

# Secretary of State Audit Report

Jeanne P. Atkins, Secretary of State

Mary Wenger, Interim Director, Audits Division



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## Keeping the State of Oregon Accountable, Fiscal Year 2015

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Every year the Audits Division of the Secretary of State's Office audits the State of Oregon's financial statements to determine whether the information reported is reliable and accurate. This annual audit provides the state with our professional opinion about the completeness, accuracy, and validity of the state's accounting information. *See the Financial Statement Audit section of this report for more discussion of Oregon's financial status.*

In addition, we annually perform compliance audits of programs funded by the federal government 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. *See the Federal Compliance Audits section of this report for more discussion of Oregon's compliance with the requirements of federal programs.*

The division communicates errors identified in financial reporting, financial processes, and non-compliance to state agencies and provides recommendations for correction to assure the integrity of financial information provided to the public. This report, "Keeping the State of Oregon Accountable," reflects the findings of those annual audits of publicly funded programs. Important conclusions in this report are:

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

- We concluded that the state's financial statements, as corrected, are fairly presented in conformance with Generally Accepted Accounting Principles.
- We reported fewer internal control weaknesses this year and found that management corrected several of the prior year findings.
- Three major changes impacted Oregon's financial statements for fiscal year 2015: a \$1.6 billion increase in Medicaid expenditures, a change in the reporting of three major universities, and new reporting standards that changed how pension information is presented.

### *Federal Compliance Audits*

- Because of ongoing internal control and compliance weaknesses, auditors were required to audit an increased percentage of the state's federal expenditures.
- Our audit included 35 findings related to 14 audited federal programs at seven state agencies. We issued "qualified" opinions on five programs, which indicate a department's internal controls are inadequate to prevent or detect significant noncompliance in a timely manner.

For more information about audit results, you can also see the official reports on our website:

Oregon's Financial Statements:

<http://sos.oregon.gov/audits/Documents/2016-03.pdf>

Single Audit (including Federal Compliance) Results:

<http://sos.oregon.gov/audits/Documents/2016-09post.pdf>

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## Financial Statement Audit

At the beginning of fiscal year 2015, three major universities became independent from the state. The University of Oregon, Oregon State University, and Portland State University are now reported separately from the state's activities in the financial statements. As a result of the change, the state recognized a loss of \$2 billion, mainly due to the transfer of capital assets. While the revenues and expenditures from the universities decreased the state's financial statements, increases in Medicaid offset the change.

Another notable change in the state's 2015 financial statements was the implementation of the Governmental Accounting Standards Board's new standards for pension reporting. These standards require certain pension amounts to be reported in the financial statements rather than in the notes to the financial statements. The state's net position was impacted by the required reporting change. For fiscal year 2015, Oregon agencies reported a net pension asset of \$430 million, meaning the pension plan is in the admirable position of having more than it needs to cover payments. However, that position will not be so favorable next year due to the effects of a Supreme Court Decision.

Last year the Oregon Supreme Court ruled that the Legislature's attempts to reduce pension costs by limiting cost of living adjustments (COLA's) to retirees was unconstitutional and established that while the Public Employees Retirement System (PERS) could limit COLA increases to future retirees, they could not limit COLAs to employees who had already retired. This decision will take effect in fiscal year 2016 and the state will report a net pension liability at June 30, 2016, currently estimated to be about \$503 million, turning the asset into a liability and tipping the scales the other direction.

Our audit of the state's financial statements provides assurance over the accuracy and reliability of financial information used to manage the state. 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 budget for the future.

To conduct this audit our financial auditors perform audit procedures of numerous accounts at several state agencies. Each year, we spend a good share of our statewide audit resources verifying the accuracy of the books and records of the Department of Human Services (DHS) and the Oregon Health Authority (OHA). These two agencies represent over 50% of the state's \$21.5 billion in governmental expenditures.

Our audit of the state's financial statements for fiscal year 2015 showed improvement over the previous year. We reported fewer internal control weaknesses this year and found that management corrected several of the previous findings. Continuing weaknesses in controls tend to be around computer system controls and the proper application of accounting principles.

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 Generally Accepted Accounting Principles.

**Figure 1: Condensed Statement of Net Position and Activities, Fiscal Year 2015**

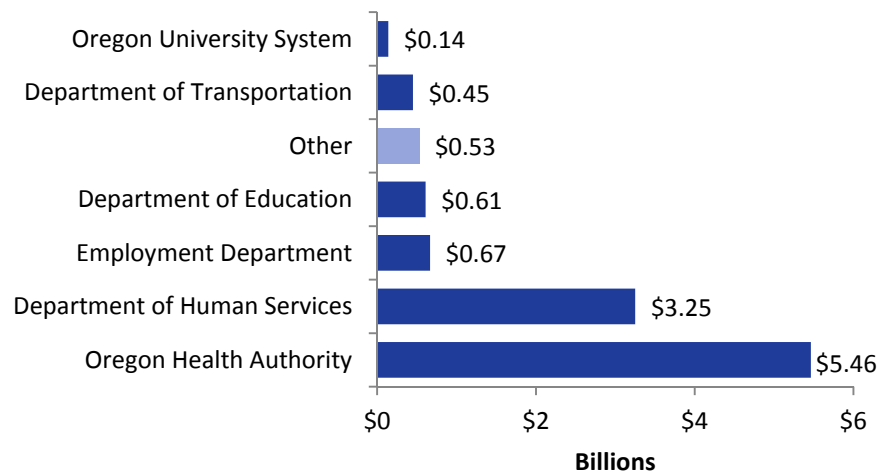
<b>Condensed Statement of Net Position</b> Governmental and Business-type Activities As of June 30, 2015 (in millions)		<b>Condensed Statement of Activities</b> Governmental and Business-type Activities For the fiscal year ended June 30, 2015 (in millions)	
<b>Assets</b>		<b>Program Revenues</b>	
Cash and Investments	\$ 10,753	Governmental activities	\$ 12,003
Receivables	6,426	Business-type activities	3,499
Capital assets, net of depreciation	14,015	<b>General Revenues</b>	
Other assets	590	Governmental activities	10,700
Total Assets	<u>31,784</u>	Business-type activities	<u>(2,224)</u>
<b>Deferred Outflows</b>	<u>373</u>	Total revenues	<u>23,978</u>
<b>Liabilities</b>		<b>Expenses</b>	
Long-term debt	12,541	Governmental activities	21,485
Other liabilities	2,944	Business-type activities	2,530
Total liabilities	<u>15,485</u>	Total expenses	<u>24,015</u>
<b>Deferred Inflows</b>	<u>837</u>	Increase in Net Position	(37)
<b>Net Assets</b>		Net Position - beginning	<u>15,872</u>
Invested in capital assets, net of related debt	11,751	Net Position - ending	<u><u>\$15,835</u></u>
Restricted	4,122		
Unrestricted	(38)		
Total Net Position	<u><u>\$15,835</u></u>		

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## Federal Compliance Audits

In fiscal year 2015 the State of Oregon spent \$11.1 billion in federal funds to administer 382 federal programs. Six of the 43 state agencies administering federal programs accounted for \$10.6 billion or 95% of the state's federal expenditures. The Department of Human Services and the Oregon Health Authority accounted for \$8.7 billion, or 78%, of the state's federal expenditures.

**Figure 2: Total Federal Expenditures by State Agency, Fiscal Year 2015**



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*The federal government is implementing Uniform Guidance in fiscal year 2016, which may result in fewer federal compliance audits*

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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 2015 and audit 88% of the state's federal expenditures of \$11.1 billion to meet audit requirements set by the OMB. For fiscal year 2015, we audited 18 federal programs expending a total of \$9.7 billion to determine if the state was compliant with federal program requirements.

## Medicaid expenditures are increasing

The Medicaid program is by far the largest public assistance program run by the State of Oregon, as depicted in Figure 3. The state spent \$6.6 billion in federal funds for the Medicaid program in fiscal year 2015, or 59% of all the state's federal expenditures.

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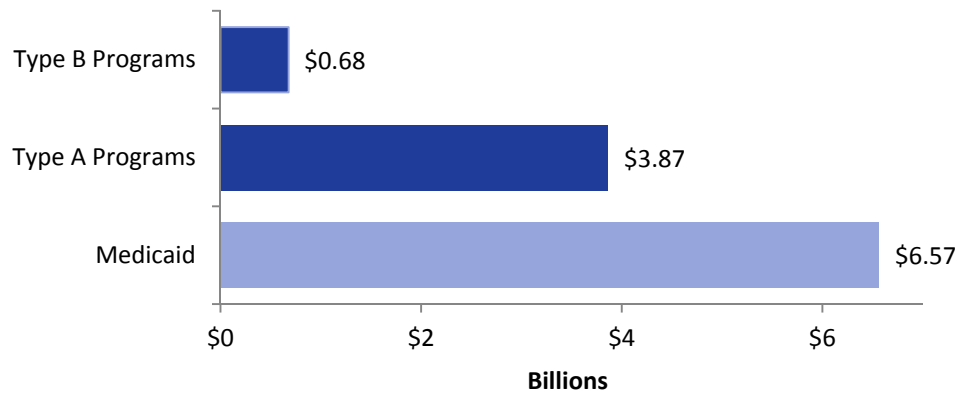
*The Medicaid Program is the largest federal program for most states*

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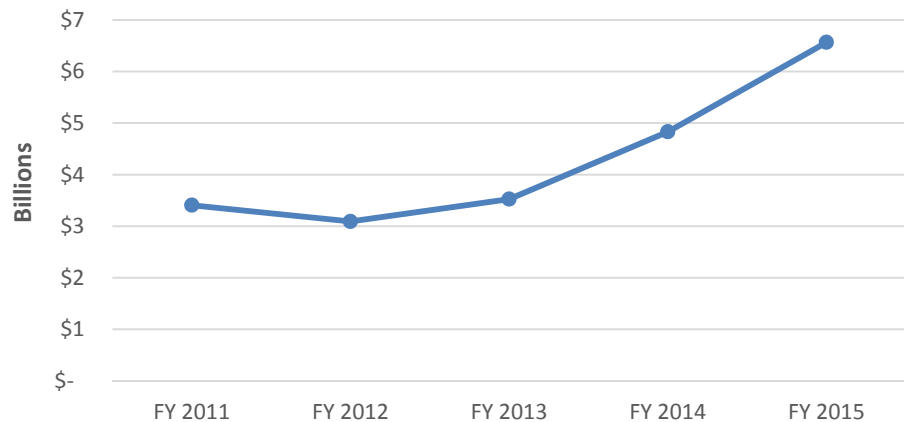
Figure 4 shows the state's federal spending for Medicaid has steadily increased in the past three years, spurred on by the Affordable Care Act. Over 400,000 additional Oregonians have health care coverage through the Oregon Health Plan since the Affordable Care Act expansion started in January 2014.

**Figure 3: Summary of Federal Expenditures, Fiscal Year 2015**

Each Type B Program's annual expenditures are less than \$30 million. Each Type A program's annual expenditures exceed \$30 million. Medicaid is a Type A Program, but is shown separately.



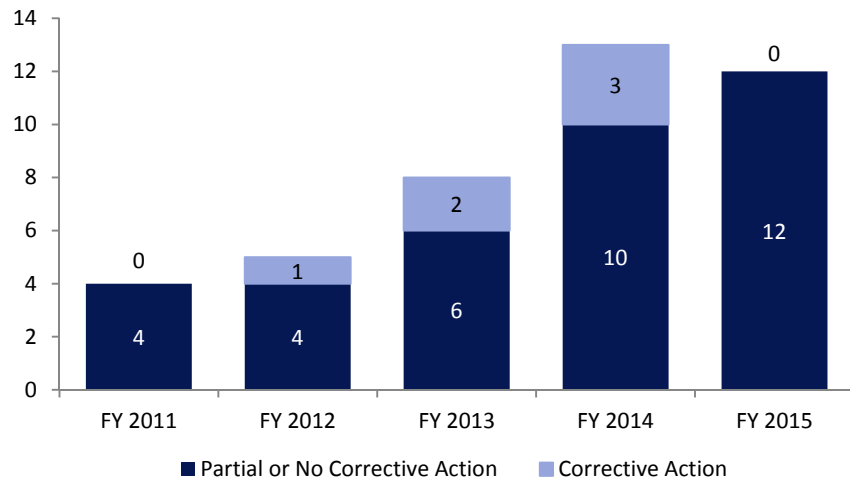
**Figure 4: Federal Medicaid Expenditures Over Time**



### **Audit Findings in the Medicaid Program**

Our 2015 audit found six control and compliance findings related specifically to the Medicaid Program. Five of these findings have been ongoing for the past three years and are related to such important concerns as documenting that provider eligibility checks were performed; documenting support for client eligibility determinations, and timely performance of nursing facility reviews. Figure 5 shows a history of Medicaid findings and illustrates how slowly they are resolved.

**Figure 5: Action Taken on Prior Year Uncorrected Medicaid Findings**



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

We found the Department of Human Services, Oregon Health Authority, and Department of Education did not establish adequate internal controls and were not materially compliant with federal requirements for five programs: Foster Care, Adoption Assistance, Medicaid, Immunization Cooperative Agreements, and Child Care and Development Fund.

#### ***Fiscal Year 2015 federal findings***

For fiscal year 2015, we questioned whether Oregon’s spending of approximately \$1.7 million in federal funds was appropriate under federal program rules and we issued 35 findings related to 14 audited federal programs at seven state agencies. 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. Some programs will require a full audit because of the severity of the findings. Of the 18 programs we audited this year, 12 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: 2015 Findings by Audited Federal Program**

Federal Program	2015 Findings	Federal Program Expenditures
Medicaid*	8	\$ 6,567,317,385
Foster Care Title IV-E*	8	95,922,134
Adoption Assistance*	6	44,960,776
Temporary Assistance for Needy Families*	6	208,462,699
Student Financial Assistance	4	129,702,312
Child Care and Development Fund	4	65,255,649
Supplemental Nutrition Program*	5	1,254,565,477
Special Education	2	128,830,805
Low-Income Home Energy Assistance	2	33,720,004
Unemployment Insurance	1	643,472,138
Child Nutrition	1	170,419,498
Title I	1	150,098,543
Immunization Grants	1	47,602,061
Workforce Investment Act	1	33,002,315
Women, Infants, and Children	0	73,560,659
Child Support Enforcement	0	54,073,055
Child and Adult Care Food	0	35,528,735
Fire Management Assistance	0	15,959,013
		<b>\$ 9,740,818,362</b>

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

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

**Figure 7: 2015 Findings & Questioned Costs by State Agency**

State Agency	Programs Audited <sup>1</sup>	2015 Findings	Questioned Costs <sup>2</sup>
Department of Human Services*	6	20	\$ 1,522,804
Oregon Health Authority*	3	7	1,342,855
Department of Education	5	5	236,424
Oregon University System	1	4	-
Oregon Housing Department	1	2	-
Employment Department	1	1	8,347
Higher Education Coordinating Commission	1	1	-
Department of Justice	1	0	-
Department of Forestry	1	0	-
			<b>\$ 3,110,430</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

### ***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 2015, we reported on the status of 63 findings from prior years because they remained uncorrected at the end of the fiscal year. Figure 8 illustrates compliance requirements with control weaknesses or noncompliance for several years.

**Figure 8: Findings History by Type of Compliance Requirement\***

Compliance Requirement	2011	2012	2013	2014	2015	Total
Activities Allowed or Unallowed	0	3	3	4	4	<b>14</b>
Allowable Costs/Cost Principles	3	12	5	4	3	<b>27</b>
Cash Management	1	1	2	2	1	<b>7</b>
Eligibility	2	5	9	5	6	<b>27</b>
Equipment	0	1	0	0	0	<b>1</b>
Matching, Level of Effort, Earmarking	0	1	2	3	4	<b>10</b>
Period of Performance	0	0	2	3	2	<b>7</b>
Procurement, Suspension, & Debarment	1	3	0	1	0	<b>5</b>
Reporting	2	5	9	10	3	<b>29</b>
Subrecipient Monitoring	1	5	2	5	4	<b>17</b>
Special Tests and Provisions	1	7	8	9	12	<b>37</b>

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

***Program findings resulting in qualified opinions***

We issued qualified opinions on five programs in fiscal year 2015. 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 federal requirements for allowable activities/costs, eligibility, period of performance, and special tests and provisions.

Figure 9 presents federal programs with qualified opinions over the last five years.

**Figure 9: Federal Programs with Qualified Opinions**

Federal Program	2011	2012	2013	2014	2015
Medicaid	X		X	X	X
Foster Care		X	X	X	X
Adoption Assistance			X	X	X
CCDF					X
Immunization					X
Temporary Assistance for Needy Families	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			
Weatherization Assistance	X	X			

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

Of particular concern is the number of findings that continue to be uncorrected year after year. 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 and the underlying problems contributing to the findings are not always easy to fix. For example, the Foster Care and Adoption Assistance programs have had ongoing issues related to period of performance since 2013 because the child welfare system was not designed to prevent the department from making claims for expenditures occurring outside the period of performance. The department has also struggled over the last four years with maintaining documentation to support federal Foster Care eligibility determinations for children and providers.

The number of uncorrected prior year findings increased in fiscal year 2015 by 15%. 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 each the fiscal years shown.

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

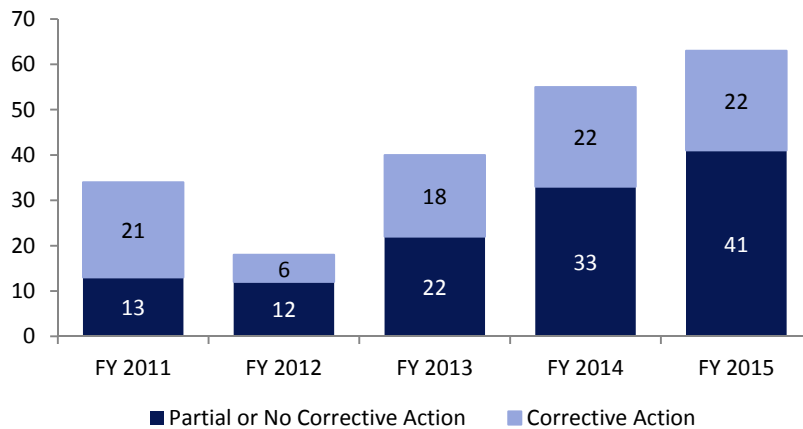


Figure 11 shows the five-year history of audited programs. Many programs were required to be audited again because of uncorrected weaknesses from the prior year.

**Figure 11: Program Audit History**

Federal Program	2011	2012	2013	2014	2015
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	X
Child Nutrition <sup>2</sup>		X	X	X	X
Child and Adult Care Food <sup>2</sup>		X	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
Title I Grants <sup>2</sup>	X			X	X
Workforce Investment Act <sup>2</sup>	X			X	X
Special Education <sup>2</sup>	X			X	X
Child Care and Development <sup>2</sup>	X			X	X
Fire Management Assistance <sup>2</sup>				X	X
Student Financial Assistance <sup>3</sup>		X			X
Women, Infants, and Children <sup>3</sup>		X			X
Disaster Grants			X	X	
Vocational Rehabilitation	X			X	
State Children's Insurance Program <sup>3</sup>	X			X	
Research and Development <sup>3</sup>	X			X	
Community Services Block Grant	X	X	X		
Military Operations and Maintenance		X	X		
State Grants for ACA Exchanges		X	X		
Highway Planning and Construction			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 FY2015 due to uncorrected weaknesses in prior year

<sup>3</sup>Program considered high-risk in FY2015 due amount of expenditures, and not audited in prior two years

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## 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 2015 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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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:

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

phone: 503-986-2255

mail: Oregon Audits Division  
255 Capitol Street NE, Suite 500  
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 2015 were commendable and sincerely appreciated.