010. We will follow up on the department's progress in addressing these issues during the next fiscal year audit.

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

We would like to express our appreciation to your staff for their assistance and cooperation during the conduct of the audit. Should you have any questions, please contact Mark Winter or me at (503) 986-2255.

Sincerely,
OREGON AUDITS DIVISION

Julianne Kennedy, CPA
Audit Manager

JK:sms

cc: Sue MacGlashan, Assistant Superintendent, Office of Finance and Administration
Tomas Flores, Accounting Services Director
Duncan Wyse, Chair, Board of Education
Ed Dennis, Chair, Audit Committee
Scott Harra, Director, Department of Administrative Services