



State of Texas Financial Portion of the

Statewide Single Audit Report for the Year Ended August 31, 2016

February 2017

Report No. 17-555



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*Statewide Single Audit Report for the Year
Ended August 31, 2016*

SAO Report No. 17-555
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Overall Conclusion

In our audit opinion dated February 21, 2017, we concluded that the basic financial statements for the State of Texas presented fairly, in all material respects, the financial position and activities of the State for the fiscal year ended August 31, 2016. The Office of the Comptroller of Public Accounts (**Comptroller's Office**) prepared the basic financial statements and published our audit opinion as part of the Comprehensive Annual Financial Report (CAFR) for fiscal year 2016, which it intends to post on its Web site at http://www.texas Transparency.org/State_Finance/Budget_Finance/Reports/Comprehensive_Annual_Financial/.

The consolidated financial statements provide a **comprehensive view of the State's financial activities** during the fiscal year and an overall picture of the financial position of the State at the end of the fiscal year. **Compiling the State's consolidated financial statements** is a major undertaking; those financial statements combine financial information for more than 200 state agencies and higher education institutions.

For fiscal year 2016, the State implemented Governmental Accounting Standards Board (GASB) Statement No. 72, *Fair Value Measurement and Application*. The State restated its beginning net position and fund balance as of September 1, 2015, to reflect the effect of the implementation of that new statement. As a result, the State restated the amount for sovereign lands, previously recorded at historical cost, at fair value with a \$1.9 billion restatement increase in the permanent school fund and governmental activities and a \$5.3 billion restatement increase in the colleges and universities fund and business-type activities.

On August 31, 2016, the Economic Stabilization Fund balance was \$10.2 billion. That amount consisted primarily of \$7.9 billion in cash in the State Treasury, \$1.8 billion in current and non-current investments, and \$439.5 million due from the General Revenue Fund. The \$439.5 million due from the General Revenue Fund was transferred to the Economic Stabilization Fund in November 2016. The Economic Stabilization Fund is reported in the General Fund on the governmental fund financial statements and in Governmental Activities on the government-wide financial statements.

Basic Financial Statements

The State's basic financial statements include both government-wide and fund financial statements:

- Government-wide financial statements display information about the State as a whole, except for its fiduciary activities.
- Fund financial statements for the **State's governmental and proprietary funds** provide information on the major funds individually and nonmajor funds in the aggregate. Fiduciary statements include financial information for fiduciary funds.

Source: Governmental Accounting Standards Board Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*.

This audit was conducted in accordance with Texas Government Code, Section 2101.014.

For more information regarding this report, please contact Angelica Ramirez, Audit Manager, or Lisa Collier, First Assistant State Auditor, at (512) 936-9500.

The fiscal year 2016 consolidated financial statements convey the use of approximately \$140.4 billion¹ during the fiscal year, an increase of \$6.7 billion or 5.0 percent since the prior fiscal year. The majority of the increase was related to Education and Health and Human Services expenses. **The State's assets on August 31, 2016, totaled \$290.0 billion, an increase of \$19.8 billion or 7.3 percent since the prior fiscal year.** Net position, which increased by \$11.7 billion or 7.9 percent to \$159.4 billion in fiscal 2016, was affected by a number of factors. Cash and cash equivalents decreased by \$5.1 billion from fiscal year 2015. Unrestricted non-current investments increased by \$7.1 billion. **The State's bonded indebtedness** was \$47.1 billion, which included new issuances of \$7 billion in state bonds to finance new construction, housing, water conservation, and other projects. Approximately \$4.5 billion in bonded debt was retired or refunded during the fiscal year.

Auditing financial statements is not limited to reviewing the numbers in those **statements. Conducting this audit also requires the State Auditor's Office to obtain** a sufficient understanding of the agencies and higher education institutions and their operating environments—including obtaining an understanding of the internal controls over systems and processes that the agencies and higher education institutions use to record their financial activities—to assess the risk of material misstatement of the financial statements. Through that effort, auditors identified specific weaknesses that four agencies should correct to improve the reliability of their financial information. Those weaknesses are discussed in Chapter 2-A through Chapter 2-C of this report.

The State Auditor's Office also audited the State's Schedule of Expenditures of Federal Awards (SEFA) in relation to the CAFR for fiscal year 2016. The Comptroller's Office prepares the SEFA by using self-reported SEFA data from all state agencies and higher education institutions that made federal expenditures **during the fiscal year. The State Auditor's Office and KPMG LLP (KPMG) audited the** processes for preparing SEFA information at 15 agencies and 10 higher education institutions. Auditors identified errors related to the SEFA information at two agencies and five higher education institutions. Those errors are discussed in Chapter 2-D of this report.

Auditors also performed prior-year finding follow-up work at seven entities and determined that recommendations for two of those findings were not yet fully implemented (see the Summary Schedule of Prior Year Audit Findings).

¹ The \$140.4 billion in annual expenditures exceeded the \$105.1 billion appropriated for fiscal year 2016 primarily because:

- Certain expenditures (such as higher education institutions' expenditures of funds held outside the State Treasury) are included in the Comprehensive Annual Financial Report (CAFR) but are not included in the General Appropriations Act (GAA).
- The CAFR presents actual expenditures of federal funds, while the GAA presents estimated amounts for federal funds.
- Additional pension-related expenditures were recorded in the CAFR to account for the effects of the implementation of GASB Statements Nos. 68 and 71 that are not included in the GAA.

The State Auditor's Office conducts this audit so that the State can comply with federal legislation (the Single Audit Act Amendments of 1996); state statute (Texas Government Code, Section 403.013(c)); and grant requirements to obtain an opinion regarding the fair presentation of its basic financial statements and a report on internal controls related to those statements. The results of this audit may be used by bond-rating companies, the Legislature, and federal agencies that award grants.

Summary of Management's Response

At the end of each chapter in this report, auditors made recommendations to address the issues identified during this audit. The agencies and higher education institutions agreed with the recommendations in this report.

Audit Objective and Scope

The audit objective was to determine whether **the State's basic financial** statements present fairly, in all material respects, the consolidated balances and activities for the State of Texas for the fiscal year ended August 31, 2016.

The Statewide Single Audit is an annual audit for the State of Texas. It is conducted so that the State complies with (1) the Single Audit Act Amendments of 1996 and Title 2, U.S. Code of Federal Regulations, Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) and (2) state statute requiring that an audited CAFR be provided to the Governor (Texas Government Code, Section 403.013(c)).

The scope of the financial portion of the Statewide Single Audit included an audit **of the State's basic financial statements and a review of significant controls over** financial reporting and compliance with applicable requirements.

The scope of the federal compliance portion of the Statewide Single Audit included an **audit of the State's SEFA, a review of compliance for each major program, and a review of significant controls over federal compliance. The State Auditor's Office** contracted with KPMG to provide an opinion on compliance for each major program and internal control **over compliance. The State Auditor's Office provided an opinion on the State's SEFA, in relation to its opinion on the CAFR. Information on** the federal compliance portion of the Statewide Single Audit is included in a separate report entitled *State of Texas Federal Portion of the Statewide Single Audit Report for the Fiscal Year Ended August 31, 2016*, by KPMG.

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Independent Auditor's Report

*State of Texas Financial Portion of the
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Summary of Auditor's Results

Financial Statements

The State's consolidated financial statements, in all material respects, were in conformity with accounting principles generally accepted in the United States of America as noted in our opinion dated February 21, 2017.

- | | |
|----------------------------------------------------------------------------------|------------|
| 1. Type of auditor's report issued: | Unmodified |
| 2. Internal control over financial reporting: | |
| a. Material weakness identified? | Yes |
| b. Significant deficiencies identified not considered to be material weaknesses? | Yes |
| c. Noncompliance material to financial statements noted? | No |

Federal Awards

A finding regarding the Schedule of Expenditures of Federal Awards for fiscal year 2016 was included in Chapter 2-D of this report. All other fiscal year 2016 federal award information was issued in a separate report (see *State of Texas Federal Portion of the Statewide Single Audit Report for the Fiscal Year Ended August 31, 2016*, by KPMG LLP).



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

The Honorable Greg Abbott, Governor
The Honorable Glenn Hegar, Comptroller of Public Accounts
The Honorable Dan Patrick, Lieutenant Governor
The Honorable Joe Straus III, Speaker of the House of Representatives
and
Members of the Legislature, State of Texas

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 consolidated financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate discretely presented component units and remaining fund information of the State of Texas as of and for the year ended August 31, 2016, and the related notes to the consolidated financial statements, which collectively comprise the State of Texas's basic financial statements, and have issued our report thereon dated February 21, 2017. Our report includes a reference to other auditors who audited the financial statements of the Department of Transportation, the Texas Lottery Commission, and the University of Texas System as described in our report on the State of Texas's consolidated 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 other auditors.

Internal Control Over Financial Reporting

In planning and performing our audit of the consolidated financial statements, we considered the State'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 consolidated financial statements, but not for the purpose of expressing an opinion on the effectiveness of the State's internal control. Accordingly, we do not express an opinion on the effectiveness of the State's internal control.

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 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 following deficiencies described in the accompanying schedule of findings and responses to be material weaknesses.

Summary of Finding	
Agency or Higher Education Institution	Finding Number
Office of the Comptroller of Public Accounts	17-555-01
Texas Workforce Commission	17-555-02

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 following deficiencies described in the accompanying schedule of findings and responses to be significant deficiencies.

Summary of Findings	
Agency or Higher Education Institution	Finding Numbers
Health and Human Services Commission and Department of Aging and Disability Services	17-555-03
Multiple agencies and higher education institutions	17-555-04

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the State’s consolidated 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 disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Auditors communicated certain issues that were not material or significant to the audit objectives in writing to the management of audited entities.

Other Work Performed by the State Auditor's Office

We issued opinions on the following financial statements, which are consolidated into the basic financial statements of the State of Texas:

- *A Report on the Audit of the Teacher Retirement System's Fiscal Year 2016 Financial Statements* (State Auditor's Office Report No. 17-015, November 2016).
- *A Report on the Audit of the Employees Retirement System's Fiscal Year 2016 Financial Statements* (State Auditor's Office Report No. 17-016, December 2016).
- *A Report on the Audit of the Department of Housing and Community Affairs' Fiscal Year 2016 Financial Statements* (State Auditor's Office Report No. 17-018, December 2016).
- *A Report on the Audit of the Permanent School Fund's Fiscal Year 2016 Financial Statements* (State Auditor's Office Report No. 17-019, January 2017).

This report, insofar as it relates to the entities listed above, 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 other auditors.

State's Responses to Findings

The State's responses to the findings identified in our audit are included in the accompanying schedule of findings and responses. The State'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 State'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 State's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Sincerely,

Lisa R. Collier, CPA, CFE, CIDA
First Assistant State Auditor

February 21, 2017

Schedule of Findings and Responses

*State of Texas Financial Portion of the
Statewide Single Audit Report for the
Year Ended August 31, 2016*

Financial Statement Findings

This chapter identifies the material weaknesses and significant deficiencies related to the financial statements that are required to be reported in accordance with *Government Auditing Standards*.

Chapter 2-A

The Office of the Comptroller of Public Accounts Should Improve Certain Controls Over Financial Reporting

Issue 1

The Office of the Comptroller of Public Accounts Should Strengthen Its Processes for Reviewing Adjusting Journal Entries and Its Annual Financial Report

Reference No. 17-555-01
(Prior Audit Issue 16-555-02)

Type of finding: Material Weakness

The Office of the Comptroller of Public Accounts – Fiscal Program Department (Comptroller’s Office) had a process to review adjusting journal entries and its annual financial report. However, that process did not detect an error that resulted in materially misstated fiscal year 2016 financial

statements and in the State’s accounting system. As a result, auditors concluded that there was a material weakness in internal control at the Comptroller’s Office (see text box for additional information on material weaknesses).

Material Weakness in Internal Control

A material weakness is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of an entity’s financial statements will not be prevented, or detected and corrected, on a timely basis.

Source: American Institute of Certified Public Accountants AU-C Section 265, *Communicating Internal Control Related Matters Identified in an Audit*.

The Comptroller’s Office’s financial statements misclassified fund balances by \$1.8 billion on the fund financial statements and in the State’s accounting system. Specifically, the Comptroller’s Office incorrectly classified \$1.8 billion in the fund balance for the Economic Stabilization Fund as restricted when it should have been classified as unassigned.

The Comptroller’s Office’s review process for its annual financial report did not detect the error discussed above. In addition, the Comptroller’s Office did not identify the error before it finalized its annual financial report.

To ensure that the issue discussed above did not affect the accuracy of the State’s Comprehensive Annual Financial Report, the Comptroller’s Office made appropriate adjustments to the fund balance during its preparation of the State’s Comprehensive Annual Financial Report.

Recommendation

The Comptroller's Office should continue to strengthen its process for reviewing adjusting journal entries and its annual financial report to ensure that it prepares, presents, and submits materially accurate financial information.

Views of Responsible Officials

Accepted. The Comptroller will institute additional independent review processes to ensure that adjusting journal entries and the resulting annual financial report are accurate prior to completion. The additional review steps will be formalized in policies and procedures and implemented prior to the next annual financial reporting period.

Corrective Action Plan

Internal policies and procedures will be revised to include additional independent review steps. Staff performing the review will receive additional training to ensure that they understand the new process.

Implementation Date: May 31, 2017

Responsible Person: Fiscal Integrity Manager

Chapter 2-B

The Texas Workforce Commission Should Improve Certain Controls Over Financial Reporting

Issue 1

The Texas Workforce Commission Should Strengthen Its Financial Reporting Processes

Reference No. 17-555-02

Type of finding: Material Weakness

The Texas Workforce Commission (Commission) had a process to ensure that the financial information it reported to the State's accounting system reconciled to the Commission's internal accounting system. However, that process did not detect an error that resulted in the Commission submitting materially misstated fiscal year 2016 financial information to the State's accounting system. As a result, auditors concluded that there was a material weakness in internal control at the Commission. (See text box in Chapter 2-A for additional information on material weaknesses.)

As a result, the Commission misclassified the net position balances that it submitted to the State's accounting system. Specifically, the Commission incorrectly classified \$1.3 billion in net position for the Unemployment Trust Funds as unrestricted when those funds should have been classified as restricted for unemployment and restricted for debt retirement.

The Office of the Comptroller of Public Accounts' (Comptroller's Office) *Reporting Requirements for Fiscal Year 2016 Annual Financial Reports of State Agencies and Universities* required each agency to ensure and certify that its financial data correctly reflected its financial position as of August 31, 2016, as recorded in the State's accounting system and the agency's internal accounting system. That included accurately classifying an agency's net position.

The Commission correctly presented the net position balances in its fiscal year 2016 annual financial report; however, its financial reporting process did not detect the error in the State's accounting system. The Comptroller's Office uses the State's accounting system to produce the State's Comprehensive Annual Financial Report. Therefore, the submission of incorrect financial data to the State's accounting system could lead the State to produce materially misstated financial statements.

To ensure that the issue discussed above did not affect the accuracy of the State's Comprehensive Annual Financial Report, the Comptroller's Office made appropriate adjustments to the net position balances during its preparation of the State's Comprehensive Annual Financial Report.

Recommendation

The Commission should strengthen its process for reviewing the financial information that it submits to the State's accounting system to ensure that it submits materially accurate financial information.

Views of Responsible Officials

The Commission's Finance staff has determined that current procedures need improvement to ensure the net position of the Unemployment Trust Fund is properly classified between restricted or unrestricted in the State's accounting system. The Commission's Finance staff took immediate action to provide corrected information to the Comptroller's Office when the net position classification issue was brought to their attention.

The Unemployment Trust Fund was accurately reported as restricted in the Commission's printed Annual Financial Report, however the Commission's

internal review procedures did not detect that the Unemployment Trust Fund was reported as unrestricted in the State's accounting system. It is important to note that this net position classification issue did not create a risk that Unemployment Trust Funds would be used for any purpose other than the payment of unemployment benefits.

Corrective Action Plan

The Commission is revising its procedures for reviewing financial information to ensure accuracy within the State's accounting system. The revised procedures will address key areas in the preparation and independent review process of the annual financial report prior to submission to the Comptroller's Office. In addition, the Commission will enhance its training program of staff assigned to the preparation and submission of the annual financial report.

Implementation Date: July 1, 2017

Responsible Person: Director of Accounting Services and Revenue and Trust Management

Chapter 2-C

The Health and Human Services Commission and the Department of Aging and Disability Services Should Improve Controls Over Information Technology

Issue 1

The Health and Human Services Commission and the Department of Aging and Disability Services Should Improve Their Management and Monitoring of Certain Information Technology

Reference No. 17-555-03
(Prior Audit Issues 14-555-03, 15-555-02, and 16-555-03)

Type of finding: Significant Deficiency

Auditors identified significant weaknesses in controls over the information technology that the Health and Human Services Commission (Commission) and the Department of Aging and Disability Services (Department) used to process claims from the Home and Community Based Services Program and the Texas Home Living Waiver Program (Programs). The Commission and the Department did not fully implement recommendations to improve information technology controls that the State Auditor's Office made in its audit reports for fiscal years 2013, 2014, and 2015. Specifically, the Commission and the Department:

- Did not consistently monitor user access.
- Did not consistently disable inactive user accounts.
- Did not consistently modify or remove inappropriate access.
- Did not consistently enforce the Commission's policies and procedures for passwords.

To protect the integrity of their information, the Commission and the Department should improve their management and monitoring of the information technology that the Programs use.

The Department is the owner of the Programs' data, and the Commission is responsible for administering components of the information technology that the Programs use, including user access.

User Access

The Commission and Department took steps to remove some inappropriate user accounts that auditors identified in the prior-year audit; however, weaknesses in access to the information technology the Programs use continued to exist in fiscal year 2016. Conducting periodic reviews of user access is important in identifying potential unauthorized access. Not having a strong user access review process increases the risk of unauthorized or undetected access to, modification of, disclosure of, or destruction of data.

Auditors reviewed 6,255 user accounts associated with the mainframe that houses the Intellectual Disabilities Client Assessment Registration (ID CARE) system. A total of 2,480 (40 percent) of those user accounts were inactive. Specifically:

- No individuals had ever logged into the mainframe that houses ID CARE through 792 of those user accounts.
- No individuals had logged into the mainframe that houses ID CARE in the 90-day period preceding October 18, 2016, through 1,688 of those user accounts. In addition, no individuals had logged into the mainframe that houses ID CARE in fiscal year 2016 through 901 of those 1,688 user accounts.

Auditors also reviewed user accounts that were associated with centralized Program operations and identified the following issues:

- Four (67 percent) of 6 user accounts tested had inappropriate administrative access to a database for ID CARE based on the users' job responsibilities.

- Twenty-six (55 percent) of 47 user accounts tested had inappropriate administrative access permissions based on their job responsibilities.

Title 1, Texas Administrative Code, Chapter 202, requires agencies to develop information technology policies and procedures. Commission information technology security standards and guidelines require user accounts to be restricted to appropriate individuals, require application owners to review user accounts at least every 12 months, and require user accounts to be disabled after 60 days of non-use for administrative accounts and after 90 days of non-use for nonadministrative accounts.

Passwords

The password configurations for a database and server the Programs used to process payments did not meet the minimum requirements in the Commission's policies and procedures for passwords. When entities do not require users to have strong passwords that allows users to reuse passwords frequently or make an excessive number of login attempts, which increases the risk of unauthorized access to systems and data.

Recommendations

The Commission and the Department should:

- Develop and implement a process for reviewing user access to information technology that the Programs use.
- Consistently disable user accounts in compliance with Commission policies and procedures.
- Ensure that password configurations for the databases and servers the Programs use comply with Commission policies and procedures.

Views of Responsible Officials

HHS IT acknowledges the findings, as the identified conditions did exist during the audit scope timeframe. HHS IT accepts the recommendations.

Work has since been completed to resolve the issues in the first two recommendations.

The Client Assessment Registration (CARE) system password configuration is not fully compliant with the current HHS Enterprise Information Security Standards and Guidelines (EISSG) due to a system limitation stemming from the age of this infrastructure.

Work is in progress to bring the database and server password configurations into compliance with the EISSG.

Corrective Action Plan

HHS IT's manual process for account maintenance and de-provisioning is as follows:

The Health and Human Services Commission (HHSC) provides the Department of Aging and Disability Services (DADS) application owners with monthly user lists for review and appropriate action. Upon notification via the appropriate paper form from a supervisor, business owner or application owner, HHS IT will promptly add, modify, or terminate access for users. A detailed version of the process is maintained on the HHSC Enterprise Identity and Access Management (EIAM) SharePoint site.

In November 2016, DADS and HHSC completed an account cleanup project which removed over 24,000 out of date accounts from the CARE mainframe platform which supports Home and Community Based Services Program and the Texas Home Living Waiver Program. This was a carefully executed interdepartmental effort to remediate and remove accounts which had not been used and/or were inactivated for a substantial period of time. The intent of this process was to clear the backlog of improperly stored/maintained accounts to allow the monthly manual process described above to appropriately handle ongoing changes.

The following steps will be taken by DADS IT Applications to address the password compliance recommendation:

- 1. Notify the Chief Information Security Office (CISO) of the non EISSG compliant system and the systemic reason for that noncompliance.*
- 2. Begin the security review process to request an exception to the EISSG due to intrinsic system limitations.*
- 3. Seek CISO guidance on how to proceed and/or what controls may be available in the HHS IT Security portfolio to remediate this issue.*
- 4. Notify EIAM of any resultant system changes which could affect the (de)provisioning processes currently in place.*

*Implementation Date: November 2016 - Account Cleanup Project
May 2017 - Password Compliance*

*Responsible Person: Director, IT Applications Management,
Applications Management - Applications
Support*

*HHSC IT Applications updated the database password configurations on
February 10, 2017 bringing them into compliance with the EISSG.*

Implementation Date: February 2017

*Responsible Person: Director, IT Enterprise Services, IT HHS
Applications*

*HHSC IT Data Center Services will coordinate with the DCS service provider,
Atos, to update the server password configurations to be in compliance with
the EISSG.*

Implementation Date: March 2017

*Responsible Person: Director, IT Sourcing Management
Services*

State Entities Should Strengthen the Preparation and Review of Their Schedules of Expenditures of Federal Awards

Reference No. 17-555-04

(Prior Audit Issues 16-555-04, 15-555-05, 14-555-07, 13-555-02, 12-555-05, 11-555-17, 10-555-26, and 09-555-19)

Type of finding: Significant Deficiency

Schedule of Expenditures of Federal Awards (SEFA)

Each state entity that expends federal awards is required to prepare a Schedule of Expenditures of Federal Awards (SEFA) and submit it to the Office of the **Comptroller of Public Accounts (Comptroller's Office)**. The expenditures are to be presented in the SEFA on the same accounting basis as each state **entity's fund financial statements**.

Federal awards include federal financial assistance and federal cost-reimbursement contracts that non-federal entities receive directly from federal awarding agencies or indirectly from pass-through entities [Title 2, Code of Federal Regulations (CFR), Section 200.38].

Federal financial assistance includes any assistance that non-federal entities receive or administer in the form of grants, loans, loan guarantees, non-cash contributions or donations of property (including donated surplus property), cooperative agreements, interest subsidies, insurance, food commodities, direct appropriations, and other assistance [Title 2, CFR, Section 200.40].

Source: *Reporting Requirements for Annual Financial Reports of State Agencies and Universities*, **Comptroller's Office**.

The agencies and higher education institutions discussed below did not appropriately prepare or adequately review their fiscal year 2016 Schedule of Expenditures of Federal Awards (SEFAs) (see text box for additional information). Therefore, the SEFAs that they submitted to the Office of the Comptroller of Public Accounts (Comptroller's Office) contained errors.

The agencies and higher education institutions discussed below reported \$1,840,859,646 in federal expenditures, or 3 percent of the total federal expenditures the State of Texas reported for fiscal year 2016. The errors listed below were not material to the fiscal year 2016 SEFA for the State of Texas or to the fiscal year 2016 Comprehensive Annual Financial Report for the State of Texas. However, collectively, they represent control weaknesses that could be significant to the State's SEFA.

The University of Texas at Arlington

The University of Texas at Arlington (UT-Arlington) incorrectly excluded \$727,126 from the notes to its SEFA for the beginning balance of outstanding loans for the Federal Perkins Loan Program. As a result, UT-Arlington understated the beginning and ending balance of outstanding Federal Perkins Loans by \$727,126 in the notes to its SEFA.

Recommendation

UT-Arlington should strengthen its SEFA preparation and review process to help ensure that it prepares its SEFA beginning and ending balances correctly for the Federal Perkins Loan Program amounts that it reports in the notes to its SEFA.

Views of Responsible Officials

The University acknowledges and agrees with the findings. Because specific direction concerning the components of the calculation of the beginning balance on Note 3 is not available in the SEFA instructions, the University will make note in its internal procedures on SEFA preparation the need to exclude the allowance for doubtful accounts included in its general ledger balance to ensure the outstanding beginning and ending balances of Federal Perkins Loans reported on Note 3 is not understated.

Corrective Action Plan

The University has made note of the change in procedure and, upon preparation of the SEFA for FY 2017, will ensure that the allowance for doubtful accounts included in its general ledger balance will be excluded from the balance reported on Note 3.

Implementation Date: September 30, 2017

Responsible Persons: Associate Vice President for Business Affairs and Controller

The University of Texas at Austin

On its SEFA, the University of Texas at Austin (UT-Austin):

- Incorrectly included \$326,712 for 1 Student Financial Assistance Catalog of Federal Domestic Assistance program (CFDA) due to a miscalculation of its administrative costs. As a result, UT-Austin overstated federal revenue by \$326,712 in note 2 to its SEFA.
- Incorrectly classified \$92,853 in expenditures related to 1 generic CFDA.

Recommendation

UT-Austin should strengthen its SEFA preparation and review process to help ensure that it prepares its SEFA correctly, including ensuring that it calculates and reports the appropriate administrative costs and reports correct CFDA's for each federal award.

Views of Responsible Officials

The University acknowledges and agrees with the findings. Through analysis of the exceptions identified in the audit, the University will work to develop and implement corrective action to further improve the processes.

Corrective Action Plan

Management is committed to improving the review processes to ensure the SEFA submission is accurate. Documentation has been revised and provided to the Texas State Auditor's Office to ensure administrative costs are correctly calculated.

Implementation Date: August 2017

*Responsible Persons: Assistant Director, Office of Sponsored Projects
Finance Manager, Office of Accounting &
Financial Management*

Management will continue to review generic CFDA's during the summer in preparation for the annual financial report. Specifically, management will review awards that have been established on credit, and at the time of award ensure that the correct CFDA has been used.

Implementation Date August 2017

*Responsible Persons: Assistant Director, Office of Sponsored Projects
Finance Manager, Office of Accounting &
Financial Management*

The University of Texas at El Paso

On its SEFA, the University of Texas at El Paso (UTEP) incorrectly included \$1,122,553 in expenditures outside of fiscal year 2016 for 2 Student Financial Assistance CFDA's and incorrectly excluded \$7,667 in expenditures outside of fiscal year 2016 for 3 Student Financial Assistance CFDA's. As a result, UTEP (1) overstated federal revenue and reconciling items by \$1,114,886 in note 2 to its SEFA and (2) overstated new loans processed for the Federal Direct Student Loans Program by \$1,011,247 in note 3 to its SEFA.

Recommendation

UTEP should strengthen its SEFA preparation and review process to help ensure that it prepares its SEFA correctly, including ensuring that it reports expenditures only for the appropriate fiscal year.

Views of Responsible Officials

Management concurs and will continue to improve the institutional processes in place to ensure the accuracy and completeness of the SEFA report.

Corrective Action Plan

The University will continue to strengthen its SEFA preparation and review process to ensure that the SEFA is prepared correctly and that the SEFA information submitted to the Comptroller's Office is complete and accurate. UTEP will further develop its internal operational and financial procedures for the SEFA preparation and review process resulting in a more timely identification and correction, if any, of variances prior to the SEFA submission.

Implementation Date: June 2017

Responsible Person: Comptroller

The University of Texas Rio Grande Valley

On its SEFA, the University of Texas Rio Grande Valley (UTRGV) incorrectly included \$1,175,524 in expenditures for 4 Student Financial Assistance CFDA's and 1 other CFDA. Specifically, it incorrectly included \$1,084,540 in expenditures that occurred prior to the start of fiscal year 2016 for 4 Student Financial Assistance CFDA's. For the remaining CFDA, UTRGV incorrectly included expenditures that it did not receive as federal funds.

As a result, UTRGV (1) overstated expenditures on its SEFA by \$1,175,524 for 5 CFDA's; (2) overstated note 2 regarding reconciliation by \$1,084,540 to its SEFA; and (3) overstated new loans processed for the Federal Direct Student Loans Program by \$796,748 in note 3 to its SEFA.

Recommendation

UTRGV should strengthen its SEFA preparation and review process to help ensure that it prepares its SEFA correctly, including ensuring that it reports expenditures only for the appropriate fiscal year and that it received as federal funds.

Views of Responsible Officials

The University of Texas Rio Grande Valley (UTRGV) acknowledges and agrees with the findings. Through analysis of the exceptions identified in the audit, the UTRGV will work to develop and implement corrective action to further improve the processes.

Corrective Action Plan

UTRGV has already implemented significant process enhancements in this area. Communications between the Financial Aid Office, Business Information Systems and Student Accounting Services is in place in order to meet a

definitive cutoff date and time for all financial aid expenditures that occur on the last day of the fiscal year. This will help ensure that expenditures are reported in the appropriate fiscal year. This plan was implemented on August 31, 2016 and produced the expected cutoff results for Banner and Oracle financials at August 31, 2016 in preparation for proper fiscal year 2017 reporting. UTRGV will strengthen its internal operational and financial procedures for the SEFA preparation to warrant a complete and accurate submission.

Implementation Date: January 1, 2017

Responsible Person: Director of Student Accounting Services

UTRGV has implemented a process of funding source and relationship verification. When an award is received, the Office of Sponsored Programs (OSP) and Grants and Contracts (G&C) will confirm the funding source and relationship before the project is created in the accounting system. When OSP is notified that a proposal has been funded, OSP will verify the funding source and relationship based on the fully executed documents. OSP will then forward the award documentation to G&C. G&C will perform a second review of the fully executed documents to verify the funding source and relationship status. If there are any questions, the funding agency will be contacted for clarification on the funding source or relationship status. Once the funding source and relationship status are verified, the project will be set up in the accounting system. This verification will ensure awards are properly recorded as contractor, prime recipient, or sub recipient from private, local, state, or federal agencies.

Implementation Date: December 1, 2016

Responsible Person: Director of Grants and Contracts

The University of North Texas

On its SEFA, the University of North Texas (UNT):

- Incorrectly excluded \$1,216,691 for 1 Student Financial Assistance CFDA. As a result, UNT understated new loans processed for the Federal Direct Student Loans Program by \$1,216,691 in the notes to its SEFA.
- Incorrectly excluded expenditures for one Student Financial Assistance CFDA from the notes to its SEFA. Specifically, UNT incorrectly excluded the beginning and ending balances of outstanding Federal Perkins Loans in the notes to its SEFA. As a result, UNT (1) understated the beginning balance of outstanding Federal Perkins Loans by \$1,581,806 in the notes

to its SEFA and (2) understated the ending balance of outstanding Federal Perkins Loans by \$1,535,394 in the notes to its SEFA.

Recommendations

UNT should strengthen its SEFA preparation and review process to help ensure that it prepares its SEFA correctly and that the SEFA it submits to the Comptroller's Office is complete and accurate by:

- Including all federal expenditures for Student Financial Assistance CFDA's.
- Including the beginning and ending balances for its Federal Perkins Loans.

Views of Responsible Officials

The University of North Texas (UNT) acknowledges and agrees with the findings. During the audit, we determined there was an error in the report used and resulted in an exclusion of \$1,216,691 on the original certified SEFA. While both the general ledger and financial aid information is reconciled, the issue was in how UNT pulled the data for the reported balance. UNT corrected this error which resulted in the discovery of the variance from the amount certified and the amount that should have been on the report.

The exclusion of beginning and ending balances of outstanding Federal Perkins Loans in the notes resulted from a process change and should have been reported in the SEFA. UNT updated processes to ensure future reporting contains this balance appropriately.

Corrective Action Plan

The University has already implemented significant process enhancements in this area. The monitoring manual will be revised to include procedures for the attributes to be tested for each relevant compliance requirement and required documentation to retain to support the review.

Implementation Date: January 9, 2017

Responsible Person: Interim UNT Controller

Higher Education Coordinating Board

On its SEFA, the Higher Education Coordinating Board (Coordinating Board):

- Incorrectly classified \$5,192,733 in pass-through expenditures as direct expenditures for 1 CFDA.

- Incorrectly classified \$496,957 in expenditures related to 2 CFDA's as part of the Research and Development cluster of federal programs.

Recommendations

The Coordinating Board should strengthen its SEFA preparation and review process to help ensure that it prepares its SEFA correctly and that the SEFA it submits to the Comptroller's Office is complete and accurate by:

- Correctly classifying pass-through expenditures and direct expenditures.
- Correctly classifying expenditures in the appropriate clusters.

Views of Responsible Officials

Accepted. The Agency has already implemented significant process enhancements in this area. Through analysis of the exceptions identified in the audit, the Agency will work to develop and implement corrective actions to further improve the processes. See the corrective action plan for further details.

Corrective Action Plan

Texas Higher Education Coordinating Board agrees with the findings and will update work processes and strengthen reviews to ensure the SEFA is reported accurately. We will update internal processes to validate all research and development cluster designations are appropriately classified based on supporting documentation received from institutions during the Comptroller's required AFR pass-through coordination process. Additionally, SEFA work papers will be redesigned to facilitate the review and tie-out of balances reported on the face of the SEFA. This will include a comprehensive supervisor review of all balances presented on the SEFA as well as their appropriate groupings and classifications. Moreover, the preparer and supervisor will verify the SEFA figures and presentation from the hard copy AFR matches the Comptroller's web portal.

Implementation Date: January 1, 2017

Responsible Person: Director – Financial Reporting

Office of the Governor

The Office of the Governor (Governor's Office) incorrectly included on its SEFA \$137,400 in pass-through expenditures to a non-state entity for 1 CFDA. As a result, it overstated federal revenue by \$137,400 in note 2 to its SEFA.

Recommendation

The Governor's Office should strengthen its SEFA preparation and review process to help ensure that it prepares its SEFA correctly and that the SEFA it submits to the Comptroller's Office is complete and accurate by including only federal expenditures for CFDA's.

Views of Responsible Officials and

The Office of the Governor (Office) agrees with the finding.

Corrective Action Plan

The Office has updated its procedures for the preparation of the SEFA to address this condition.

The Office has also incorporated additional review of the SEFA into its internal procedures.

Implementation Date: February 2017

Responsible Person: Director of Financial Services

Federal Award Findings and Questioned Costs

A finding regarding the Schedule of Expenditures of Federal Awards for fiscal year 2016 was included in Chapter 2-D of this report. All other fiscal year 2016 federal award information was issued in a separate report. See *State of Texas Federal Portion of the Statewide Single Audit Report for the Year Ended August 31, 2016*, by KPMG LLP.

Summary Schedule of Prior Audit Findings

*State of Texas Financial Portion of the
Statewide Single Audit Report for the
Year Ended August 31, 2016*

Summary Schedule of Prior Audit Findings

Federal regulations (Title 2, U.S. Code of Federal Regulations, Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards*) state that “the auditee is responsible for follow-up and corrective action on all audit findings.” As part of this responsibility, the auditees report the corrective actions they have taken for the findings reported in:

State of Texas Financial Portion of the Statewide Single Audit Report for the Year Ended August 31, 2008 (State Auditor’s Office Report No. 09-555, April 2009).

State of Texas Financial Portion of the Statewide Single Audit Report for the Year Ended August 31, 2009 (State Auditor’s Office Report No. 10-555, March 2010).

State of Texas Financial Portion of the Statewide Single Audit Report for the Year Ended August 31, 2010 (State Auditor’s Office Report No. 11-555, February 2011).

State of Texas Financial Portion of the Statewide Single Audit Report for the Year Ended August 31, 2011 (State Auditor’s Office Report No. 12-555, February 2012).

State of Texas Financial Portion of the Statewide Single Audit Report for the Year Ended August 31, 2012 (State Auditor’s Office Report No. 13-555, February 2013).

State of Texas Financial Portion of the Statewide Single Audit Report for the Year Ended August 31, 2013 (State Auditor’s Office Report No. 14-555, February 2014).

State of Texas Financial Portion of the Statewide Single Audit Report for the Year Ended August 31, 2014 (State Auditor’s Office Report No. 15-555, February 2015).

State of Texas Financial Portion of the Statewide Single Audit Report for the Year Ended August 31, 2015 (State Auditor’s Office Report No. 16-555, February 2016).

The Summary Schedule of Prior Audit Findings (for the year ended August 31, 2016) has been prepared to address these responsibilities.

The Office of the Comptroller of Public Accounts Should Improve Certain Controls Over Financial Reporting

Issue 1

The Office of the Comptroller of Public Accounts Should Strengthen Its **Preparation and Review of the State's Comprehensive Annual Financial Report**

Reference No. 16-555-01
(Prior Audit Issue 15-555-01)

Type of finding: Significant Deficiency

The Office of the Comptroller of Public Accounts (Comptroller's Office) improved its processes for preparing and reviewing the State's fiscal year 2015 Comprehensive Annual Financial Report (CAFR) and the Schedule of Expenditures of Federal Awards (SEFA).

However, the Comptroller's Office should strengthen those processes to ensure that it obtains significant and necessary information. The Comptroller's Office did not ensure that it obtained the audited annual financial report for a major governmental fund, which it needed to prepare the State's fiscal year 2015 CAFR. As a result, the nonspendable and restricted fund balances in the State's fiscal year 2015 CAFR were misclassified by \$13.5 billion for the Permanent School Fund. That misclassification was also included in the State's governmental activities in the government-wide statement of net position and in the note disclosures to the financial statements. The Comptroller's Office's review process did not detect that error in the fiscal year 2015 CAFR that the Comptroller's Office initially prepared. The CAFR is among the State's most important financial documents and is critical in enabling the State to demonstrate its financial position.

The Comptroller's Office corrected all significant errors that auditors brought to its attention before it finalized the fiscal year 2015 CAFR. Adequate preparation and review of the CAFR is critical to helping ensure that the State's financial statements and note disclosures are complete, accurate, and comply with financial reporting standards.

Recommendation

The Comptroller's Office should improve its preparation and review of the information that it uses to compile the State's financial data and prepare the CAFR to help ensure that information is complete, accurate, and complies with financial reporting standards.

Views of Responsible Officials and Corrective Action Plan

Corrective action was taken.

Issue 2

The Office of the Comptroller of Public Accounts Should Strengthen Its Processes for Reviewing Adjusting Journal Entries and Its Annual Financial Report

Reference No. 16-555-02

Type of finding: Material Weakness

The Office of the Comptroller of Public Accounts – Fiscal Program Department (Comptroller’s Office) had a process to review adjusting journal entries. However, that process did not detect an error that resulted in materially misstated fiscal year 2015 financial statements. As a result, auditors concluded that there was a material weakness in internal control at the Comptroller’s Office (see text box for additional information on material weaknesses).

Material Weakness in Internal Control

A material weakness is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of **an entity’s financial statements** will not be prevented, or detected and corrected, on a timely basis.

Source: American Institute of Certified Public Accountants AU-C Section 265, *Communicating Internal Control Related Matters Identified in an Audit*.

The Comptroller’s Office’s financial statements understated oil and natural gas production tax revenue by \$1.1 billion on the fund financial statements. That occurred because the Comptroller’s Office made an adjusting journal entry that incorrectly recognized \$1.1 billion of oil and natural gas production tax revenue in the State Highway Fund, rather than in the State’s General Revenue Fund.

The Comptroller’s Office’s review process for adjusting journal entries did not detect the incorrect adjusting journal entry or prevent it from being recorded in the financial accounting system. In addition, the Comptroller’s Office did not identify the \$1.1 billion understatement in oil and natural gas tax revenue before the Comptroller’s Office finalized its annual financial report.

To ensure that the issue discussed above did not affect the accuracy of the State’s Comprehensive Annual Financial Report, the Comptroller’s Office made appropriate adjustments to oil and natural gas production tax revenue during its preparation of the State’s Comprehensive Annual Financial Report.

Recommendation

The Comptroller’s Office should strengthen its process for reviewing adjusting journal entries and its annual financial report to ensure that it prepares and presents materially accurate financial statements.

Views of Responsible Officials and Corrective Action Plan

See current year finding 17-555-01.

Chapter 4-B

The Health and Human Services Commission and the Department of Aging and Disability Services Should Improve Controls over Information Technology

Issue 1

The Health and Human Services Commission and the Department of Aging and Disability Services Should Improve Their Management and Monitoring of Certain Information Technology

Reference No. 16-555-03
(Prior Audit Issues 14-555-03 and 15-555-02)

Type of finding: Significant Deficiency

Auditors identified significant weaknesses in controls over the information technology that the Health and Human Services Commission (Commission) and the Department of Aging and Disability Services (Department) use to process claims from the Home and Community Based Services Program and the Texas Home Living Waiver Program (Programs). The Commission and the Department did not fully implement recommendations to improve information technology controls that the State Auditor's Office made in its audit reports for fiscal years 2013 and 2014. Specifically, the Commission and the Department did not consistently monitor user access, did not consistently deactivate user accounts when individuals' employment ended, and did not consistently modify or remove inappropriate access. To protect the integrity of their information, the Commission and the Department should improve their management and monitoring of the information technology that the Programs use.

The Department is the owner of the Programs' data, and the Commission is responsible for administering components of the information technology that the Programs use, including user access.

User Access

Weaknesses in user access to the information technology the Programs use continued to exist in fiscal year 2015. Periodic review of user access is important in identifying potential unauthorized access. Not having a strong user access review process increases the risk of unauthorized or undetected access to, modification of, disclosure of, or destruction of data.

Auditors identified 9,698 active user accounts associated with the Intellectual Disabilities Client Assessment Registration (ID CARE) system. However, 5,066 (52 percent) of those user accounts were inactive. Specifically:

- No individuals had ever logged into ID CARE through 2,332 of those user accounts.
- No individuals had logged into ID CARE in fiscal year 2015 through 2,734 of those user accounts.

Auditors also identified 1,622 disabled user accounts that the Commission had not deleted in accordance with its policies and procedures.

In addition, auditors reviewed 1,003 of the 9,698 active user accounts discussed above that were associated with central agency operations and identified the following issues:

- A total of 189 (19 percent) user accounts were associated with individuals whose employment had been terminated.
- A total of 9 (1 percent) user accounts were associated with individuals for whom the Commission and the Department were unable to verify their employment status.
- A total of 25 individuals had two separate, active user accounts. The Commission asserted that 37 of those 50 user accounts were not necessary.

Title 1, Texas Administrative Code, Chapter 202, requires agencies to develop information technology policies and procedures. Commission information technology security standards and guidelines require user accounts to be restricted to appropriate individuals, require application owners to review user accounts at least every 12 months, require that user accounts be modified or terminated when employment changes are made, and require inactive user accounts to be disabled and deleted.

Passwords

The password configurations for one database the Programs use to process payments did not meet the minimum requirements in the Commission's policies and procedures for passwords. When entities do not require users to change passwords periodically, or allow users to reuse passwords frequently, that increases the risk of unauthorized access to systems and data.

Recommendations

The Commission and the Department should:

- Develop and implement a process for reviewing user access to information technology that the Programs use.
- Disable employees' and contractors' access immediately upon termination of employment or services in compliance with Commission policies and procedures.
- Consistently delete disabled user accounts in compliance with Commission policies and procedures.
- Ensure that password configurations for the databases the Programs use comply with Commission policies and procedures.

Views of Responsible Officials and Corrective Action Plan

See current year finding 17-555-03.

State Entities Should Strengthen the Preparation and Review of Their Schedules of Expenditures of Federal Awards

Reference No. 16-555-04

(Prior Audit Issues 15-555-05, 14-555-07, 13-555-02, 12-555-05, 11-555-17, 10-555-26, and 09-555-19)

Type of finding: Significant Deficiency

Schedule of Expenditures of Federal Awards (SEFA)

Each state entity that expends federal awards is required to prepare a Schedule of Expenditures of Federal Awards (SEFA) and submit it to the Office of the Comptroller of Public Accounts

(Comptroller's Office). The expenditures are to be presented in the SEFA on the same accounting basis as each state entity's fund financial statements.

Federal awards include federal financial assistance and federal cost-reimbursement contracts that non-federal entities receive directly from federal awarding agencies or indirectly from pass-through entities [Office of Management and Budget (OMB) Circular A-133, Section .105, and Title 2, Code of Federal Regulations (CFR), Section 200.38].

Federal financial assistance includes any assistance that non-federal entities receive or administer in the form of grants, loans, loan guarantees, non-cash contributions or donations of property (including donated surplus property), cooperative agreements, interest subsidies, insurance, food commodities, direct appropriations, and other assistance [OMB Circular A-133, Section .105, and Title 2, CFR, Section 200.40].

Source: *Reporting Requirements for Annual Financial Reports of State Agencies and Universities*, Office of the Comptroller of Public Accounts.

The agency and higher education institutions discussed below did not appropriately prepare or adequately review their fiscal year 2015 Schedules of Expenditures of Federal Awards (SEFAs) (see text box for additional information). Therefore, the SEFAs that those state entities submitted to the Office of the Comptroller of Public Accounts (Comptroller's Office) contained errors.

The agency and higher education institutions discussed below reported approximately \$3.8 billion in federal expenditures, or 7 percent of the total federal expenditures the State of Texas reported for fiscal year 2015. The errors listed below were not material to the fiscal year 2015 SEFA for the State of Texas or to the fiscal year 2015 Comprehensive Annual Financial Report for the State of Texas. However, collectively, they represent control weaknesses that could be significant to the State's SEFA.

Prairie View A&M University

Prairie View A&M University (Prairie View A&M) incorrectly included expenditures for two Student Financial Assistance Catalog of Federal Domestic Assistance (CFDA) programs on its SEFA. Specifically, it incorrectly included \$947,520 for 2 CFDA's. As a result, Prairie View A&M (1) overstated expenditures on its SEFA by \$947,520 for 2 CFDA's; (2) overstated federal revenue by \$47,520 in the notes to its SEFA; and (3) overstated new loans processed for the Federal Direct Student Loans Program by \$900,000 in the notes to its SEFA.

Views of Responsible Officials and Corrective Action Plan

Corrective action was taken.

Sam Houston State University

Sam Houston State University (SHSU) incorrectly excluded expenditures for three Student Financial Assistance CFDA's from its SEFA. Specifically, it incorrectly excluded \$2,380,458 for 3 CFDA's. As a result, SHSU (1) understated expenditures on its SEFA by \$2,380,458 for 3 CFDA's; (2) understated federal revenue by \$60,651 in the notes to its SEFA; and (3) understated new loans processed for the Federal Direct Student Loans Program by \$2,319,807 in the notes to its SEFA.

Recommendation

SHSU should strengthen its SEFA preparation and review process to help ensure that it prepares its SEFA correctly and that the SEFA it submits to the Comptroller's Office is complete and accurate.

Implementation Status

Partially implemented.

Views of Responsible Officials and Corrective Action Plan 2015

SHSU agrees with the stated findings and has established report controls to correct this deficiency and ensure the SEFA is complete and accurate when submitted to the Comptroller's Office. This includes the recognition of revenue and expenses related to administrative allowances.

Responsible Person: Interim Controller

Implementation date: January 2016

Views of Responsible Officials and Corrective Action Plan 2016

SHSU agrees with the stated findings and has established report controls to correct this deficiency and ensure the SEFA is complete and accurate when submitted to the Comptroller's Office. This includes the recognition of revenue and expenses related to administrative allowances.

Responsible Person: Interim Controller

Implementation date: Fall 2016

Stephen F. Austin State University

Stephen F. Austin State University (SFASU) incorrectly excluded expenditures for one Student Financial Assistance CFDA from its SEFA. Specifically, it incorrectly excluded \$63,031 for 1 CFDA. As a result, SFASU (1) understated expenditures on its SEFA by \$63,031 for 1 CFDA and (2) did not report \$63,031 in administrative costs in its notes to its SEFA.

Views of Responsible Officials and Corrective Action Plan

Corrective action was taken.

Texas A&M University

Texas A&M University (TAMU) excluded \$167,036 from the notes to its SEFA for the ending balance for loans from prior years for the Health Professions Student Loans Program.

Views of Responsible Officials and Corrective Action Plan

Corrective action was taken.

Texas Department of Agriculture

On its SEFA, the Texas Department of Agriculture (TDA):

- **Incorrectly excluded \$257,976 in expenditures for 2 CFDA's. As a result, TDA understated federal revenue by \$257,976 in the notes to its SEFA.**
- **Incorrectly classified \$405,912 in expenditures between 2 CFDA's.**

Views of Responsible Officials and Corrective Action Plan

Corrective action was taken.

Texas Tech University

On its SEFA, Texas Tech University (Texas Tech):

- Did not identify \$24,497 in expenditures for 1 CFDA as American Recovery and Reinvestment Act (ARRA) expenditures.
- Incorrectly classified \$136,058 in expenditures related to 2 generic CFDA's.

Views of Responsible Officials and Corrective Action Plan

Corrective action was taken.

The University of Texas at Arlington

On its SEFA, the University of Texas at Arlington (UT-Arlington):

- Incorrectly classified \$1,329,737 in direct expenditures for 8 CFDA's as reconciling items (specifically, federal revenue received under a vendor relationship between the agency and the federal government) in Note 2 to its SEFA. As a result, UT-Arlington, understated expenditures by \$1,329,737 for 8 CFDA's.
- Did not identify \$13,441 in expenditures for 1 CFDA as ARRA expenditures.
- Incorrectly reported expenditures in the notes to its SEFA for the ending balance for loans from prior years for three Student Financial Assistance CFDA's. Specifically, it incorrectly reported \$396,282 for the Federal Perkins Loan Program; \$111,720 for the Nurse Faculty Loan Program; and \$28,620 for the ARRA-Nurse Faculty Loan Program.

Views of Responsible Officials and Corrective Action Plan

See current year finding 17-555-04.

The University of Texas at Austin

On its SEFA, the University of Texas at Austin (UT-Austin):

- Incorrectly classified \$135,310 in expenditures related to 1 CFDA as part of the Research and Development cluster of federal programs.

- Incorrectly reported expenditures in the notes to its SEFA for the ending balance for loans from prior years for two Student Financial Assistance CFDA's. Specifically, it (1) incorrectly included \$46,568 for the Nurse Faculty Loan Program and (2) incorrectly excluded \$1,856,885 for the Federal Perkins Loan Program.
- Incorrectly classified \$116,751 in expenditures related to 3 generic CFDA's.

Views of Responsible Officials and Corrective Action Plan

See current year finding 17-555-04.

The University of Texas at Dallas

On its SEFA, the University of Texas at Dallas (UT-Dallas):

- Incorrectly excluded \$37,918 for 1 Student Financial Assistance CFDA. As a result, UT-Dallas understated federal revenue by \$37,918 in the notes to its SEFA.
- Incorrectly classified \$96,189 in pass-through expenditures as direct expenditures for 1 CFDA.
- Incorrectly classified \$375,409 in expenditures related to 3 generic CFDA's.

Views of Responsible Officials and Corrective Action Plan

Corrective action was taken.

The University of Texas at El Paso

On its SEFA, the University of Texas at El Paso (UTEP):

- Incorrectly included \$137,669 in expenditures for 2 Student Financial Assistance CFDA's and incorrectly excluded \$87,453 in expenditures for 1 Student Financial Assistance CFDA. As a result, UTEP overstated federal revenue by \$50,216 in the notes to its SEFA.
- Incorrectly classified \$3,151,584 in expenditures related to 10 CFDA's as part of the Research and Development cluster of federal programs.

- Incorrectly classified \$7,300 in expenditures among 2 Student Financial Assistance CFDA's. As a result, (1) UTEP did not report \$7,300 in new loans processed for the Nurse Faculty Loan Program in the notes to its SEFA; (2) overstated the new loans processed for the ARRA-Nurse Faculty Loan Program by \$7,300 in the notes to its SEFA; and (3) did not identify \$7,300 in expenditures for 1 CFDA as ARRA expenditures.
- Incorrectly reported expenditures in the notes to its SEFA for the ending balance for loans from prior years for four Student Financial Assistance CFDA's. Specifically, it (1) incorrectly included \$3,941,520 for the Federal Perkins Loan Program, \$6,340,163 for the Federal Direct Student Loans Program, and \$69,519 for the ARRA-Nurse Faculty Loan Program and (2) incorrectly excluded \$277,047 for the Nurse Faculty Loan Program.

Views of Responsible Officials and Corrective Action Plan

See current year finding 17-555-04.

The University of Texas Health Science Center at Houston

On its SEFA, the University of Texas Health Science Center at Houston (UTHSC-Houston):

- Did not correctly identify ARRA expenditures. Specifically, it did not identify \$53,135 in expenditures for 2 CFDA's as ARRA, and it incorrectly identified \$651 in expenditures for 1 CFDA as ARRA.
- Incorrectly reported expenditures in the notes to its SEFA for the ending balance for loans from prior years for two Student Financial Assistance CFDA's. Specifically, UTHSC-Houston incorrectly included \$297,040 for the Federal Perkins Loan Program and \$26,643 for the Health Professions Student Loans Program.

Views of Responsible Officials and Corrective Action Plan

Corrective action was taken.

The University of Texas Health Science Center at San Antonio

On its SEFA, the University of Texas Health Science Center at San Antonio (UTHSC-San Antonio):

- Incorrectly included \$117,138 in expenditures for 1 CFDA. As a result, UTHSC-San Antonio overstated federal revenue by \$117,138 in the notes to its SEFA.
- Incorrectly reported expenditures in the notes to its SEFA for the ending balance for loans from prior years for two Student Financial Assistance CFDA's. Specifically, UTHSC-San Antonio incorrectly excluded \$11,700 for the Nurse Faculty Loan Program and \$143,044 for the Health Professions Student Loans Program.

Recommendation

UTHSC-San Antonio should strengthen its SEFA preparation and review process to help ensure that it prepares its SEFA correctly and that the SEFA it submits to the Comptroller's Office is complete and accurate.

Implementation Status

Partially implemented.

Views of Responsible Officials and Corrective Action Plan 2015

Management concurs and will continue to fine tune processes in place to ensure the accuracy and completeness of the SEFA report. Specifically, (1) exclude any expenditures in programs where the sponsoring state agency designates us as a vendor (as opposed to a pass-thru entity) and (2) include in the notes the ending loan balances for all federal student assistance programs on our general ledger, and not only for those with new expenditures in the report year.

Responsible Party: AVP for Business Affairs

Implementation Date: March 1, 2016

Views of Responsible Officials and Corrective Action Plan 2016

Management concurs with the SAO on the 2016 finding of 'partially implemented.' We have identified and will execute additional procedures going forward to ensure that our year-end ledger balances of federal SFA

loans accurately reflect student accounts. We will also ensure that when we perform services for a state agency spending federal funds, and we agree with the sponsor to be classified as a vendor, the related expenditures and revenue are excluded from both the SEFA and the SEFA notes.

Responsible Party: Senior Director of Accounting

Implementation Date: March 1, 2017

The University of Texas M.D. Anderson Cancer Center

On its SEFA, the University of Texas M.D. Anderson Cancer Center (Cancer Center):

- Incorrectly classified \$4,115 in direct expenditures for 1 CFDA as pass – through expenditures.
- Incorrectly classified \$1,248,747 in pass-through expenditures as direct expenditures for 6 CFDA.

Views of Responsible Officials and Corrective Action Plan

Corrective action was taken.

The University of Texas - Pan American

On its SEFA, the University of Texas - Pan American (UT-Pan American):

- Incorrectly classified \$26,837 in expenditures among 2 CFDA.
- Incorrectly classified \$16,000 in pass-through expenditures as direct expenditures for 1 CFDA.
- Incorrectly included \$65,306 in pass-through expenditures from the Texas A&M Research Foundation on its SEFA. It should have reported that amount as a reconciling item for federal grants from the Texas A&M Research Foundation in the notes to its SEFA.
- Incorrectly reported expenditures in the notes for the ending balance for loans from prior years for one Student Financial Assistance CFDA. Specifically, UT-Pan American incorrectly included \$607,467 for the Federal Perkins Loan Program.

UT-Pan American became a part of the University of Texas Rio Grande Valley at the beginning of fiscal year 2016.

Views of Responsible Officials and Corrective Action Plan

See current year finding 17-555-04 for the University of Texas Rio Grande Valley.

The University of Texas at San Antonio

The University of Texas at San Antonio (UTSA) incorrectly classified \$119,707 in expenditures on its SEFA related to 1 generic CFDA.

Views of Responsible Officials and Corrective Action Plan

Corrective action was taken.

Appendices

Appendix 1

Objective, Scope, and Methodology

Objective

The audit objective was to determine whether the State's basic financial statements present fairly, in all material respects, the consolidated balances and activities for the State of Texas for the fiscal year ended August 31, 2016.

The Statewide Single Audit is an annual audit for the State of Texas. It is conducted so that the State complies with (1) the Single Audit Act Amendments of 1996 and Title 2, U.S. Code of Federal Regulations, Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) and (2) state statute requiring that an audited Comprehensive Annual Financial Report be provided to the Governor (Texas Government Code, Section 403.013(c)).

Scope

The scope of the financial portion of the Statewide Single Audit included an audit of the State's basic financial statements and a review of significant controls over financial reporting and compliance with applicable requirements. The opinion on the basic financial statements, published in the Comprehensive Annual Financial Report for the fiscal year ended August 31, 2016, was dated February 21, 2017.

The scope of the federal compliance portion of the Statewide Single Audit included an audit of the State's Schedule of Expenditures of Federal Awards (SEFA), a review of compliance for each major program, and a review of significant controls over federal compliance. The State Auditor's Office contracted with KPMG LLP (KPMG) to provide an opinion on compliance for each major program and internal control over compliance. The State Auditor's Office provided an opinion on the State's SEFA, in relation to its opinion on the CAFR. Information on the federal compliance portion of the Statewide Single Audit is included in a separate report entitled *State of Texas Federal Portion of the Statewide Single Audit Report for the Fiscal Year Ended August 31, 2016*, by KPMG.

Methodology

The audit methodology included collecting information, identifying risk, conducting data analyses, performing selected audit tests and other

procedures, and analyzing and evaluating the results against established criteria.

To avoid duplication of effort, the State Auditor's Office relied on KPMG's testing of the internal controls over certain systems and processes as they related to the financial portion of the Statewide Single Audit.

Auditors assessed the reliability of the State's data by (1) performing electronic tests of required data elements, (2) reviewing existing information about data and the systems that produced the data, and (3) interviewing agency and higher education institution officials knowledgeable about data. Auditors determined that the data was sufficiently reliable for the purposes of this audit.

Sampling Methodology

As part of the audit procedures performed at Texas A&M University, auditors used professional judgment to select a risk-based sample of depreciable capital assets for testing. The sample items were generally not representative of the population; however, they were selected so that auditors could obtain sufficient appropriate evidence regarding whether:

- The fiscal year 2016 depreciable capital assets beginning balances contained misstatements that materially affected the current period's financial statements.
- Appropriate accounting policies reflected in the fiscal year 2016 beginning balances had been consistently applied in the current period's financial statements or changes thereto were appropriately accounted for and adequately presented and disclosed in accordance with the applicable financial reporting framework.

Auditors determined that the fiscal year 2016 beginning balances for depreciable capital assets described above were fairly presented.

As part of the audit procedures performed on the Schedule of Expenditures of Federal Awards, auditors used professional judgment to select a sample of generic Catalog of Federal Domestic Assistance numbers (CFDAs) to test that the correct unique identifying number was reported. Auditors also used professional judgment to select a sample of state entities to verify that the beginning balances for loans with continuing compliance requirements reported on Note 5 were accurate.

Information collected and reviewed included the following:

- Agency and higher education institution policies and procedures.

- Agency and higher education institution systems documentation.
- Agency and higher education institution accounting data.
- Agency and higher education institution year-end accounting adjustments.
- Agency and higher education institution fiscal year 2016 annual financial reports.
- Agency and higher education institution fiscal year 2016 SEFA submissions to the Office of the Comptroller of Public Accounts.

Information systems reviewed included the following:

- Agency and higher education institution internal accounting systems.
- Uniform Statewide Accounting System.

Procedures and tests conducted included the following:

- Evaluating automated systems controls.
- Performing analytical tests of account balances.
- Comparing agency and higher education institution accounting practices with Office of Comptroller of Public Accounts' reporting requirements.

Criteria used included the following:

- Texas Statutes.
- Texas Administrative Code.
- General Appropriations Act (84th Legislature).
- The Office of the Comptroller of Public Accounts' policies and procedures.
- The Office of the Comptroller of Public Accounts' Reporting Requirements for Fiscal Year 2016 Annual Financial Reports of State Agencies and Universities.
- Agency and higher education institution policies and procedures.
- Title 2, Code of Federal Regulations, Section 200.501, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards*.

- Generally accepted accounting principles as established by existing authoritative literature including, but not limited to, literature published by the Governmental Accounting Standards Board and the Financial Accounting Standards Board.

Project Information

Audit fieldwork was conducted from August 2016 through February 2017. We conducted this audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that the State Auditor's Office and those performing the audit be independent, and that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. The State Auditor's Office implemented safeguards to maintain its independence to perform this audit. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

The following members of the State Auditor's staff performed the audit of the Comprehensive Annual Financial Report:

- Robert Pagenkopf, MBA, CFE (Project Manager)
- Jeannette Quiñonez Garcia, CPA (Assistant Project Manager)
- Robert H. (Rob) Bollinger, CPA, CFE
- Robert P. Burg, MPA, CPA, CFE
- Charlotte Carpenter
- Katherine M. Curtsinger
- Joseph T. Fredrick, CPA
- Taylor L. Huff
- Teri Lynn Incremona
- Robert G. Kiker, CGAP
- Jack Lee, CPA
- Anca Pinchas, CPA, CISA, CIDA
- Melissa May Prompungorn

- Sarah Jane M. Puerto, CFE
- Fabienne Robin, MBA
- Adam Ryan
- Taylor Sams
- Nakeesa Shahparasti, CPA, CFE
- Philip Stringer, CPA
- Jessica Volkmann, CPA
- Damian Zorrilla, CPA, CIA, CFE, CGAP
- Dennis Ray Bushnell, CPA (Quality Control Reviewer)
- Michelle Ann Duncan Feller, CPA, CIA (Quality Control Reviewer)
- Ann E. Karnes, CPA (Quality Control Reviewer)
- Mary Ann Wise, CPA, CFE (Quality Control Reviewer)
- Angelica M. Ramirez, CPA (Audit Manager)

The following members of the State Auditor's staff performed the audit of the Schedule of Expenditures of Federal Awards:

- Lilia C. Srubar, CPA (Project Manager)
- Bianca F. Pineda, CGAP (Assistant Project Manager)
- Frances Mikus Barker, MSA
- Adam Berry
- Rebecca Franklin, CISA, CGAP, CFE, CICA
- Allison Fries
- Nick Hoganson
- Thomas Andrew Mahoney, CGAP
- Bryan McGloin, MBA, MS
- Sonya Tao, CFE
- John Zhang, MPA

- Mary Ann Wise, CPA, CFE (Quality Control Reviewer)
- Audrey O’Neill, CIA, CFE, CGAP (Audit Manager)

Agencies and Higher Education Institutions Audited

Financial accounts were audited at the following agencies and higher education institutions:

- Department of Aging and Disability Services.
- Health and Human Services Commission.
- Office of the Comptroller of Public Accounts.
- Texas A&M University.
- Texas Education Agency.
- Texas Workforce Commission.

Schedules of expenditures of federal awards at the following agencies and higher education institutions were audited by either the State Auditor's Office or KPMG LLP:

- Department of Aging and Disability Services.
- Department of Agriculture.
- Department of Assistive and Rehabilitative Services.
- Department of Family and Protective Services.
- Department of Housing and Community Affairs.
- Department of Public Safety.
- Department of State Health Services.
- Department of Transportation.
- General Land Office.
- Health and Human Services Commission.
- Higher Education Coordinating Board.
- Office of the Governor.
- Prairie View A&M University (auditors performed only prior-year finding follow-up work).

- Sam Houston State University (auditors performed only prior-year finding follow-up work).
- Stephen F. Austin State University (auditors performed only prior-year finding follow-up work).
- Texas A&M University.
- Texas Education Agency.
- Texas State University.
- Texas Tech University.
- Texas Workforce Commission.
- The University of Houston.
- The University of North Texas.
- The University of Texas at Arlington.
- The University of Texas at Austin.
- The University of Texas at Dallas (auditors performed only prior-year finding follow-up work).
- The University of Texas at El Paso.
- The University of Texas at San Antonio.
- The University of Texas Health Science Center at Houston (auditors performed only prior-year finding follow-up work).
- The University of Texas Health Science Center at San Antonio (auditors performed only prior-year finding follow-up work).
- The University of Texas M.D. Anderson Cancer Center (auditors performed only prior-year finding follow-up work).
- The University of Texas Medical Branch at Galveston.
- The University of Texas Rio Grande Valley.

Copies of this report have been distributed to the following:

Legislative Audit Committee

The Honorable Dan Patrick, Lieutenant Governor, Joint Chair
The Honorable Joe Straus III, Speaker of the House, Joint Chair
The Honorable Jane Nelson, Senate Finance Committee
The Honorable Robert Nichols, Member, Texas Senate
The Honorable John Zerwas, House Appropriations Committee
The Honorable Dennis Bonnen, House Ways and Means Committee

Office of the Governor

The Honorable Greg Abbott, Governor

Boards, Commissions, Chancellors, Executive Directors, and Presidents of the Following Agencies and Higher Education Institutions

Department of Aging and Disability Services
Department of Agriculture
Department of Family and Protective Services
Department of Housing and Community Affairs
Department of Public Safety
Department of State Health Services
Department of Transportation
General Land Office
Health and Human Services Commission
Higher Education Coordinating Board
Office of the Comptroller of Public Accounts
Prairie View A&M University
Sam Houston State University
Stephen F. Austin State University
Texas A&M University
Texas Education Agency
Texas State University
Texas Tech University
Texas Workforce Commission
Trusted Programs within the Office of the Governor
University of Houston
University of North Texas
The University of Texas at Arlington
The University of Texas at Austin
The University of Texas at Dallas
The University of Texas at El Paso
The University of Texas at San Antonio
The University of Texas Health Science Center at Houston
The University of Texas Health Science Center at San Antonio
The University of Texas M.D. Anderson Cancer Center
The University of Texas Rio Grande Valley



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