

# Secretary of State Audit Report

Jeanne P. Atkins, Secretary of State

Gary Blackmer, Director, Audits Division



## Keeping the State of Oregon Accountable, Fiscal Year 2014

As the state's independent auditors, every year we audit the State of Oregon's financial statements. Among the billions of dollars of transactions, each year we find errors amounting to millions of dollars due to incorrect coding of financial transactions or misinterpretation of Generally Accepted Accounting Principles (GAAP). We propose adjustments to correct errors and we report findings with recommendations to strengthen controls.



The Departments of Education, Administrative Services, and Human Services/Oregon Health Authority reduced the dollar amount of errors requiring audit adjustments this year, while some other agencies showed increases in the amount of errors. Overall, this year's audit results showed improvement over last year. While the improvements shown may reflect increased efforts by some agency management to implement better controls over accuracy, we have found that diligence is required to ensure accuracy of accounting records continues to improve.

Our annual financial audit provides the state with our professional opinion about the completeness, accuracy and validity of the state's accounting information. Accurate and reliable accounting data is crucial to ensuring state dollars are properly spent and provides a starting point for the next budget cycle. State agencies use financial data to create budget requests for the Oregon Legislature to allocate the state's resources. Without an accurate accounting of the revenues, expenditures, assets and liabilities of the state, the Legislature doesn't have correct information to budget for the future.

Our services also include audits of the state's administration of major federal programs that provide billions of dollars in federal revenue to the State of Oregon. Every year, our audit results show state agencies are out of compliance with federal requirements because the agencies' controls are not adequate to administer federal programs in accordance with federal requirements. The common errors we find in federal program compliance often continue from year to year and are slow to be resolved.

For more information about audit results, see the reports listed on our website:

Oregon's Financial Statements:

<http://sos.oregon.gov/audits/Documents/2014-32.pdf>

Single Audit (including Federal Compliance) Results:

<http://sos.oregon.gov/audits/Documents/2015-05post.pdf>

## Summary of the Financial Statement Audit

We reported 11 weaknesses related to internal controls over financial reporting for the fiscal year ended June 30, 2014 and 7 weaknesses from prior years that remained uncorrected. We proposed 26 audit adjustments at nine state agencies to correct about \$200 million in financial reporting errors. The proposed adjustments affected 55 different financial statement accounts, with five accounts requiring adjustments of at least \$30 million. This year shows improvement over last year when we reported twice as many weaknesses in internal control and several more adjustments that accounted for \$1 billion in misstatements.

Last year we reported that some agencies appear to rely on auditors to identify mistakes that should be detected by the agency's control processes. Improvements were noted at a few agencies; for example, management at the Department of Human Services and Oregon Health Authority initiated training this year for financial services staff to better understand the proper application of GAAP. In particular, they implemented procedures to report expenditures in the appropriate year, which resulted in fewer audit adjustments for their agencies. Although there is noticeable improvement, over half of the adjustments proposed for the state's financial statements were to correct errors in the Department of Human Services and Oregon Health Authority financial information.

We issued an unmodified opinion on the state's financial statements. An unmodified opinion means the state's financial statements, as corrected, are fairly presented in conformance with GAAP. Figure 1 presents a summary of the state's financial statements for fiscal year 2014.

**Figure 1: Condensed Statement of Net Position and Activities, Fiscal Year 2014**

<b>Condensed Statement of Net Position</b>		<b>Condensed Statement of Activities</b>	
Governmental and Business-type Activities		Governmental and Business-type Activities	
As of June 30, 2014 (in millions)		For the fiscal year ended June 30, 2014 (in millions)	
<b>Assets</b>		<b>Program Revenues</b>	
Cash and Investments	\$ 10,764	Governmental activities	\$ 10,578
Receivables	5,910	Business-type activities	5,608
Capital assets, net of depreciation	16,287	<b>General Revenues</b>	
Other assets	1,637	Governmental activities	9,654
Total Assets	<u>34,598</u>	Business-type activities	(115)
<b>Deferred Outflows</b>	<u>93</u>	Total revenues	<u>25,725</u>
<b>Liabilities</b>		<b>Expenses</b>	
Long-term debt	12,607	Governmental activities	19,678
Other liabilities	4,042	Business-type activities	4,857
Total liabilities	<u>16,649</u>	Total expenses	<u>24,535</u>
<b>Deferred Inflows</b>	<u>6</u>	Increase in Net Position	1,190
<b>Net Assets</b>		Net Position - beginning	<u>16,845</u>
Invested in capital assets, net of related debt	11,425	Net Position - ending	<u>\$18,035</u>
Restricted	4,074		
Unrestricted	2,536		
Total Net Position	<u>\$18,035</u>		

## Summary of the Single Audit

### ***Significant control weaknesses identified in multiple federal programs***

We audited 20 federal programs representing \$8.5 billion in federal funds to determine if the state was compliant with federal program requirements.

We found the Department of Human Services and Oregon Health Authority did not establish adequate internal controls and were not materially compliant with federal requirements for three programs: Foster Care, Adoption Assistance, and Medicaid. We issued qualified opinions on these three programs in fiscal year 2014.

A program receives a qualified opinion if we find a department's internal controls will not reasonably prevent or detect significant noncompliance in a timely manner. For these programs, we identified control weaknesses and noncompliance in the areas of allowable activities/costs, eligibility, period of availability, reporting, and special tests and provisions.

Figure 2 presents federal programs with qualified opinions over the last five years.

**Figure 2: Federal Programs with Qualified Opinions**

<b>Federal Program</b>	<b>2010</b>	<b>2011</b>	<b>2012</b>	<b>2013</b>	<b>2014</b>
Medicaid	X	X		X	X
Foster Care			X	X	X
Adoption Assistance				X	X
Temporary Assistance for Needy Families	X	X		X	
Low Income Home Energy Assistance		X	X	X	
Child Nutrition			X		
Child and Adult Care Food			X		
Community Services Block Grant	X	X	X		
Weatherization Assistance		X	X		
Children's Health Insurance Program	X				

### **Federal findings**

For fiscal year 2014, we questioned whether Oregon's spending of approximately \$450,000 was appropriate under federal program rules and we issued 42 findings related to 17 audited federal programs at eight state agencies. Programs with findings are generally considered high-risk and require an audit in the following year. Of the 20 programs we audited this year, 16 will have to be re-audited next year just to follow up on whether findings are corrected.

Figure 3 provides details on programs audited and number of findings identified for each program. As shown in figure 4, we audited more programs and identified more findings at the Department of Human Services.

**Figure 3: 2014 Findings by Audited Federal Program**

<b>Federal Program</b>	<b>2014 Findings</b>	<b>Federal Program Expenditures</b>
Medicaid*	8	\$ 4,831,713,091
Temporary Assistance for Needy Families*	6	162,458,931
Foster Care Title IV-E*	6	80,752,932
Supplemental Nutrition Program*	5	1,254,565,477
Child Care and Development Fund*	5	73,551,418
Adoption Assistance*	5	27,037,701
Child Nutrition*	3	159,638,698
Immunization Grants*	3	42,608,756
Low-Income Home Energy Assistance*	3	35,016,252
Children's Health Insurance Program*	2	214,192,030
Title I*	2	144,269,779
Special Education*	2	120,427,751
Child Support Enforcement	2	48,662,615
Fire Management Assistance	2	40,226,983
Unemployment Insurance	1	896,141,920
Child and Adult Care Food*	1	33,430,639
Workforce Investment Act	1	31,357,871
Research and Development	0	252,394,495
Vocational Rehabilitation	0	47,710,942
Disaster Grants	0	10,592,573
		<b>\$ 8,506,750,855</b>

\*Some findings pertain to multiple programs and therefore are counted more than once

**Figure 4: 2014 Findings & Questioned Costs by State Agency**

State Agency	Programs Audited <sup>1</sup>	2014 Findings	Questioned Costs <sup>2</sup>
Department of Human Services*	7	19	\$ 326,038
Department of Education	5	9	122,977
Oregon Health Authority*	3	8	742
Oregon Housing Department	1	3	-
Department of Justice	1	2	-
Department of Forestry	1	2	1,518
Employment Department	1	1	-
Community Colleges and Workforce Development	1	1	-
Oregon Military Department	1	0	-
Commission for the Blind	1	0	-
Oregon University System	1	0	-
			\$ 451,275

<sup>1</sup>Some programs are audited at more than one agency and therefore are counted more than once

<sup>2</sup>Auditors are not always able to determine questioned costs. Questioned costs may exist that we could not quantify due to lack of controls

\*Some findings pertain to multiple agencies and therefore are counted more than once

### **Finding history**

Of particular concern is the number of findings that continue to be uncorrected year after year. Figure 5 illustrates compliance requirements that have had control weaknesses or noncompliance for several years. The Department of Human Services is responsible for most of the weaknesses that remain uncorrected. This may not be surprising as the department is responsible for administering many large federal programs. The programs with uncorrected weaknesses at the Department of Human Services represent \$2.8 of the \$10.6 billion received by the state and affect the following large programs: Foster Care, Adoption Assistance, Temporary Assistance for Needy Families, Supplemental Nutrition Assistance, and some portions of Medicaid. The size of these programs underscores why it is important to correct these weaknesses so they don't continue from one year to the next. Figure 5 shows the types of federal requirements that tend to have findings that carry forward from one year to the next.

**Figure 5: Findings History by Type of Compliance Requirement\***

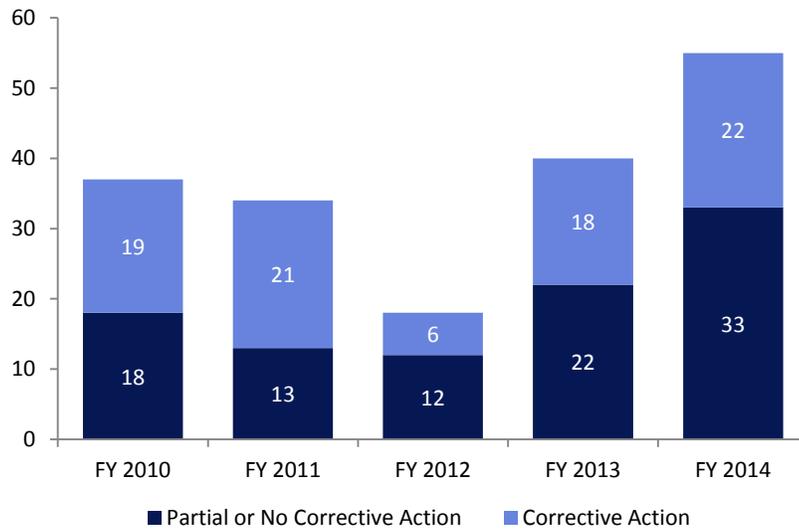
Compliance Requirement	2010	2011	2012	2013	2014	Total
Activities Allowed or Unallowed	0	0	3	3	4	10
Allowable Costs/Cost Principles	2	3	12	5	4	26
Cash Management	2	1	1	2	2	8
Eligibility	5	2	5	9	5	26
Equipment	0	0	1	0	0	1
Matching, Level of Effort, Earmarking	1	0	1	2	3	7
Period of Availability	0	0	0	2	3	5
Procurement, Suspension, & Debarment	2	1	3	0	1	7
Reporting	3	2	5	9	10	29
Subrecipient Monitoring	4	1	5	2	5	17
Special Tests and Provisions	1	1	7	8	9	26

\*Some findings pertain to multiple requirements and therefore are counted more than once.

### **Corrective action taken on federal findings**

Audit findings include recommendations that address noncompliance and internal control weaknesses. In response to audit findings and recommendations, state agencies must design a corrective action plan to submit to the federal granting agency. Federal agencies issue a decision on the findings including the questioned costs the state will be required to repay. During future audit periods, we are required to determine whether agencies have taken corrective, partial, or no action. In fiscal year 2014, we reported on the status of 33 findings from prior years because they remained uncorrected at the end of the fiscal year. The number of uncorrected prior year findings increased by 50% from fiscal year 2013. Historically, many findings remain uncorrected from one year to the next because the agencies don't correct the underlying issues leading to noncompliance or control weaknesses. When a finding is not corrected, we must re-issue the finding the next year. Figure 6 presents the action taken over the last five years on prior year findings that remained uncorrected at the end of each the fiscal years shown.

**Figure 6: Action Taken on Prior Year Uncorrected Federal Findings**



## Background and Statistics

Specific procedures, prescribed by the Federal Office of Management and Budget (OMB), are used to determine the federal programs selected for audit each year. High risk programs are required to be audited, which includes programs with prior year findings, and large expenditure programs that have not been audited in the most recent two years. At least 50% of total federal expenditures are required to be audited each year. However, due to internal control and compliance weaknesses, auditors had to increase that coverage for fiscal year 2014 to 74% of the state's total federal expenditures in order to meet audit requirements set by the OMB. Figure 7 below shows the five-year history of audited programs. Programs audited in consecutive years were due to weaknesses identified in a prior year. When agencies do not correct program weaknesses, we are required to re-audit the program, resulting in diverting audit efforts from other areas that warrant attention.

**Figure 7: Program Audit History**

Federal Program	2010	2011	2012	2013	2014
Medicaid <sup>1</sup>	X	X	X	X	X
Unemployment Insurance <sup>2</sup>	X	X	X	X	X
Temporary Assistance for Needy Families <sup>2</sup>	X	X	X	X	X
Low-Income Home Energy Assistance <sup>2</sup>	X	X	X	X	X
Supplemental Nutrition Assistance <sup>2</sup>	X	X	X	X	X
Foster Care <sup>2</sup>			X	X	X
Child Nutrition <sup>2</sup>			X	X	X
Child and Adult Care Food <sup>2</sup>			X	X	X
Child Support Enforcement <sup>2</sup>	X			X	X
Adoption Assistance <sup>2</sup>	X			X	X
Immunization Grants <sup>2</sup>	X			X	X
Disaster Grants <sup>2</sup>				X	X
Title I Grants <sup>3</sup>	X	X			X
Vocational Rehabilitation <sup>3</sup>	X	X			X
State Children's Insurance Program <sup>3</sup>	X	X			X
Workforce Investment Act <sup>3</sup>	X	X			X
Special Education <sup>3</sup>	X	X			X
Child Care and Development <sup>3</sup>	X	X			X
Research and Development <sup>3</sup>	X	X			X
Fire Management Assistance					X
Military Operations and Maintenance			X	X	
State Grants for ACA Exchanges			X	X	
Highway Planning and Construction	X			X	
Community Services Block Grant	X	X	X	X	
Weatherization Assistance	X	X	X		

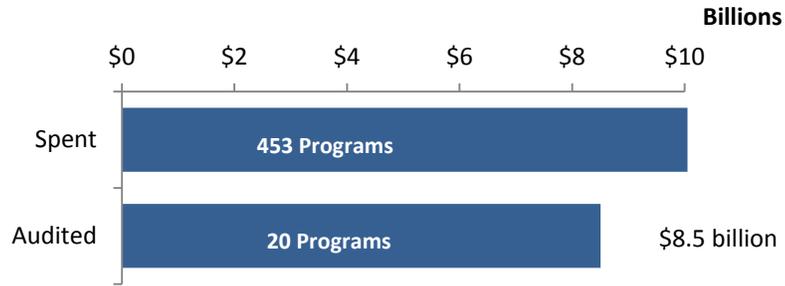
<sup>1</sup>Medicaid is noted as high-risk by the federal government, and requires audit each year, regardless of status of findings; however, Medicaid has had findings every year for the years displayed.

<sup>2</sup>Program considered high-risk in FY2014 due to uncorrected weaknesses in prior year

<sup>3</sup>Program considered high-risk in FY2014 due amount of expenditures, and not audited in prior two years

In fiscal year 2014 Oregon spent approximately \$10.6 billion in federal cash and noncash assistance (such as immunization vaccines and food) for 453 programs administered by 45 state agencies. We selected 20 programs to audit that are considered to be at the highest risk of misusing funds; 11 of those programs were determined high risk due to uncorrected findings identified in prior years. The 20 audited programs were administered by 9 state agencies and totaled \$8.5 billion in federal funds.

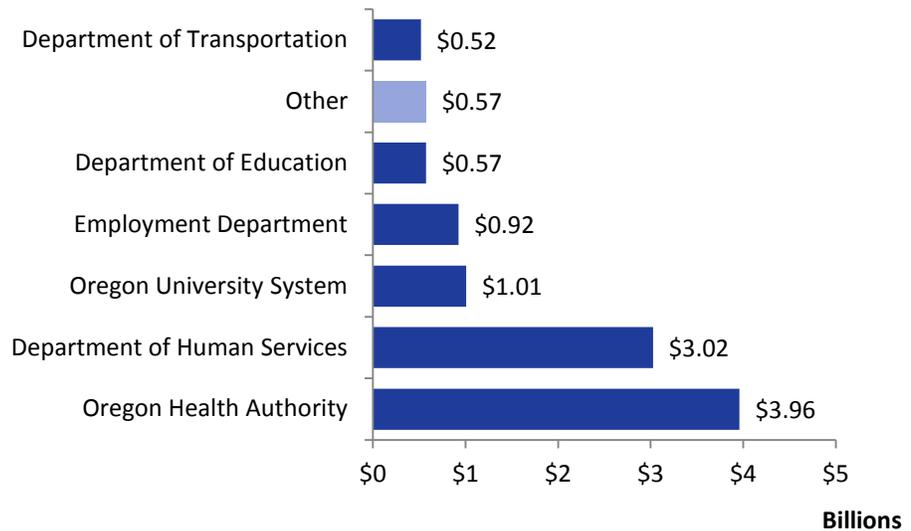
**Figure 8: Coverage of Fiscal Year 2014 Single Audit**



***Federal expenditures by state agency for fiscal year 2014***

Federal funds were expended by 45 state agencies during fiscal year 2014. Six of the 45 agencies accounted for \$10 billion or 95% of federal expenditures. The Department of Human Services and the Oregon Health Authority began operating as two separate agencies during fiscal year 2012. However, many of their functions are performed by a shared services arrangement; combined, the two agencies accounted for \$7 billion, or 66%, of federal expenditures.

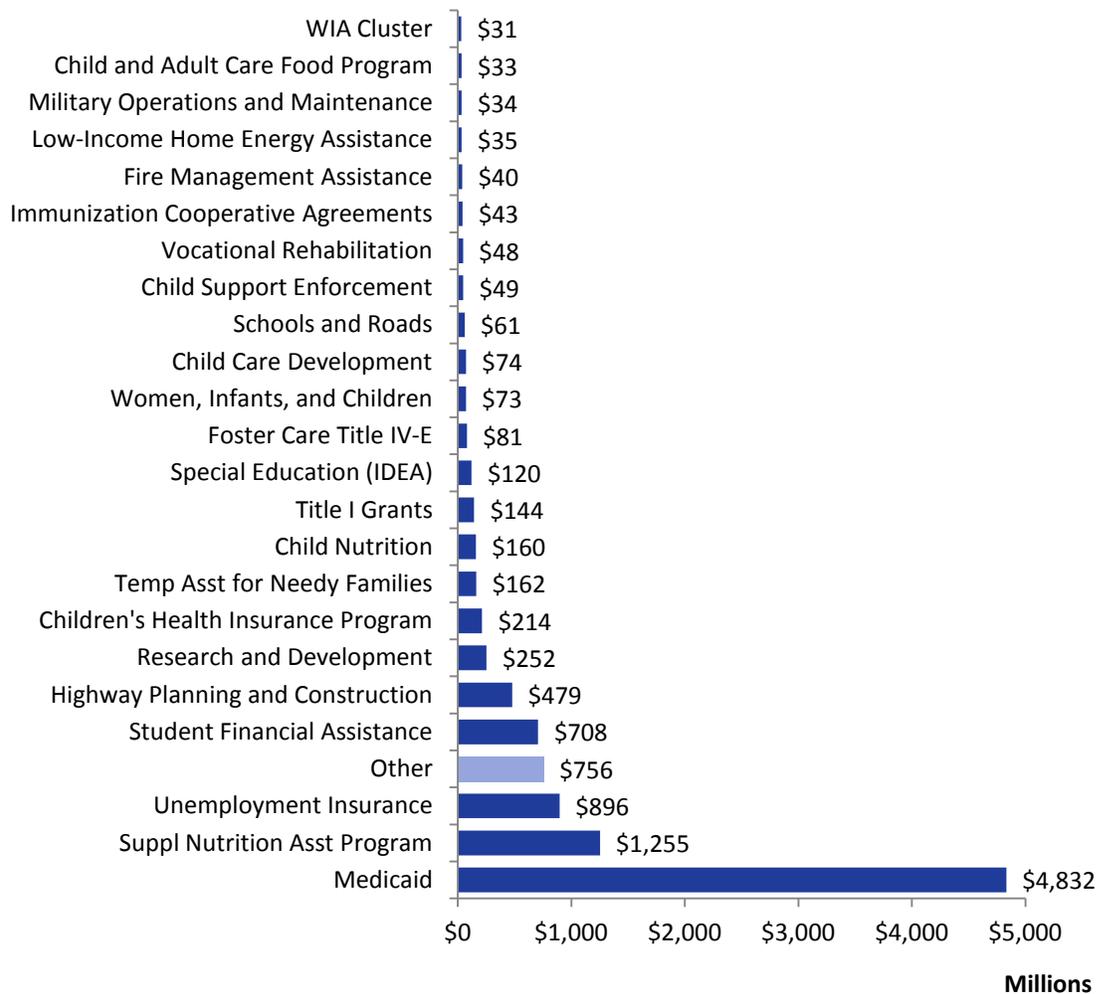
**Figure 9: Total Federal Expenditures by State Agency, Fiscal Year 2014**



**Federal expenditures by federal program for fiscal year 2014**

Twenty-three of the 453 federal programs administered by the State of Oregon accounted for 93% of the state’s total federal expenditures in fiscal year 2014. Federal expenditures for the Medicaid program alone were \$4.8 billion or 46% of total federal expenditures. The Other category, shown in figure 10, combines 430 federal programs, each with expenditures less than \$30 million.

**Figure 10: Total Federal Expenditures by Federal Program, Fiscal Year 2014**



## Authority, Purpose, and Scope

The State of Oregon's management is responsible for preparing annual financial statements, preparing a schedule of expenditures of federal awards, maintaining effective internal controls, and being accountable to the citizens of Oregon for its use of public monies.

The financial statements provide a comprehensive view of the state's financial activities during the fiscal year (Statement of Activities) and an overall picture of the state's financial position at the end of the fiscal year (Statement of Net Position). The management of each state agency is responsible for maintaining effective internal controls over financial reporting and ensuring financial information is complete and accurate. Statewide Accounting and Reporting Services (SARS), part of the Department of Administrative Services, is responsible for preparing the state's financial statements in accordance with Generally Accepted Accounting Principles, which are numerous and complex. SARS prepares the financial statements by providing guidance and training to agency staff throughout the year, compiling financial information from more than 100 state agencies, and making numerous accounting adjustments to ensure amounts are properly reported.

The Secretary of State Audits Division is responsible for expressing opinions on the state's financial statements. We conduct our work following *Government Auditing Standards* applicable to financial audits, which require that we plan and perform the work to obtain reasonable assurance about whether the financial statements are materially correct. The work includes examining evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by state management, as well as evaluating whether the financial statements are presented properly. The Audits Division audits the state's financial statements, schedule of federal awards, and major federal programs on an annual basis. We conduct the annual statewide Single Audit, which is required by the federal government for Oregon to continue to receive federal financial assistance. The purpose of the fiscal year 2014 audit was to:

- Determine if the amounts reported in the State of Oregon's financial statements were materially correct and adequately supported;
- Review internal accounting and compliance control procedures;
- Determine whether the Schedule of Expenditures of Federal Awards (SEFA) is presented fairly in relation to the state's financial statements; and
- Evaluate the state's major federal programs for compliance with applicable laws, rules, and regulations.

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## About the Secretary of State Audits Division

The Oregon Constitution provides that the Secretary of State shall be, by virtue of her office, Auditor of Public Accounts. The Audits Division exists to carry out this duty. The division reports to the elected Secretary of State and is independent of other state agencies within the Executive, Legislative, and Judicial branches of Oregon government. The division audits all state officers, agencies, boards, and commissions and oversees audits and financial reporting for local governments.

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### Audit Team

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This report, a public record, is intended to promote the best possible management of public resources. Copies may be obtained from:

website: [sos.oregon.gov/audits](http://sos.oregon.gov/audits)

phone: 503-986-2255

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The courtesies and cooperation extended by officials and employees of the State of Oregon during the course of the Statewide Single Audit for fiscal year 2014 were commendable and sincerely appreciated.