

Office of the Secretary of State

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Audits Division

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February 3, 2014

Rob Saxton, Deputy Superintendent
Department of Education
255 Capitol St. NE, Suite 200
Salem, OR 97310

Dear Mr. Saxton:

We have completed audit work of selected financial accounts at your department for the year ended June 30, 2013. This audit work was not a comprehensive financial audit of the department, but was performed as part of our annual audit of the State of Oregon's financial statements. We audited accounts that we determined to be material to the State of Oregon's financial statements.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements of the State of Oregon as of and for the year ended June 30, 2013, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, we considered the department's internal control over financial reporting as a basis for designing auditing procedures that are appropriate in the circumstances 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.

A deficiency in internal control 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 and correct, misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A significant deficiency is a deficiency, or combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit the attention of those charged with governance.

Our consideration of internal control was for the limited purpose described above and was not designed to identify all deficiencies in internal control that might be *material weaknesses or significant deficiencies*, and therefore, *material weaknesses or significant deficiencies* may exist that have not been identified. However, as discussed below, we identified a deficiency in internal control that we consider to be a *significant deficiency*.

Significant Deficiency

Review Accrual Processes

According to the Oregon Accounting Manual, and in compliance with generally accepted accounting principles, expenditures are subject to accrual if they are expected to be paid within 90 days after fiscal year-end. Additionally, revenues received within 90 days of fiscal year-end for expenditures that occurred during the fiscal year should be recognized in the year in which the expenditures occurred.

The Department has a process at year-end to identify and accrue revenue and expenditures in the proper period. Part of the process includes preparing, for select expenditures, a post-close adjustment for reimbursement requests received from school districts after the close of the fiscal year-end. The department may also update the prior year post close amount as part of this process based on availability of additional information. During our review of the department's process for multiple accounts, we identified the following:

- The department does not evaluate and prepare a post close adjustment for all of its significant expenditure accounts. As a result, in the General Fund, the department did not accrue \$5.2 million of distributions to local school districts.
- Subsequent to audit, the department updated a fiscal year 2012 post close entry for a distribution to local school districts account in the Education Support Fund. The department's update caused the fiscal year 2013 account to be understated \$1.2 million.

Additionally, based on a prior year audit recommendation, the department made adjustments in fiscal year 2013 to ensure federal revenue accruals at the grant level would be correct. When making the adjustments, the department did not make the related adjustment to accounts receivable. As a result, accounts receivable was overstated \$40 million in the Education Support Fund.

We recommend department management review the accrual process and incorporate assessments of all significant accounts when determining whether post-close adjustments should be made to record transactions in the correct period. We also recommend the department not update the prior year post close adjustment unless it was determined to be materially incorrect. Finally, we also recommend management ensure its accrual process includes appropriate adjustments to accounts receivable to ensure the balance is correct in the next fiscal year.

The above significant deficiency, along with your response, will be included in our Statewide Single Audit Report for the fiscal year ended June 30, 2013. Please prepare a response to the finding and include the following information as part of your corrective action plan:

- 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 11, 2014.

Rob Saxton, Deputy Superintendent
Department of Education
Page 3

The purpose of this letter is solely to describe the scope of our testing of internal control and the result of that testing, and not to provide an opinion on the effectiveness of the department's internal control. This communication is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the department's internal control. Accordingly, this letter is not suitable for any other purpose.

We appreciate your staff's assistance and cooperation during this audit. Should you have any questions, please contact Michelle Searfus or me at (503) 986-2255.

Sincerely,
OREGON AUDITS DIVISION

Kelly L. Olson, CPA
Audit Manager

KLO:MNS:jas

cc: Susan MacGlashan, Assistant Superintendent, Office of Finance and Administration
Tomas Flores, Financial Services Director
Jim Scott, Internal Auditor
Samuel Henry, Chair, Oregon State Board of Education
Michael J. Jordan, Director, Department of Administrative Services