



State Audit Update

Financial Management Advisory Council

May 25, 2017

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Jim Brownell, Audit Manager

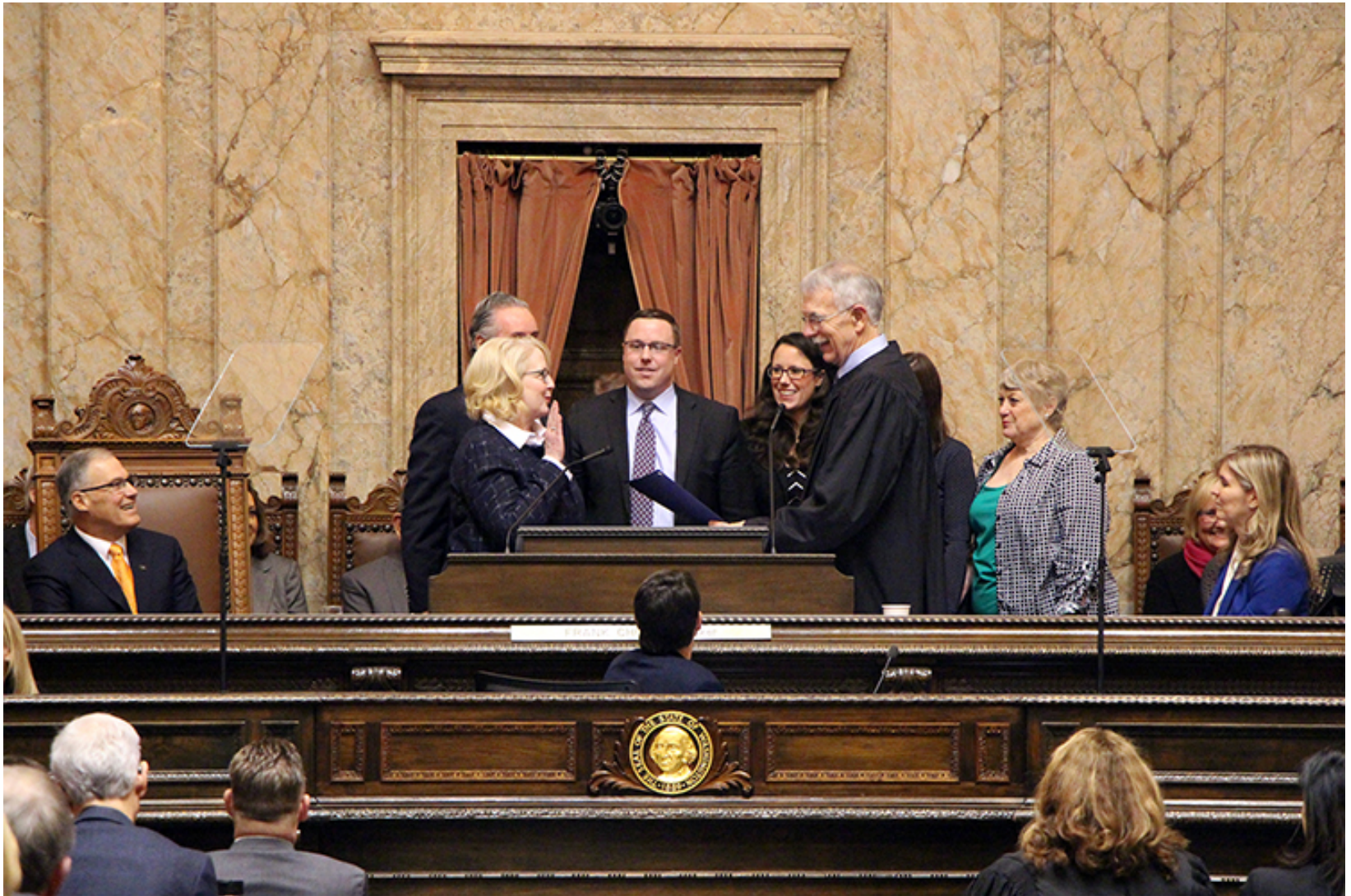
Sarah Mahugh, CPA, Program Manager

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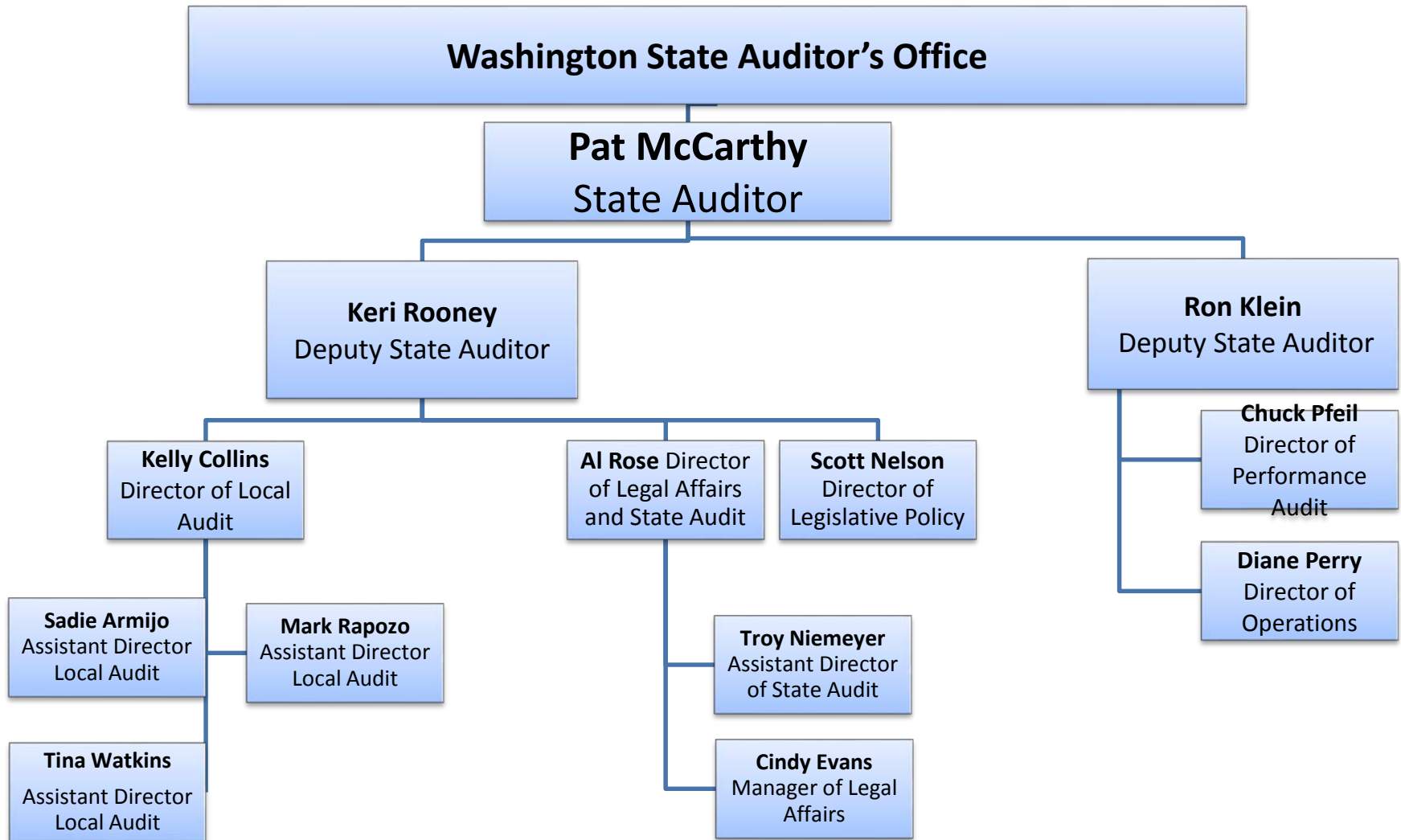
Topics

- New State Auditor
- Current organizational structure
- State Audit
- New requirement
- State of Washington Single Audit
- Whistleblower program
- Fraud
- State CAFR 2016
- Contracted financial audits
- Accountability audits
- Future audit work plan

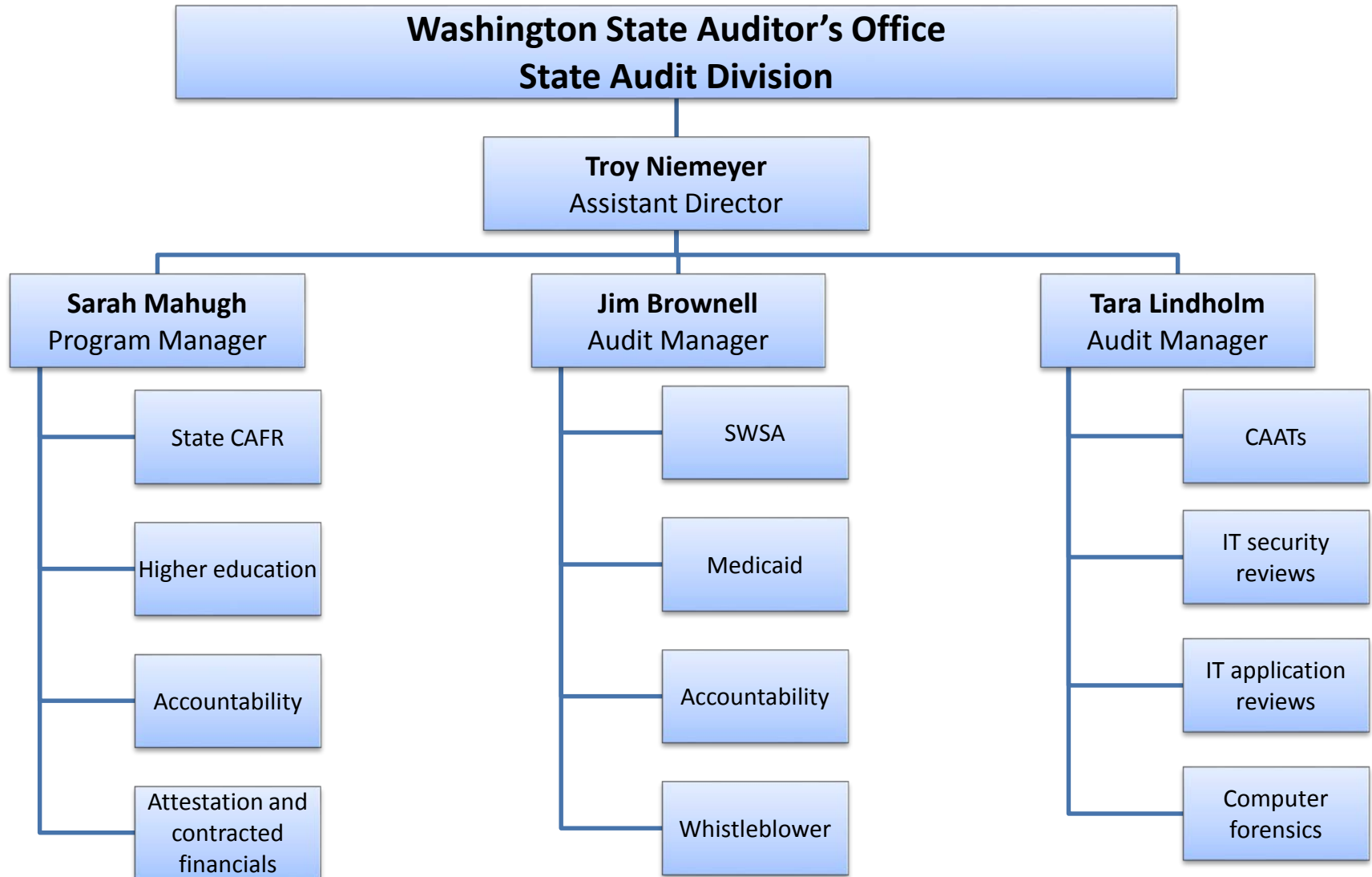
New State Auditor



New State Auditor



Current organizational structure



State Audit



New requirement

SSB 5372

- Passed unanimously by House and Senate
- Adds a new section to 43.09 RCW
- Changes the agency requirement slightly
- Requires additional reporting by our Office
 - Non-compliance with state law
 - If substantial progress not made – our Office must report
 - Governor
 - JLARC
 - Legislative committees

State of Washington Single Audit

Overview

- The Single Audit is an independent audit of systems and internal controls over federally funded programs to ensure compliance with federal regulations.
- The audit is conducted in accordance with the federal Office of Management and Budget's uniform administrative requirements and U.S. government auditing standards.
- The state spent about \$17.2 billion in federal assistance in fiscal year 2016.

State of Washington Single Audit

Audit coverage and reporting

- We audited 21 major and Type B programs
 - Major programs > \$30 million
 - Type B programs – selected based on risk
- Performed audit work at 12 state agencies (including universities and community colleges)
- The audit report is published by OFM:
 - The 2016 report was published on March 31, 2017.
 - A summary report will be published on our website this month.

State of Washington Single Audit: Five-year history

SWSA Findings and Likely Questioned Costs - 2012 to 2016

Audit Year	Total federal assistance	Programs audited	Audit findings	Likely questioned costs
2012	\$15,764,520,777	30	63	\$29,016,503
2013	\$14,892,685,569	31	45	\$14,799,519
2014	\$15,730,569,572	32	55	\$13,861,873
2015	\$17,030,229,853	31	56	\$142,222,871
2016	\$17,205,753,785	21	50	\$363,488,380

State of Washington Single Audit

Audit results

- 50 audit findings
 - Single audit findings report material weaknesses and significant deficiencies in internal controls, material non-compliance and questioned costs that exceed \$25,000
 - Adverse opinion on a major federal program for the second consecutive year due to significant questioned costs and material non-compliance in multiple areas
 - 22 findings related to the Medicaid program
 - Likely questioned costs are increasing mostly because of our expanded use of statistical sampling

Whistleblower program

- Our Office investigates reports of improper governmental action submitted by state employees.
- Legislation passed in 2017 expanded whistleblower protections



Whistleblower program

- The program is staffed by two full-time whistleblower investigators and a lead investigator (supervisor).
- In 2016, our Office:
 - Received 188 whistleblower complaints
 - Investigated 39 of the complaints
 - Published 25 reports; 11 resulted in reasonable cause findings
 - In some instances, we made recommendations on how agencies could improve internal controls.

Whistleblower program

Common investigative findings:

- Personal use of state resources
 - More than de minimis (brief and infrequent) in nature
 - Computer use
 - Not working required hours and failing to submit leave
- Non-compliance with contracting laws and required state policies (SAAM)
- Gross mismanagement
- Gross waste of public funds

Fraud

- State law requires state agencies and local governments to immediately report known or suspected losses of public funds and illegal activity to our Office.
- We assess the reports and determine whether to open investigations.
- We continue to see an uptick in loss reports:
 - Theft of client funds
 - Payroll misappropriation
 - Purchasing personal items with state credit cards

Overview

- Managed by Team Financial Audit
 - We perform an independent audit of the Comprehensive Annual Financial Report (CAFR) in accordance with Generally Accepted Governmental Auditing Standards.
 - This is our Office's second largest audit.
 - Over 9,600 hours
 - 40 staff from nine different audit teams assist in completing this audit.

STATE OF WASHINGTON
OFFICE OF FINANCIAL MANAGEMENT

Comprehensive Annual Financial Report

FOR THE FISCAL YEAR ENDED JUNE 30, 2016



NOVEMBER 2016

The outcome of the CAFR audit can affect our State's credit and bond rating

Bond ratings

On June 30, 2016, the state's general obligation debt was rated Aa1 by Moody's Investors Service, AA+ by Standard & Poor's Ratings Services and AA+ by Fitch Ratings. These ratings remain unchanged since 2011. Bond ratings are an important measure of the state's economic strength and accountability. They determine how much interest the state pays when it borrows money. Washington is considered to have good bond ratings. Standard & Poor's described the state's long term outlook as "stable," reflecting its view that the state's liquidity, financial trends and strengthening economy point to an improving financial position. The credit rating service also considers the state's strong financial-management policies and institutions in its projection.

Audit coverage and reporting

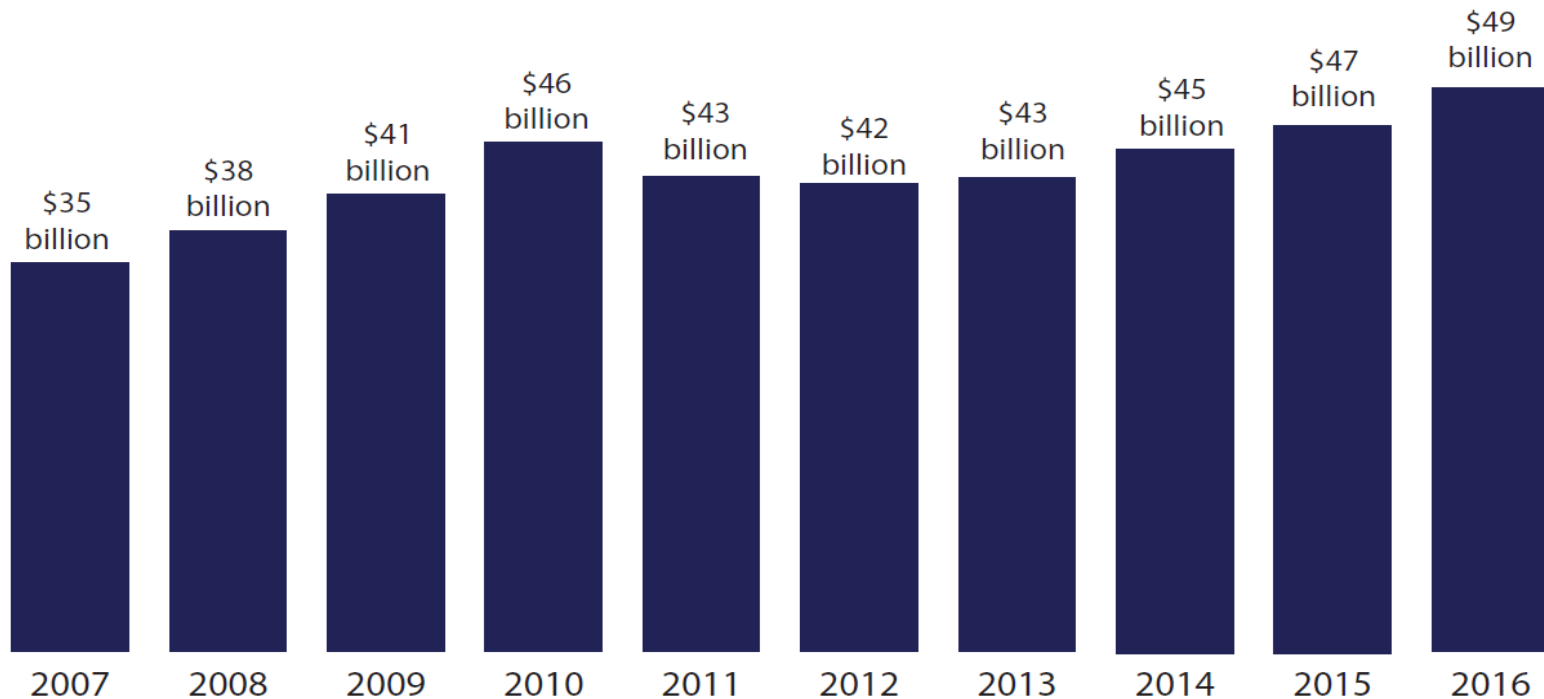
- Audited 15 agencies with 147 account balances material to the state's basic financial statements
- Audit reports:
 - Financial statement opinion released on November 1, 2016.
 - One of the fastest issuances of a state CAFR in the Nation
 - Report on internal controls over financial reporting and compliance and other matters was published in the State of Washington Single Audit report.
 - CAFR Summary Report

State CAFR 2016

CAFR Summary Report

Exhibit 2 – Total primary government expenses: 2007-2016

For fiscal years ending June 30



http://www.sao.wa.gov/resources/Documents/2016_CAFR_Summary.pdf

Significant risks

- Guaranteed Education Tuition program
- GASB 72 - Fair Value Measurement and Application
- Employment Security Department's Next Generation Tax System (NGTS)
- Management override of controls

Audit results

- Clean (unmodified) audit opinion
- Deficiencies in internal controls that represented a material weakness:
 - Changes to the Guaranteed Education Tuition program resulted in complicated and unique accounting for the program activities. OFM and program staff did not have a process in place to ensure activities were correctly reported.
 - Financial statement errors as a result of system processing, reporting and reconciliation issues in the State's Next Generation Tax System

Contracted financial audits

In 2016, we performed 28 financial audits for state agencies, universities, and community or technical colleges.

- 5 audit findings at 5 different organizations that identified areas needing improved internal controls
- A majority of the significant issues related to inaccurate tracking and reporting of capital assets (SAAM 20.15.30 c).

Accountability audits

State agency accountability audits

AUDIT SUMMARY

Results in brief

In the areas we audited, Board operations complied with applicable requirements and provided adequate safeguarding of public resources. The Board also complied with state laws and regulations and its own policies and procedures in the areas we examined.

Accountability audits

State agency accountability audit results in 2016

- 45 individual accountability audits for state agencies, including institutions of higher education
- 7 audit findings; the most significant ones are listed in our Annual Report here:

www.sao.wa.gov/resources/Pages/AnnualReports.aspx



The screenshot shows the website for the Office of the Washington State Auditor, Pat McCarthy. The header includes the state seal and navigation links: About Us, Local Government, State Government, Investigations, Resources, and Search Reports. A search bar is located in the top right. Below the navigation, there is a section for 'Annual Reports' with a sidebar menu on the left containing links for Resources, Public Records, Annual Reports, Local Government Resources, and Media Resources. The main content area features the title 'Annual reports from the State Auditor's Office' and a sub-section 'State Auditor's Office Annual Report'. The text explains that the office reports annually on its work and is required by state law to publish the report by December 31. Two links are provided: 'State Auditor's Office 2016 annual report (pdf, 612 kb)' and 'Performance Audit division 2016 progress report (pdf, 1.6 mb)'. A note indicates that to read reports from earlier years, users should visit a specific page. A decorative image of colorful coral is visible on the right side of the page.

Accountability audits

Area	Improvement area
Purchase cards	<ul style="list-style-type: none">• Used to purchase unallowable items• Lack of supporting documentation (business purpose)• Lack of pre-approval
Payroll	<ul style="list-style-type: none">• Payroll increase not properly approved or supported
Leases	<ul style="list-style-type: none">• Compliance with lease terms not adequately monitored

Accountability audits

Area	Improvement area
Contracts	<ul style="list-style-type: none">• Advertisements and winning bidders not posted to WEBS• Payments were made without valid contracts in place
Vendor payments	<ul style="list-style-type: none">• Missing or inadequate support for payments• Unallowable costs for the program or SAAM policies• Lack of documentation to ensure gift cards issued were used for allowable purposes
Cash receipting	<ul style="list-style-type: none">• Cash handling procedures not developed or not followed• Cash handling duties not adequately segregated• Lack of controls to ensure fees collected were complete• Billing rate plans lacked policies and OFM approval

Future audit work plan

- Our Office's goal is to cycle through all state agencies.
- Agencies are selected for accountability audits based on a risk assessment that includes many factors, such as:
 - Prior audit issues (findings, ML's, etc.)
 - Hotline or whistleblower complaints, and prior fraud reports
 - Size and complexity of agency
 - Financial activity (large amount of revenues and expenditures)

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