

The background of the top half of the cover features a large, light blue, semi-transparent seal of the State of Oregon. The seal is circular, with the words "STATE OF OREGON" around the top and "1859" at the bottom. Inside the seal is an eagle with spread wings perched on a shield. The shield depicts a landscape with a ship on the left, a sun rising over mountains in the center, and a plow on the right. A banner across the shield reads "THE UNION".

State of Oregon

# Keeping the State of Oregon Accountable, Fiscal Year 2016

Secretary of State  
**Dennis Richardson**

Audits Division, Director  
**Kip Memmott**

Report 2017 – 12  
July 2017

# Secretary of State Audit Report

Dennis Richardson, Secretary of State

Kip Memmott, Director, Audits Division



## Keeping the State of Oregon Accountable, Fiscal Year 2016

### Purpose

*We are the state's  
independent auditors*

Every year the Secretary of State Audits Division audits the State of Oregon's financial statements and the state's compliance with federal program requirements. These audits are required for Oregon to continue receiving approximately \$11.5 billion in federal financial assistance. The results of these annual audits are included in the State's Comprehensive Annual Financial Report and in the annual Statewide Single Audit Report. This report is a summary report of the audit results of the fiscal year 2016 financial and federal annual audits. The annual financial and federal reports are available on our website. See

<http://sos.oregon.gov/audits/Documents/2016-37.pdf> and  
<http://sos.oregon.gov/audits/Documents/2017-08.pdf>

### Results

#### *Audit of the State of Oregon's Financial Statements*

- We found \$690 million in accounting errors and proposed adjustments to correct these errors in the state's financial statements.
- We wrote 16 recommendations for improvements to standard controls used to ensure the accuracy of financial information.
- The accounting errors and recommendations increased compared to the results of last year's financial audit.

#### *Audits of Compliance with Federal Program Requirements*

- We wrote 23 findings related to 12 audited federal programs at nine state agencies.
- We issued "qualified" opinions on two programs, Foster Care and the Child Care and Development Fund. A qualified opinion indicates the department's internal controls are inadequate to prevent or detect significant noncompliance in a timely manner.
- Unresolved findings from prior years continue to require auditing efforts beyond normal federal requirements. While Medicaid is required to be audited each year, five of the remaining 11 programs audited in fiscal year 2016 were required to be audited again in 2016 due to material weaknesses identified in the prior year.

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## Background

### Annual Reporting

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

The financial statements provide a comprehensive view of the state's financial activities during the fiscal year (Statement of Activities), an overall picture of the state's financial position at the end of the fiscal year, (Statement of Net Position), and a summary of the state's federal program expenditures (Schedule of Expenditures of Federal Awards) that occurred during the fiscal year. 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, 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.

### Annual Audits

The Secretary of State Audits Division audits the state's financial statements, schedule of federal awards, and major federal programs on an annual basis. We conduct our work following *Government Auditing Standards* applicable to financial audits, which require that we plan and perform audit work to obtain reasonable assurance about whether the financial statements are materially correct. We conduct the annual statewide Single Audit, which is required by the federal government, for Oregon to continue to receive federal financial assistance. We audit federal programs to ensure state agencies are administering federal programs in accordance with federal requirements.

The purpose of the fiscal year 2016 audits were 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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## Financial Statement Audit – Fiscal Year 2016 Results

This annual audit of the state's financial statements provides the state with our professional opinion about the completeness, accuracy, and validity of the statements and the state's accounting information as well as providing assurance over the accuracy and reliability of financial information used to manage state programs. 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 does not have correct information to plan for the future.

The state accounts for sources and uses of resources in various funds in the financial statements, and are presented in the Comprehensive Annual Financial Report. The financial statements include significant accounts, including assets, liabilities, revenues, and expenditures for each fund. The General Fund is the state's primary operating fund, which is used to account for financial resources of the general government (except those accounted for in another fund), including personal income and corporate income tax revenue.

Special Revenue Funds are used to account for specific revenue sources that are restricted to expenditures for specified purposes. Revenue for the different funds comes from various sources, such as federal grants, tobacco taxes, healthcare provider taxes, highway user taxes, vehicle registration taxes, user fees, investment income, transfers from other funds, and forest management. The state reports five Special Revenue Funds: Health and Social Services, Public Transportation, Environmental Management, Educational Support, and Common School.

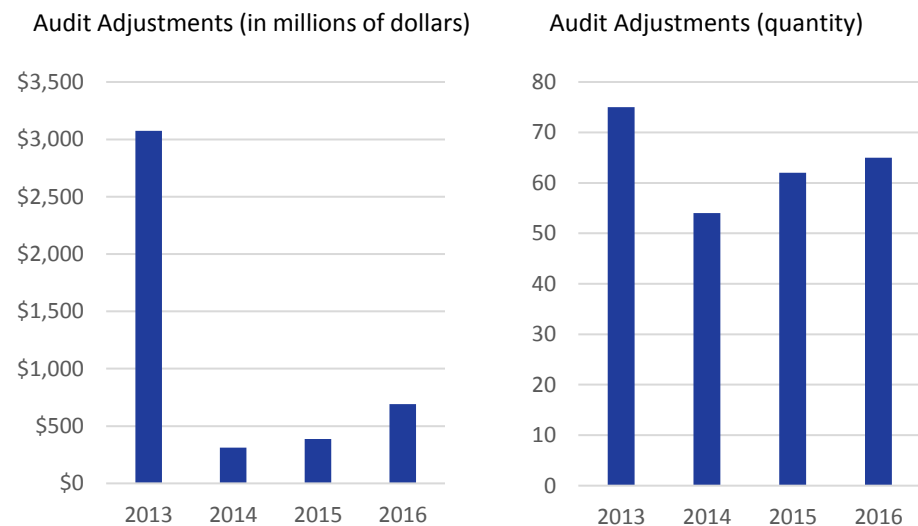
Proprietary (Enterprise) Funds are used to account for activities where fees are charged for goods and services provided. These funds include activities that finance multi-family rental housing, single-family mortgages for low to moderate-income families, single-family residential housing for qualified Oregon veterans, Lottery products, and unemployment benefits. The state reports four proprietary funds: Housing and Community Services, Veterans' Loan, Lottery Operations, and Unemployment Compensation.

We issued an unmodified opinion on the state's financial statements for fiscal year 2016. An unmodified opinion means the financial statements, as corrected, are fairly presented in conformance with Generally Accepted Accounting Principles.

To conduct this audit, our financial auditors performed audit procedures of all major funds and audited approximately 500 accounts at 25 state agencies; including, but not limited to, the Department of Human Services, Oregon Health Authority, Oregon Department of Transportation, and the Department of Education. During the course of our audit, we reviewed \$27.7 billion of the state's assets, \$15.1 billion of the state's liabilities, \$25.1 billion of the state's revenues, and \$25.3 billion of the state's expenditures.

In the course of our work, we identified \$690 million in accounting errors and proposed adjustments to 65 accounts to correct these errors. We issued 16 recommendations to 9 state agencies for improvements to standard controls used to ensure the accuracy of financial information. We reported the results of our audits to agency management, federal officials and to the public. Figure 1 shows the proposed adjustments and number of accounts adjusted for the last four fiscal years. Fiscal year 2013 included adjustments to accounts to correctly report fund balance; the adjustments were not indicative of misstatements to the financial statements as a whole.

**Figure 1: Financial Audit Adjustments (Total Amounts Adjusted and Quantity)**

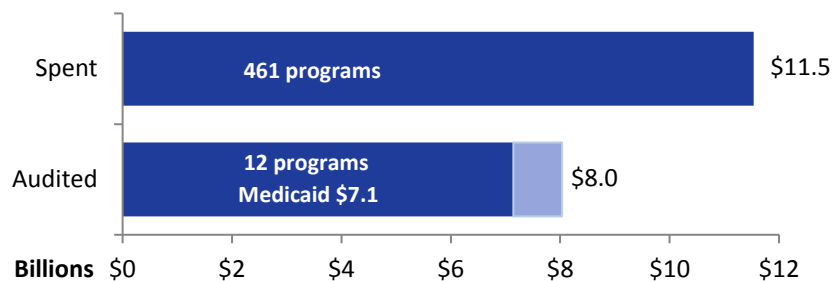


## Federal Compliance (Single Audit) – Fiscal Year 2016 Results

Every year we perform compliance audits of federal programs to determine if they meet federal requirements for tracking and using federal dollars. These programs provide billions of federal dollars to Oregon citizens for important social, economic, and environmental missions. These annual audits, summarized in the Single Audit Report, are required by the federal government for the state to receive federal financial assistance.

In fiscal year 2016 the State of Oregon spent \$11.5 billion in federal funds for 461 federal programs administered by 42 state agencies. As shown in Figure 2, Medicaid represented about 88% of the federal expenditures we audited.

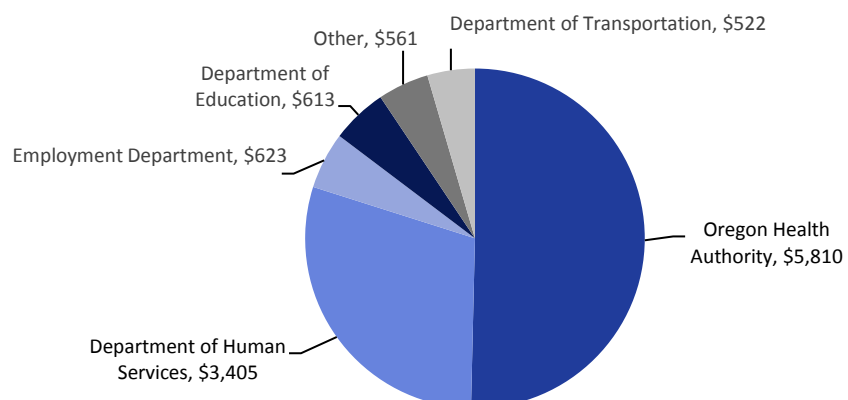
**Figure 2: Audit Coverage of Fiscal Year 2016 Single Audit**



*93% of the Oregon Health Authority's Federal Spending is Medicaid*

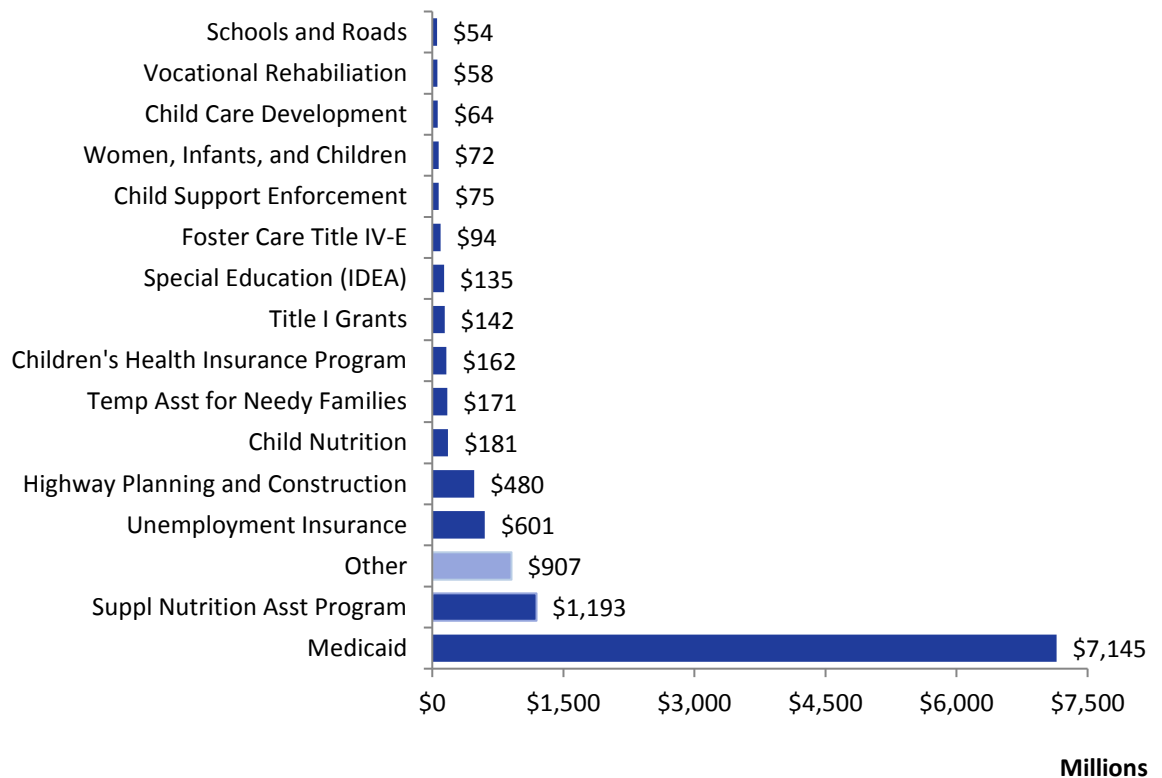
The Department of Human Services and the Oregon Health Authority accounted for \$9.2 billion, or 80%, of the state's federal expenditures, as seen in Figure 3. The Department of Human Services administers some of the state's larger federal programs; including Supplemental Nutrition Assistance, Temporary Assistance for Needy Families, and Medicaid (\$1.7 billion). The Oregon Health Authority jointly administers the Medicaid Program, which represents \$5.4 billion of its federal expenditures.

**Figure 3: Federal Expenditures by State Agency, Fiscal Year 2016 (in millions)**



Of the 461 federal programs administered by the State of Oregon, 15 programs accounted for 92% of the state's total federal expenditures in fiscal year 2016. The Medicaid program is by far the largest public assistance program administered by the state, as depicted in Figure 4.

**Figure 4: Summary of Federal Expenditures by Federal Program, Fiscal Year 2016**



### ***Medicaid expenditures are increasing***

Figure 5 shows that federal expenditures for Medicaid have steadily increased since 2012, while state expenditures for Medicaid have remained fairly consistent. The increase in federal spending is largely due to the expansion of Medicaid eligibility to low income individuals through the Affordable Care Act (ACA). According to a September 2016 report issued by the Oregon Health Authority, 95% of Oregonians now have health insurance, which includes coverage through Medicaid. Healthinsurance.org reports the number of Oregonians covered by Medicaid as of June 30, 2016 is over 1 million, an increase of about 409,000 since the fall of 2013. As of June 30, 2016, "newly eligible" individuals are estimated at 325,000 and are covered 100% with federal dollars for the first three years of the program, meaning the expenditures for newly insured individuals do not require any state funding. Beginning with federal fiscal year 2017, the federal portion covering "newly eligible" individuals will gradually decrease to 90% by federal fiscal year 2020 with the expectation that the state will pay the difference. Further, at the national level, the federal government is considering making additional changes to further lower the federal share of Medicaid expenditures.

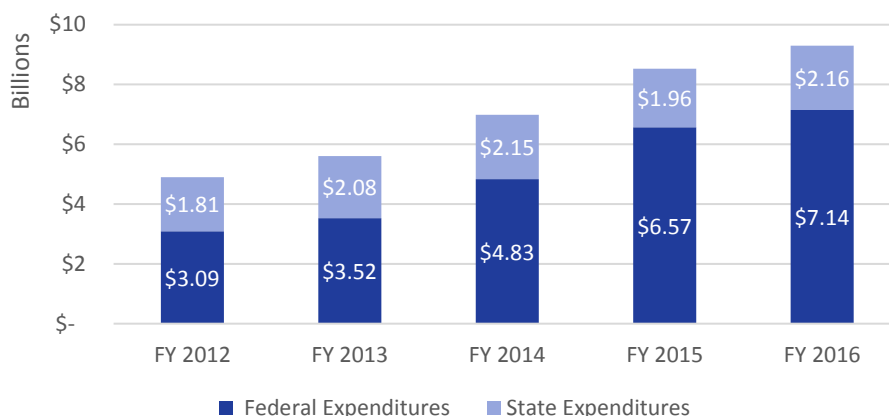
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*The Medicaid Program is the largest federal program for most states*

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**Figure 5: Federal and State Medicaid Expenditures Over Time**



## Federal Findings for Fiscal Year 2016

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 as well as large expenditure programs that have not been audited in the most recent two years. At least 40% of total federal expenditures are required to be audited each year.

However, due to internal control and compliance weaknesses from prior years, we increased the audit coverage for fiscal year 2016 to meet audit requirements set by OMB. For fiscal year 2016, we audited 12 federal programs, expending a total of \$8 billion, to determine if the state was compliant with federal program requirements. While Medicaid is required to be audited each year, five of the remaining 11 programs we audited in fiscal year 2016 were required to be audited due to material weaknesses identified in the prior year.

For fiscal year 2016, we questioned whether Oregon's spending of approximately \$1.4 million in federal expenditures was appropriate under federal program rules and we issued 23 findings related to 7 audited federal programs. Federal procedures require us to perform follow-up procedures in the next year for programs with findings to determine whether the agency has resolved the findings. Depending on the severity of the findings, some programs may require a full audit while others just a follow-up on the status of the implementation of the audit recommendations. Of the 12 programs audited, 8 will require follow-up procedures or full audits next year.

Figure 6 provides details on programs audited and the number of findings identified for each program. As shown in Figure 7, we audited more programs and identified more findings at the Department of Human Services.



**Figure 6: 2016 Findings by Audited Federal Program**

Federal Program	2016 Findings	Federal Program Expenditures
Foster Care Title IV-E	5	\$ 94,099,236
Medicaid	4	7,145,077,432
Adoption Assistance	3	39,069,109
ACA – State Innovation Models: Funding for Model Design and Model Testing Assistance	3	12,073,831
Pacific Coast Salmon Recovery/Pacific Salmon Treaty Program	3	10,759,150
Child Care and Development Fund	2	63,840,972
Low-Income Home Energy Assistance	2	34,739,568
Immunization Grants	0	45,609,117
Highway Planning and Construction	0	480,317,115
Forest Service Schools and Roads	0	54,162,865
National Guard Military Operations and Maintenance (O&M) Projects	0	35,915,469
Veterans' State Nursing Home Care	0	16,069,412
Multiple Programs	1	
	<b>23</b>	<b>\$ 8,031,733,276</b>

*Due to the complexity of the programs, number of transactions, and numerous federal requirements, most states report several audit findings.*

**Figure 7: 2016 Findings & Questioned Costs by State Agency**

State Agency	Programs Audited <sup>1</sup>	2016 Findings	Questioned Costs <sup>2</sup>
Department of Human Services*	4	12	\$ 956,560
Oregon Health Authority*	3	8	4,528
Oregon Housing Department	1	2	424,378
Oregon Department of Fish and Wildlife	1	2	4,577
Oregon Department of Education	1	1	-
Oregon Watershed Enhancement Board	1	1	-
Oregon Department of Veterans' Affairs	1	0	-
Oregon Department of Administrative Services	1	0	-
Oregon Department of Transportation	1	0	-
			<b>\$ 1,390,043</b>

<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.

### ***Fewer programs with qualified opinions in 2016***

As shown in Figure 8, the number of qualified programs decreased from the prior year. 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. Three federal programs that received qualified opinions in the prior year did not receive qualified opinions in fiscal year 2016. The Medicaid program did not receive a qualified opinion as we reported fewer program findings and the issues identified in 2016 did not result in material noncompliance. We also saw improvement in the Adoption Assistance program where no material noncompliance was identified. The Immunization program also completed subrecipient site visits to remediate the prior year control deficiency and material noncompliance.

We found the Department of Human Services and Department of Education did not establish adequate internal controls and were not materially compliant with federal requirements for two programs: Foster Care and the Child Care and Development Fund. We issued qualified opinions on these two programs. For these programs, we identified control weaknesses and noncompliance in the areas of federal requirements for allowable costs/costs principles, eligibility, and subrecipient monitoring.

**Figure 8: Federal Programs with Qualified Opinions**

Federal Program	2012	2013	2014	2015	2016
Foster Care	X	X	X	X	X
CCDF				X	X
Medicaid		X	X	X	
Adoption Assistance		X	X	X	
Immunization				X	
Temporary Assistance for Needy Families		X			
Low Income Home Energy Assistance	X	X			
Child Nutrition	X				
Child and Adult Care Food	X				
Community Services Block Grant	X				
Weatherization Assistance	X				

## Finding history

Audit findings include recommendations that address noncompliance with federal requirements and internal control weaknesses related to those requirements. 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 2016, we reported on the status of 55 findings from prior years because they remained uncorrected at the end of the prior fiscal year. Figure 9 illustrates compliance requirements with control weaknesses or noncompliance for the past five years.

**Figure 9: Findings History by Type of Compliance Requirement\***

Compliance Requirement	2012	2013	2014	2015	2016	Total
Activities Allowed or Unallowed	3	3	4	4	2	<b>16</b>
Allowable Costs/Cost Principles	12	5	4	3	9	<b>33</b>
Cash Management	1	2	2	1	1	<b>7</b>
Eligibility	5	9	5	6	4	<b>29</b>
Equipment	1	0	0	0	0	<b>1</b>
Matching, Level of Effort, Earmarking	1	2	3	4	1	<b>11</b>
Period of Performance	0	2	3	2	0	<b>7</b>
Procurement, Suspension, & Debarment	3	0	1	0	1	<b>5</b>
Reporting	5	9	10	3	2	<b>29</b>
Subrecipient Monitoring	5	2	5	4	3	<b>19</b>
Special Tests and Provisions	7	8	9	12	3	<b>39</b>
	<b>43</b>	<b>42</b>	<b>46</b>	<b>39</b>	<b>26</b>	<b>196</b>

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

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

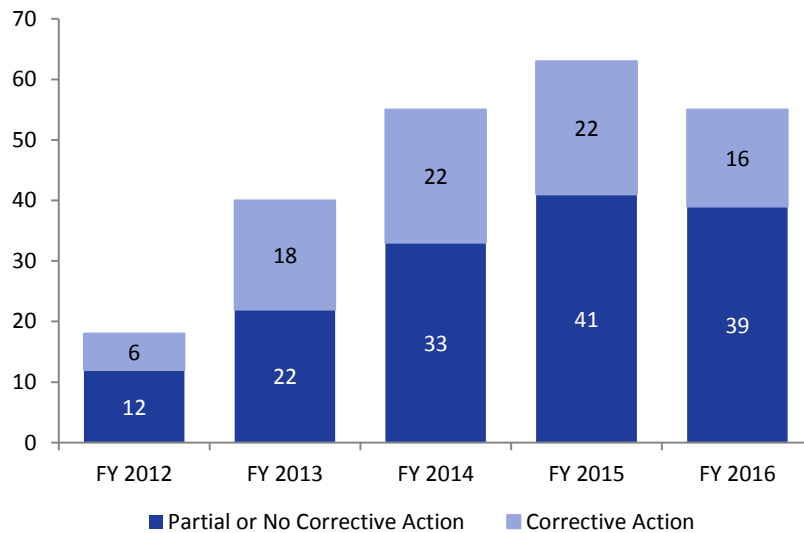
The number of uncorrected prior year findings decreased in fiscal year 2016 by 13%. However, the number of findings that continue to be uncorrected year after year continues to be of concern. Historically, many findings remain uncorrected from one year to the next because agencies do not correct the underlying issues leading to noncompliance or control weaknesses.

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. For example, the Foster Care and Adoption Assistance programs have had ongoing issues related to maintaining documentation to support federal Foster Care eligibility determinations for children and providers. The department should be maintaining eligibility documentation in the child welfare system, but documents are frequently maintained by staff at branch offices and there are significant delays in getting the documentation into the system. The department also has not made clear policies as to what documentation should be maintained to support child and provider eligibility within the child welfare system. Federal funding could be at risk with ongoing compliance issues; these programs are under a Program Improvement plan, issued by the Administration for Children and Families.

In 2016, issues underlying five prior year Medicaid findings that had been ongoing for several years were corrected and issues underlying seven prior year Medicaid findings were not fully corrected. Those issues relate to client eligibility, provider eligibility, security reviews of automated data processing equipment, and review of administrative charges.

When a finding is not corrected, we must re-issue the finding the next year. Figure 10 presents actions taken over the last five years on prior year findings that remained uncorrected at the end of the fiscal years shown below.

**Figure 10: Action Taken on Prior Year Uncorrected Federal Findings**



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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 the 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 is authorized to audit all state officers, agencies, boards, and commissions and oversees audits and financial reporting for local governments.

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Financial and Compliance Audit Staff

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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:

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Salem, Oregon 97310

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 2016 were commendable and sincerely appreciated.