

State of Idaho
Internal Control Report

Independent Auditor's Report on Internal Control Over
Financial Reporting and on Compliance and Other Matters
Based on an Audit of Financial Statements
Performed in accordance with *Government Auditing Standards*

Fiscal Year 2014



Legislative Services Office
Idaho State Legislature

Serving Idaho's Citizen Legislature

Eric Milstead
Director

February 20, 2015

Honorable C.L. "Butch" Otter, Governor
Honorable Members of the Legislature
Honorable Brandon D. Woolf, State Controller

We are pleased to submit the State of Idaho *Internal Control Report* as it relates to our audit of the statewide *Comprehensive Annual Financial Report (CAFR)* covering the fiscal year ended June 30, 2014. This *Internal Control Report* is an integral part of the *CAFR* audit process and is required by *Government Auditing Standards* issued by the Comptroller General of the United States.

These standards require that we consider the internal control over financial reporting and disclose weaknesses that could have a material effect on the financial statements. We are also required to perform and disclose the results of tests of compliance with certain laws, regulations, and other requirements that could have a direct and material effect on the financial statement amounts.

The results of our audit identified four significant deficiencies in internal control and two material weaknesses in internal control. Although the risk of misstatement exists as a result of these issues, none of these weaknesses resulted in material misstatements that were not corrected as a result of the audit. As such, we were able to issue an unmodified opinion on the financial statements.

This report is available on our website at www.legislature.idaho.gov, and the *CAFR* can be obtained from the Office of the Idaho State Controller's website at www.sco.idaho.gov.

Sincerely,

April Renfro

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Legislative Audits Division

Mike Nugent, Manager
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Cathy Holland-Smith, Manager
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Eric Milstead
Director

Legislative Services Office
Idaho State Legislature

Serving Idaho's Citizen Legislature

December 23, 2014

Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*

Honorable C.L. "Butch" Otter, Governor
Honorable Members of the Legislature
Honorable Brandon D. Woolf, State Controller

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the State of Idaho as of and for the year ended June 30, 2014, and the related notes to the financial statements, which collectively comprise the State of Idaho's basic financial statements, and have issued our report thereon dated December 23, 2014. Our report includes a reference to other auditors who audited the financial statements of Boise State University, Eastern Idaho Technical College, Idaho State University, Lewis-Clark State College, University of Idaho and their respective component units, nor the Idaho Potato Commission, Idaho Dairy Products Commission, Idaho State Bar, Idaho Wheat Commission, Endowment Fund Investment Board, State Lottery Commission, Public Employee Retirement System of Idaho, Public Employees' Deferred Compensation Plan, Idaho Judges' Retirement Fund, IDeal Idaho College Savings Program, Idaho Individual Risk Reinsurance Pool, Idaho Small Employer Health Reinsurance Program, Idaho Health Insurance Exchange, State of Idaho Idle Pool, Local Government Investment Pool, Diversified Bond Fund, Idaho Building Authority, Bond Bank Authority, and the Idaho Housing and Finance Association as described in our report on the State of Idaho's financial statements. This report does not include the results of the other auditors' testing of internal control over financial reporting or compliance and other matters that are reported on separately by those auditors. The financial statements of the Eastern Idaho Technical College Foundation, Boise State University Foundation, Idaho State University Foundation, and the Public Employees' Deferred Compensation Plan were not audited in accordance with *Government Auditing Standards*.

Internal Control Over Financial Reporting
In planning and performing our audit of the financial statements, we considered the State of Idaho's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the State of Idaho's internal control. Accordingly, we do not express an opinion on the effectiveness of the State of Idaho's internal control.

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Our consideration of internal control was for the limited purpose described in the preceding paragraph 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 were not identified. However, as described in the accompanying Schedule of Findings and Responses, we identified certain deficiencies in internal control that we consider to be material weaknesses and significant deficiencies.

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. We consider the deficiencies described in the accompanying Schedule of Findings and Responses to be material weaknesses: 2014-104 and 2014-105.

A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiencies described in the accompanying Schedule of Findings and Responses to be significant deficiencies: 2014-101, 2014-102, 2014-103, and 2014-106.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the State of Idaho's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests did not disclose instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards.*

State of Idaho's Responses to Findings

The State of Idaho's responses to the findings identified in our audit are described in the accompanying Schedule of Findings and Responses. The State of Idaho's responses were not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on them.

Purpose of this Report

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

Sincerely,



April Renfro, CPA, Manager
Legislative Audits Division

STATE OF IDAHO
INTERNAL CONTROL REPORT
SCHEDULE OF FINDINGS AND RESPONSES
FOR THE YEAR ENDED JUNE 30, 2014

OFFICE OF THE STATE CONTROLLER

2014-101 Internal control weaknesses allowed misstatements in the statewide financial statements and note disclosures to go undetected.

2014-102 Internal control deficiencies over the processing of statutory transfers led to noncompliance as well as miscoded and unsupported transactions.

IDAHO STATE DEPARTMENT OF EDUCATION

2014-103 Errors in the accounts receivable closing package were not detected or prevented by internal control procedures in place.

IDAHO DEPARTMENT OF HEALTH AND WELFARE

2014-104 Deficiencies in internal control allowed several errors in various closing packages to go undetected.

IDAHO STATE TAX COMMISSION

2014-105 Errors in the data used to prepare the taxes receivable estimate were not detected by internal control procedures, resulting in misstatements.

IDAHO DEPARTMENT OF TRANSPORTATION

2014-106 Internal controls intended to reduce the risk of misstatements in the inventory closing package were not performed at a level of detail necessary to detect significant errors.

STATE OF IDAHO
INTERNAL CONTROL REPORT
FINDINGS AND RESPONSES
FOR THE YEAR ENDED JUNE 30, 2014

OFFICE OF THE STATE CONTROLLER (OFFICE)

FINDING 2014-101

Internal control weaknesses allowed misstatements in the statewide financial statements and note disclosures to go undetected.

Type of Finding: Significant Deficiency

Related to Prior Finding: 2013-101

Criteria: The Internal Control Integrated Framework published by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) provides a basis for organizations to design internal control procedures to ensure reliable financial reporting, effective and efficient operations, and compliance with applicable laws and regulations. Components of this framework include risk assessment and control activities. Risk assessment is the identification and analysis of various risks entities face because of changing economic, industry, regulatory, and operating conditions. It provides a basis to develop appropriate responses to manage those risks. Control activities are policies and procedures that help ensure management directives are carried out and risks are mitigated. Verifications, approvals, reconciliations, authorizations, and segregation of duties are all control activities that support this objective.

Condition: Several misstatements were identified that exceeded our trivial materiality threshold, but did not exceed materiality. The misstatements were all communicated during the audit process, however the number of errors indicate weaknesses in the internal control system that could lead to a material error that would go undetected and uncorrected. The most significant errors included incorrect financial statement classifications and note disclosure omissions, misclassifications, and inconsistencies with the financial statements.

Cause: Weaknesses in the internal controls established by the Office allowed misstatements and errors in the financial statements and note disclosures to go undetected.

Effect: The financial statements and note disclosures submitted for audit contained misstatements and errors that were not material but more than inconsequential. All errors except one were corrected before the *Comprehensive Annual Financial Report (CAFR)* was finalized. The remaining error was included on the passed on adjustments schedule.

Recommendation: We recommend that the Office improve the design and effectiveness of internal controls over the compilation of the statewide financial statements and note disclosures.

Management's View and Corrective Action Plan: *We will continue to improve our trend analysis and make modifications to our risk assessment to identify potential errors in the financial statements. Additionally, we will evaluate internal controls over the financial reporting process to ensure changes in the financial statements are subsequently reflected in the relevant note disclosures.*

Scheduled Completion Date for Corrective Action Plan: The Office did not provide a completion date. We will revisit progress on the corrective action during the 90-day follow-up.

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Auditor's Concluding Remarks: We thank the Office for its cooperation and assistance throughout the audit. We will review the status of the Office's corrective action during follow-up procedures completed 90 days after issuance of this report.

FINDING 2014-102
Internal control deficiencies over the processing of statutory transfers led to noncompliance as well as miscoded and unsupported transactions.

Type of Finding: Significant Deficiency

Criteria: The Internal Control Integrated Framework published by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) provides a basis for organizations to design internal control procedures to ensure reliable financial reporting, effective and efficient operations, and compliance with applicable laws and regulations. Components of this framework include risk assessment and control activities. Risk assessment is the identification and analysis of various risks entities face because of changing economic, industry, regulatory, and operating conditions. It provides a basis to develop appropriate responses to manage those risks. Control activities are policies and procedures that help ensure management directives are carried out and risks are mitigated. Verifications, approvals, reconciliations, authorizations, and segregation of duties are all control activities that support this objective.

In addition, Idaho Code Section 67-1001 provides that it is the duty of the State Controller to superintend the fiscal concerns of the State, with its accounting, informational, payroll, and related data processing services. To assist in this duty, Idaho Code Section 67-1007 grants authority to the State Controller to examine any documents (books, papers, accounts, vouchers, and other) of any State officers or custodians of State funds. When a transfer of funds is required, legislation generally states that the State Controller shall perform the transaction. The following legislation is relevant to exceptions noted during our audit.

- House Bill 297 from the 2013 legislative session directed the State Controller to transfer $25,000 from the State Highway Fund to the Tourism and Promotion Fund to provide matching fund support of the Gateway Visitor Centers.
- Senate Bill 1181 from the 2013 legislative session requested the State Controller to transfer $627,600 from the Idaho Millennium Income Fund to the Office of Drug Policy for the implementation of a statewide "Lock Your Meds" campaign.
- Idaho Code Section 39-107B requires the approval by the Board of Examiners for transfers requested by the agency director from the General Fund and any other funds appropriated to the Department of Environmental Quality (DEQ).

Condition: The Office processes statutory transfers based on appropriation bills, session law, or agency requests. Some transfers are calculated by the agency making the transfer and reviewed and relied upon by the Office; other transfers are calculated and initiated by the Office. In both situations, with a couple of exceptions, the Bureau Chief of Accounting Operations prepares the batch header to record the transfers; however, there is no review performed to verify that the information on the batch header is correct, accurate, and in compliance with statute.

Out of the 54 transfers tested, we noted the following exceptions:

- The $25,000 transfer from the State Highway fund to the Tourism and Promotion fund was improperly made to the Seminars and Publications fund. Upon further review, we noted that this transfer has been requested annually and improperly coded this way since fiscal year 2004.
- $627,600 was improperly transferred from the Millennium Income fund to the Office of Energy Resources instead of the Office of Drug Policy. The Office of Drug Policy notified the Office after they were unable to pay expenditures because of unavailable funds. This error was subsequently resolved.
- Idaho Code Section 72-1347B requires a monthly transfer of the unencumbered balance in excess of $6.0 million from the Workforce Development Training fund to the Employment Security Reserve fund. We determined that no transfer was required in fiscal year 2014; however, the Office was unaware of the transfer required by this code section.
- Four routine transfers requested by the DEQ lacked appropriate Board of Examiner approval. Upon further review of the Board of Examiners' minutes, none of the $18.5 million in transfers requested by this agency were approved.
- Adequate supporting documentation was not obtained or maintained for two agency initiated transfers.

Cause: Risk assessments performed by the Office did not adequately identify and address risks related to statutory transfers. The Office maintains the view that it is the agency's responsibility to ensure that transfers are correctly made and calculated. Control activities contain deficiencies to ensure statutory transfers are properly identified, approved, and supported. The prior audit recommendation to institute a secondary review of transfers was not implemented. Procedures are inadequate to prevent and detect errors and instances of noncompliance.

Effect: Our testing did not identify any material misstatements or noncompliance. However, statutory transfers totaling $275,000 over the past eleven years have not been deposited into the Tourism and Promotion fund as specified in session law. In addition, $18.5 million was transferred into the DEQ Cooperative Welfare fund, without Board of Examiners approval as required by Idaho Code Section 39-107B.

Recommendation: We recommend that the Office perform a risk assessment of statutory transfers. We also recommend that the Office design and implement control procedures to ensure that transfers are properly identified, tracked, supported, and recorded.

Management's View and Corrective Action Plan: *We have modified our review process for statutory transfers by documenting the verification of compliance with Idaho Code, verifying information is keyed correctly, and ensuring supporting documentation is attached. In addition, prior to fiscal year 2016 we will review statutory transfers to identify if there are other risks and whether our new review process can reasonably be expected to preclude those from occurring.*

Scheduled Completion Date for Corrective Action Plan: The Office did not provide a completion date. We will revisit progress on the corrective action during the 90-day follow-up.

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Auditor's Concluding Remarks: We thank the Office for its cooperation and assistance throughout the audit. We will review the status of the Office's corrective action during follow-up procedures completed 90 days after issuance of this report.

IDAHO STATE DEPARTMENT OF EDUCATION (DEPARTMENT)

FINDING 2014-103

Errors in the accounts receivable closing package were not detected or prevented by internal control procedures in place.

Type of Finding: Significant Deficiency

Criteria: Generally Accepted Accounting Principles (GAAP) for government entities require different bases of reporting for different financial statements in the state *Comprehensive Annual Financial Report (CAFR)*. The Office of the State Controller (Office) collects information from State agencies on year-end closing packages to make adjustments from cash basis financial statements to the GAAP basis financial statements included in the *CAFR*.

The accounts receivable closing package reports estimated amounts to be collected within 60 days, one year, and thereafter from the end of the fiscal year. These amounts and collection periods are necessary to comply with GAAP financial reporting requirements. Government-wide financial statements are prepared on the full accrual basis in which revenue is recognized when earned regardless of when it is collected. Governmental fund financial statements are prepared on the modified accrual basis in which revenues are recognized when they are measurable and available, which the State considers to be those collected within 60 days after the fiscal year end. Governmental funds report revenue expected to be collected after 60 days separately as a deferred inflow of resources.

The Committee of Sponsoring Organizations of the Treadway Commission (COSO) published the *Internal Control Integrated Framework* which provides a basis for organizations to design internal control procedures to ensure reliable financial reporting, effective and efficient operations, and compliance with applicable laws and regulations. A component of this framework is control activities, which are the policies and procedures that help ensure the entity's objectives are met. These activities include adequate review and authorization of financial reporting.

Condition: The Department receives federal grant funds and passes the funds through to school districts. The school districts request reimbursement for qualifying expenditures from the Department, who in turn requests reimbursement from the federal agency. The Department reports amounts due to the districts as a payable and the amounts due from the federal agencies as a receivable.

Many school districts incur qualifying expenditures prior to the State's fiscal year-end, but may not request reimbursement until many months after fiscal year-end. To accurately report accounts receivable in accordance with GAAP and the Office's closing package instructions, the Department must estimate the amount of the reimbursement requests they will pay and the corresponding federal revenue they expect to receive. The Department uses prior year data to create these estimates.

In the initial closing package, the Department reported all accounts receivable as collectible within 60 days after the end of the fiscal year. However, part of the receivable recorded was an estimate based on school district reimbursement requests. The Department did not expect to receive the estimated amount until more than 60 days after the end of the fiscal year.

At fiscal year-end, the Department had requested federal funds for qualifying expenditures but had not received the revenue. This amount was included twice in the accounts receivable calculations causing an overstatement.

Cause: The Department's internal control procedures for completing closing packages include a review prior to final submission to the Office of the State Controller. Review procedures were not performed at the level of detail necessary to detect the closing package errors.

Effect: The entire balance of accounts receivable was reported as collectible within 60 days. This caused the revenue reported as measurable and available on the governmental fund financial statements to be overstated by $7.3 million, and the amount reported as deferred inflows to be understated by the same amount. Including the same request for federal revenue twice caused the total receivable reported to be overstated by $269,673.

These errors were less than material, but more than inconsequential to the State financial statements. The errors were corrected and the accounts receivable closing package was resubmitted before the financial statements were issued. However, because the review procedures did not detect the errors, a deficiency exists in the Department's internal control that may result in future errors.

Recommendation: We recommend that the Department improve the design and implementation of internal control procedures intended to detect and prevent closing package errors.

Management's View and Corrective Action Plan: *The Department has taken steps to reduce the risk of such occurrences happening in the future by requiring additional training for employees working on the CAFR and enhancing its review process of closing packages.*

Scheduled Completion Date for Corrective Action Plan: The Department did not provide a completion date. We will revisit progress on the corrective action during the 90-day follow-up.

Contact Person: Louie Konkol
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Auditor's Concluding Remarks: We thank the Department for its cooperation and assistance throughout the audit. We will review the status of the Department's corrective action during follow-up procedures completed 90 days after issuance of this report.

IDAHO DEPARTMENT OF HEALTH AND WELFARE (DEPARTMENT)

FINDING 2014-104

Deficiencies in internal control allowed several errors in various closing packages to go undetected.

Type of Finding: Material Weakness

Related to Prior Finding: 2013-104

Criteria: The *Internal Control Integrated Framework, published by* the Committee of Sponsoring Organizations of the Treadway Commission (COSO), identifies control activities that help ensure management directives are carried out and risks are mitigated. These activities include adequate review and authorization of financial reporting and using the general ledger or other reliable records as the basis for reports. Additionally, each year, State agencies are required to report accounting information to the Office of the State Controller (Office) in the form of closing packages, which provide the details necessary to prepare the statewide *Comprehensive Annual Financial Report (CAFR).* The Office provides instructions for preparing the closing packages in accordance with Generally Accepted Accounting Principles (GAAP).

Condition: The Department's internal control system failed to prevent or detect misstatements in various closing packages. The most significant errors include:

- The Department reports total Medicaid claims that are owed but will not be submitted until after 60 days from the end of the fiscal year as an incurred but not reported amount (IBNR) and an associated amount for grants receivable. This amount was reported twice on the grants receivable closing package, as both collectable within 60 days and collectable greater than 60 days. This resulted in an overstatement of $28,677,816.
- The Office instructions for the grants receivable closing package indicate that amounts received within the first 60 days following the fiscal year-end should be recognized as revenue. The Department reported receipts received in the first 83 days following the fiscal year-end. This resulted in an overstatement of $1,274,045.
- The accounts payable closing package failed to include all amounts subject to the reporting guidelines. Audit procedures reviewed the database of transactions occurring in the first 60 days following the fiscal year-end and found qualifying amounts not included in the total amount reported. This resulted in an understatement of $561,785.
- The capital assets closing package contained an error relating to intangible assets that was carried forward from the prior year's ending balance. Our review found that the original fiscal year 2013 calculation included errors in amounts from three grant numbers. This resulted in a $20,433,305 overstatement to the fiscal year 2014 intangible assets beginning balance.

Cause: Review procedures were not performed at the level of detail necessary to detect duplicated information and other errors in closing packages prior to submission to the Office.

Effect: Subsequent to communications with the Department regarding the errors noted during the audit, the Department resubmitted information to the Office to correct the material

misstatements. The material corrections included a decrease in Grants Receivable by $28,677,816 and a decrease in the capital assets balance of $20,433,305. Other errors not material to the statewide financial statements that were not corrected include a grants receivable overstatement of $1,274,045 and an accounts payable understatement of $561,785.

Recommendation: We recommend that the Department strengthen the design and effectiveness of internal controls over the completion of closing packages to ensure accurate and reliable financial information is provided to the Office.

Management's View and Corrective Action Plan: *We agree with this finding. Corrective actions have been implemented to reduce errors in future closing packages. Procedures have been updated and documented to prevent these errors from re-occurring. Trend analysis will be documented in some areas to identify anomalies in future closing packages used to report year end estimates.*

Scheduled Completion Date for Corrective Action Plan: The Department did not provide a completion date. We will revisit progress on the corrective action during the 90-day follow-up.

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Auditor's Concluding Remarks: We thank the Department for its cooperation and assistance throughout the audit. We will review the status of the Department's corrective action during follow-up procedures completed 90 days after issuance of this report.

IDAHO STATE TAX COMMISSION (COMMISSION)

FINDING 2014-105

Errors in the data used to prepare the taxes receivable estimate were not detected by internal control procedures, resulting in misstatements.

Type of Finding: Material Weakness

Related to Prior Finding: 2013-105

Criteria: Generally Accepted Accounting Principles (GAAP) for government entities require different bases of reporting for different financial statements in the state *Comprehensive Annual Financial Report (CAFR)*. The Office of the State Controller (Office) collects information from State agencies on year-end closing packages to make adjustments from cash basis financial statements to the GAAP basis financial statements included in the *CAFR*.

The accounts receivable closing package reports the taxes receivable, net of allowances for tax refunds and doubtful accounts, and including estimated amounts to be collected within 60 days, one year, and thereafter from the end of the fiscal year. These amounts and collection periods are necessary to comply with GAAP financial reporting requirements. Government-wide financial statements are prepared on the full accrual basis in which revenue is recognized when earned

regardless of when it is collected. Governmental fund financial statements are prepared on the modified accrual basis in which revenues are recognized when they are measurable and available, which the State considers to be those collected within 60 days after the fiscal year end. Governmental funds report revenue expected to be collected after 60 days separately as a deferred inflow of resources.

The Committee of Sponsoring Organizations of the Treadway Commission (COSO) published the *Internal Control Integrated Framework* which provides a basis for organizations to design internal control procedures to ensure reliable financial reporting, effective and efficient operations, and compliance with applicable laws and regulations. Components of this framework include control activities and information and communication.

Management is responsible for establishing a process for preparing accounting estimates based on relevant, sufficient, and reliable data. Control activities are policies and procedures that help ensure management directives are carried out and risks are mitigated. These activities include adequate review and authorization of financial reporting and using the general ledger or other reliable records as the basis for reports. Information and communication is the identification, capture, and exchange of information, including adequate source documentation to support financial transactions.

Condition: Our audit procedures discovered several errors in the Commission's taxes receivable closing package, which led to misstatements. Completing the closing package includes preparing an estimate of future tax revenues based on past collections.

The Commission uses GenTax as its system of record for taxpayer information such as personal information, returns filed, payments received, and refunds paid. Financial information from GenTax is summarized and uploaded to Navision, the Commission's accounting system. Navision uploads to STARS (Statewide Accounting and Reporting System), the State's accounting system. State financial reporting is based on STARS data.

The Commission's process for estimating taxes receivable was based on reports from GenTax showing revenue collected in past years. Our testing found that GenTax reports were double counting some revenue types and not correctly counting others, which overstated past revenue collected compared to STARS data and led to a net overstatement of the taxes receivable estimate.

Also, the initial closing package submitted to the Office reported the revenue expected to be received within 30 days of fiscal year-end instead of the required 60 days, causing the available revenue to be understated and the deferred inflow of resources to be overstated.

Cause: Several factors contributed to the taxes receivable errors. The Commission has procedures in place to ensure all closing packages are reviewed prior to submission to the Office; however, the review procedures were not performed at a level of detail necessary to detect the errors.

While preparing the taxes receivable estimate, the Commission was also upgrading the GenTax system from version 6 to version 9, which required considerable time and effort from the financial staff to ensure the new version was working properly and all taxpayer data had been accurately transferred.

To increase the accuracy of the estimate, the Commission used a different method to estimate taxes receivable than in past years, which also required additional time and effort from the financial staff. This new method included estimating future audit collections and required the Commission to create new reports in GenTax version 6, which would be used only for fiscal year 2014 because of the upgrade to version 9.

Effect: Subsequent to communications with the Commission regarding the errors noted during the audit, the closing package was resubmitted to the Office to correct the material misstatements. The net effect of the errors was the following overstatements / (understatements):

- Government-wide Financial Statements, Net Taxes Receivable: $48,886,028
- Governmental Funds, General Column, Net Taxes Receivable: $72,610,838
- Governmental Funds, Transportation Column, Net Taxes Receivable: ($23,081,535)
- Governmental Funds, General Column, Deferred Inflows: $85,570,612

Recommendation: We recommend that the Commission implement control procedures to ensure closing packages are prepared in accordance with the Office instructions, and the data used to prepare the taxes receivable estimate is relevant, sufficient, and reliable.

Management's View and Corrective Action Plan: *The methodology for estimating Taxes Receivable at fiscal year-end was significantly changed this year, based on last year's recommendation, to measure returns or taxable events that have not yet been filed or reported within approximately 60 days after the end of the fiscal year. While we can be accurate to the penny with true cash received in the fiscal year, all parties recognize that there are numerous assumptions necessary to purport to capture a reasonable estimate of the unknown 'receivable' at year-end for accounting and reporting purposes. That said, we acknowledge missing the fact that the reports generated out of our older version of GenTax inadvertently double counted some payment amounts in the estimate. The estimated receivable amounts are large enough that the overstated amounts seemed reasonable, and were reviewed and discussed extensively. It was not a lack of review or effort, but a weakness in our ability to generate accurate reports under limits of time and resources, that mainly contributed to the overstatement. We believe that better information, more readily verifiable, will be available this coming year with our updated version 9 of GenTax. Again, our ultimate objective is to provide the most accurate estimate possible with the continued help, advice, and concurrence of SCO reporting staff and of LSO audit acceptance.*

Scheduled Completion Date for Corrective Action Plan: The Commission did not provide a completion date. We will revisit progress on the corrective action during the 90-day follow-up.

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Auditor's Concluding Remarks: We thank the Commission for its cooperation and assistance throughout the audit. We will review the status of the Commission's corrective action during follow-up procedures completed 90 days after issuance of this report.

IDAHO DEPARTMENT OF TRANSPORTATION (DEPARTMENT)

FINDING 2014-106

Internal controls intended to reduce the risk of misstatements in the inventory closing package were not performed at a level of detail necessary to detect significant errors.

Type of Finding: Significant Deficiency

Criteria: The Committee of Sponsoring Organizations of the Treadway Commission (COSO) published the *Internal Control Integrated Framework* which provides a basis for organizations to design internal control procedures to ensure reliable financial reporting, effective and efficient operations, and compliance with applicable laws and regulations. Components of this framework include risk assessment, control activities, and information and communication.

Control activities are the policies and procedures that help ensure the entity's objectives are met. These activities include adequate review and authorization of financial reporting, and using the general ledger or other reliable records as the basis for reports. Information and communication is the identification, capture, and exchange of information, including adequate source documentation to support financial transactions.

Each year, State agencies are required to report accounting information to the Office of the State Controller (Office) in the form of closing packages, which provide the details necessary to prepare the statewide *Comprehensive Annual Financial Report*. The Office provides instructions for preparing the closing packages in accordance with Generally Accepted Accounting Principles (GAAP).

Condition: Our testing found significant errors in reporting the value of inventory.

Anti-skid material stockpiles are stored in various sheds around the State. Each year, the volume of the piles must be measured to determine and report their value in the accounting system. The value in the accounting system for several piles did not match the value in the support documentation for volume and value calculations. We also found various errors in the calculations used to determine the value of several other piles. These errors included math errors and incorrect formulas used to calculate volume based on the shape of the piles.

The Department also keeps snowplow blades on hand in the various sheds around the State. The six district offices account for snowplow blades in different ways. Some expense them as they are purchased and show $0 on hand at year-end. Some enter all of them in inventory and track them until they are used. And some districts expense some of the blades and enter others in inventory depending on their storage.

Cause: The Department has implemented internal control procedures designed to reduce the risk of stockpile valuation errors such as reviewing measurements, volume calculations, and entries in the accounting system. However, these internal control procedures were not performed at a level of detail necessary to detect the errors that led to misstatements.

Each of the six district offices determines how they record snowplow blades in the inventory system with no guidance from the Department's headquarters. While this may be efficient operationally, the inconsistent measurement of snowplow blade inventory is not in compliance

with GAAP reporting standards and led to misstatements in reporting inventory value on the statewide financial statements.

Effect: The net effect of the inventory errors was not significant to the financial statements because the errors resulted in both overstatements and understatements. However, the errors indicate that internal controls are not effectively designed or implemented to reduce the risk of material misstatements in the statewide financial statements. Following is a summary of the errors we found:

- The calculated value of anti-skid material not matching the recorded value in the accounting system resulted in overstatements of $550,411 and understatements of $133,138, which net to an overstatement of $417,273.
- The errors in calculating the volume of the anti-skid material stockpiles resulted in overstatements of $7,903 and understatements of $564,276, which net to an understatement of $556,373.
- The inconsistent treatment of recording snowplow blades in inventory resulted in an estimated $653,201 understatement. Our estimate was the result of conversations with Department personnel and analysis of snowplow blade purchases and inventory recorded at the six districts. This process resulted in an estimate that only 50% of the snowplow blades on hand at the end of the fiscal year were recorded as inventory in the accounting system.
- All of the inventory errors net to an understatement of $792,301.

Recommendation: We recommend that the Department implement internal controls to detect errors in the anti-skid material valuation process and design and implement procedures to ensure the consistent accounting treatment of snowplow blades.

Management's View and Corrective Action Plan: *The Department agrees with this finding. The Department will implement procedures to ensure adequate review of source documentation to support financial transactions to include:*

- *The District Operations Engineer (DOE) will review counts and calculations of stockpile materials for accuracy and completeness. The DOE will initial and date the count sheets evidencing a review of accuracy, completeness and compliance with procedural requirements.*
- *The District Business Manager will reconcile the reviewed inventory counts and prepare adjustments based on approved count sheets from the DOE's supporting documentation. The District will retain original supporting documentation used in the completion of stockpile material calculations and inventory adjustments and forward a copy to Financial Services.*
- *Financial Services will reconcile balance sheet account balances to a summary compilation of the district count sheets to ensure inventory balances are accurately reflected in the year- end financial report.*
- *Snowplow blades will be accounted for as inventory while they are physically located in a centralized district warehouse and subsequently expensed when issued to a maintenance shed. Financial Services will reconcile the physical inventory count sheets to the appropriate balance sheet accounts.*

The execution of these additional controls should resolve the control weaknesses identified in the recent audit and prevent future failures of the same nature from occurring.

Scheduled Completion Date for Corrective Action Plan: The Department did not provide a completion date. We will revisit progress on the corrective action during the 90-day follow-up.

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Auditor's Concluding Remarks: We thank the Department for its cooperation and assistance throughout the audit. We will review the status of the Department's corrective action during follow-up procedures completed 90 days after issuance of this report.

STATE OF IDAHO
INTERNAL CONTROL REPORT
SCHEDULE OF PRIOR FINDINGS AND RESPONSES
FOR THE YEAR ENDED JUNE 30, 2013

		Current Status
OFFICE OF THE STATE CONTROLLER		
2013-101	Internal control weaknesses allowed misstatements in the statewide financial statements to go undetected.	Open
2013-102	Reporting for the Idle Pool in the statewide financial statements contains a $27.2 million understatement and a $20.8 million overstatement for a net understatement of $6.4 million.	Closed
IDAHO DEPARTMENT OF HEALTH AND WELFARE		
2013-103	Hospital assessments of $14.7 million were levied and collected without statutory authority.	Closed
2013-104	Financial reporting processes contain significant deficiencies in internal control allowing several errors in various closing packages to go undetected.	Open
IDAHO STATE TAX COMMISSION		
2013-105	Estimates used to determine the amount of taxes receivable accrued at year-end are not properly evaluated for reliability, resulting in misstatements.	Open
OFFICE OF THE STATE TREASURER		
2013-106	The Office of the State Treasurer inappropriately transferred investments from the Local Government Investment Pool to the Idle Pool resulting in a disproportionate share of investment losses incurred by the State.	Closed
2013-107	The Office of the State Treasurer misclassified one security in the Idle Pool investment closing package.	Closed

OFFICE OF THE STATE CONTROLLER (OFFICE)

FINDING 2013-101

Internal control weaknesses allowed misstatements in the statewide financial statements to go undetected.

Recommendation: We recommended that the Office improve the design and effectiveness of internal controls over the compilation of the statewide financial statements.

Audit Follow-up: The Office has become more conscious of ensuring consistency, accuracy, and completeness when coding and compiling information for the State's *Comprehensive Annual Financial Report (CAFR)*, especially related to coding financial information for entities that receive an outside audit. The Office made changes to the instructions for the compilation process which include comparing prior and current year coding of financial statement line items, reviewing prior errors identified by auditors and Office staff, and examining details of the notes to audited financial statements of entities that are incorporated into the *CAFR*.

In addition, the Office developed a memo to document the general treatment and resolution of classification discrepancies between the audit reports received for the colleges and universities and their respective foundations. The Office has also been in communication with foundation fiscal staff to better understand classification differences encountered between the audits received.

The Office began performing trend analyses over select closing package information during this audit period, in addition to the trend procedures they already complete on the financial statements. However, a significant number of errors, though not material individually or in the aggregate, indicate significant deficiencies in the internal controls over the preparation of the statewide financial statements and note disclosures still exist.

Current Status: Open; repeated as current year Finding 2014-101

FINDING 2013-102

Reporting for the Idle Pool in the statewide financial statements contains a $27.2 million understatement and a $20.8 million overstatement for a net understatement of $6.4 million.

Recommendation: We recommended that the Office continue to gain a greater understanding of the underlying data in STARS and reported by Office of the State Treasurer for the Idle Pool. This understanding should be used to develop an appropriate method of evaluating the mark-to-market adjustment and reconciling cash to supported reports.

Audit Follow-up: The Office held meetings and continues to be in communication with the Office of the State Treasurer to gain a better understanding of their systems, processes, and the information they provide. Additionally, the Office of the State Treasurer obtained an independent audit of the investment pools for fiscal year 2014. The independent audit results were provided to the Office to be included in the statewide *Comprehensive Annual Financial Report* and a mark-

to-market adjustment was calculated and completed by the Office. We noted no misstatements or errors.

Current Status: Closed

IDAHO DEPARTMENT OF HEALTH AND WELFARE (DEPARTMENT)

FINDING 2013-103
Hospital assessments of $14.7 million were levied and collected without statutory authority.

Recommendation: We recommended that the Department strengthen internal controls over compliance with laws and regulations to ensure fees charged and collected are appropriately authorized. We also recommended that the Department clarify the purpose and legislative intent for the hospital assessment fees and, if necessary, work to amend Idaho Code Section 56-1404.

Audit Follow-up: The Department implemented new procedures relating to the review of legislation pertaining to hospital assessments and other areas with potential financial impact to the Department. Review by members of the Department's Administrative Rules Unit is now logged on a tracking document, and proposed legislation is monitored as it moves through the processes involved in becoming law. Additionally, House Bill 561 was passed and signed into law effective March 26, 2014. It removes the fiscal year limitations on the authority to levy and collect hospital assessments.

Current Status: Closed

FINDING 2013-104
Financial reporting processes contain significant deficiencies in internal control allowing several errors in various closing packages to go undetected.

Recommendation: We recommended that the Department strengthen the design and effectiveness of internal controls over the completion of closing packages. We also recommended that the Department enhance the monitoring of internal controls to ensure they are operating as designed to comply with Generally Accepted Accounting Principles (GAAP) reporting requirements and Office of the State Controller closing package instructions. We further recommended that the Department strengthen the review process to ensure accurate and reliable financial information is provided to the Office.

Audit Follow-up: The Department made changes to staff assignments to ensure those staff responsible for duties related to closing package preparation obtained the necessary training. Additionally, new procedures were implemented for tracking progress of assigned tasks related to closing package preparation, such as research of new guidance. However, material errors were still identified during the fiscal year 2014 audit.

Current Status: Open; repeated as current year Finding 2014-104

IDAHO STATE TAX COMMISSION (COMMISSION)

FINDING 2013-105

Estimates used to determine the amount of taxes receivable accrued at year-end are not properly evaluated for reliability, resulting in misstatements.

Recommendation: We recommended that the Commission implement closing package procedures to ensure that all tax types and collection methods are considered in the estimate for taxes receivable and that the estimate is compared to actual results for reasonableness.

Audit Follow-up: The Commission established a new method of estimating taxes receivable at year-end, based on looking back at the previous five years of collection data, which includes all tax types and collection methods. To implement this new method, the Commission created new reports in their stand alone tax accounting system, GenTax version 6. These reports were intended to enable the Commission to create the estimate and later compare the estimate to the actual amounts collected. The Commission is upgrading GenTax to version 9, which will be completed in fiscal year 2015. Version 9 has greater reporting and user interface capabilities that will streamline the process of creating and verifying the taxes receivable estimate. The new method of creating the taxes receivable estimate, and the additional step of comparing the estimate to the actual amounts collected, address the recommendation. However, material errors were still identified during the fiscal year 2014 audit.

Current Status: Open; repeated as current year Finding 2014-105

OFFICE OF THE STATE TREASURER (OFFICE)

FINDING 2013-106

The Office of the State Treasurer inappropriately transferred investments from the Local Government Investment Pool to the Idle Pool resulting in a disproportionate share of investment losses incurred by the State.

Recommendation: We recommended that the Office strengthen processes to reduce the risk of management override of controls. This could include the addition of an independent oversight function in the form an investment board and financial consultants with specific expertise related to investment pools and activities. We also recommended that the Office evaluate the structure of all investments, including securities lending agreements, to ensure the preservation of their fiduciary duty of undivided loyalty to both the State's Idle Pool and the Local Government Investment Pool (LGIP). The Office should design and implement appropriate internal controls to segregate investment activities and decision making between the two pools. We further recommended that the Office review the Securities Lending Agreement activity since July 1, 2008, to identify all losses incurred by the Idle Pool due to the inappropriate reallocation of assets.

Audit Follow-up: The first two recommendations were addressed through the enactment of Senate Bill No. 1350 during the 2014 legislative session. This legislation created a State Treasurer Investment Advisory Board (Board). The Board will provide recommendations on the types and kinds of investments made by the State Treasurer as well as investment policies governing the investment of funds by the State Treasurer. As of the issuance of this report, the

Board members have been appointed. Meetings of the board will commence after Senate confirmations have been completed. Additionally, the legislation amended Idaho Code Section 67-1210A and added Idaho Code Section 67-1210B to remove securities lending agreements as an allowable investment of the State Treasurer in the future.

Subsequent to completion of the *90-Day Follow-Up Report* issued June 26, 2014, the Office provided documentation to support a completed review of the securities lending transactions for reallocation of assets between investment portfolios directed by the Office. The reviews included analysis of securities lending statements and searches of electronic records including email communications, hard drives, and server archives for topics related to securities lending transactions. The Office determined that there were no further reallocations to report.

Current Status: Closed

FINDING 2013-107
The Office of the State Treasurer misclassified one security in the Idle Pool investment closing package.

Recommendation: We recommended that the Office strengthen the review process over closing package preparation to ensure that amounts reported in the investment pool schedules are properly classified.

Audit Follow-up: The Office obtained an independent audit of the investment pools for fiscal year 2014. The independent audit results were provided to the Office of the State Controller to be included in the statewide *Comprehensive Annual Financial Report* and no misstatements were noted in the presentation included in the statewide financial statements and note disclosures.

Current Status: Closed

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