State of Texas Financial Portion of the

Statewide Single Audit Report for the Year Ended August 31, 2018

February 2019

Report No. 19-555

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Overall Conclusion

In our audit opinion dated February 21, 2019, 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, 2018. 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 2018, which it intends to post on its Web site at https://comptroller.texas.gov/transparency/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.

> **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*.

Economic Stabilization Fund

On August 31, 2018, the Economic Stabilization Fund balance was $12.5 billion. That amount consisted primarily of $8.7 billion in cash in the State Treasury, $2.3 billion in current and non-current investments, and $1.4 billion due from the General Revenue Fund. The $1.4 billion due from the General Revenue Fund was transferred to the Economic Stabilization Fund in November 2018. 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.

This audit was conducted in accordance with Texas Government Code, Section 403.013(c), and TItle 31, United States Code, Section 7502.

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

Fiscal Year 2018 Financial Summary

- As of August 31, 2018, the State reported total assets of $334.1 billion, which primarily consisted of $144.4 billion in capital assets, $115.2 billion in investments, and $36.5 billion in cash and cash equivalents.
- As of August 31, 2018, the State reported total liabilities of $208.2 billion, which consisted of $75.9 billion for other postemployment benefits (OPEB) liabilities, $45.0 billion for pension liabilities, and $54.3 billion for bonds payable liabilities.
- As of August 31, 2018, the State reported a net position of $99.5 billion. Net position is the total ending balance for the State.
- The fiscal year 2018 consolidated financial statements convey the use of approximately $140.3 billion[1] during the fiscal year.
- The State's Schedule of Expenditures of Federal Awards (SEFA) reported expenditures of $56.0 billion related to federal awards.

The State is also the trustee or fiduciary for six defined benefit plans and one defined contribution plan. It is also responsible for other assets that can only be used for trust beneficiaries. All state fiduciary activities are reported in separate statements of fiduciary net position and changes in fiduciary net position. These activities are reported separately from other financial activities because the state cannot use the assets to finance its operations. The state's fiduciary responsibilities include ensuring that assets reported in those funds are used for their intended purposes. The financial activity and balances for those fiduciary activities are not included in the fiscal year 2018 totals listed above.

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.

The State Auditor's Office also audited the State's SEFA in relation to the CAFR for fiscal year 2018. The Comptroller's Office prepares the SEFA by using self-reported SEFA data from all state agencies and higher education institutions that made

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[1] The $140.3 billion in annual expenditures exceeded the $108.7 billion appropriated for fiscal year 2018 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 and OPEB-related expenditures were recorded in the CAFR to account for the effects of the implementation of GASB Statements Nos. 68, 71, 73, and 75 that are not included in the GAA.

federal expenditures during the fiscal year. The State Auditor's Office and KPMG LLP (KPMG) audited the processes for preparing SEFA information at nine agencies and five higher education institutions. Auditors identified errors related to the SEFA information at one agency and five higher education institutions. Those errors are discussed in Chapter 2-A of this report.

As part of the audit work for SEFA, auditors performed prior-year finding follow-up work at six higher education institutions and determined that recommendations for two of those findings were not yet fully implemented (see the Summary Schedule of Prior Year Audit Findings).

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 certain chapters 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, 2018.

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 Year Ended August 31, 2018*, by KPMG.

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Appendices

Independent Auditor's Report

State of Texas Financial Portion of the Statewide Single Audit Report for the Year Ended August 31, 2018

Summary of Auditor's Results

Financial Statements

1. Type of auditor's report issued:	Unmodified
2. Internal control over financial reporting:	
a. Material weakness identified?	No
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 2018 was included in Chapter 2-A of this report. All other fiscal year 2018 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, 2018*, 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*

Independent Auditor's Report

The Honorable Greg Abbott, Governor
The Honorable Glenn Hegar, Comptroller of Public Accounts
The Honorable Dan Patrick, Lieutenant Governor
The Honorable Dennis Bonnen, 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, 2018, 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, 2019. 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.

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 consolidated financial statements will not be prevented, or detected and corrected on a timely basis. 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.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section 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. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. We did identify certain deficiencies in internal control, described in the accompanying schedule of findings and responses that we consider to be significant deficiencies.

Summary of Finding	
Agency or Higher Education Institution	Finding Number
Multiple agencies and higher education institutions	19-555-01

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 consolidated 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 2018 Financial Statements* (State Auditor's Office Report No. 19-015, December 2018).
- *A Report on the Audit of the Department of Housing and Community Affairs' Fiscal Year 2018 Financial Statements* (State Auditor's Office Report No. 19-017, December 2018).
- *A Report on the Audit of the Employees Retirement System's Fiscal Year 2018 Financial Statements* (State Auditor's Office Report No. 19-018, December 2018).
- *A Report on the Audit of the Permanent School Fund's Fiscal Year 2018 Financial Statements* (State Auditor's Office Report No. 19-021, January 2019).

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 consolidated 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, 2019

Schedule of Findings and Responses

State of Texas Financial Portion of the Statewide Single Audit Report for the Year Ended August 31, 2018

Financial Statement Findings

This chapter identifies the significant deficiencies related to the financial statements that are required to be reported in accordance with *Government Auditing Standards*. There are no significant deficiencies related to the State's basic financial statements, but Chapter 2-A below discusses significant deficiencies related to the State's Schedule of Expenditures of Federal Awards.

Chapter 2-A

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

Reference No. 19-555-01

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, U.S. 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 agency and higher education institutions discussed below did not appropriately prepare or adequately review their fiscal year 2018 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 agency and higher education institutions discussed below reported $2,157,552,213 in federal expenditures, or 4 percent of the total federal expenditures that the State of Texas reported for fiscal year 2018. The errors listed below were not material to the fiscal year 2018 SEFA for the State of Texas or to the fiscal year 2018 Comprehensive Annual Financial Report for the State of Texas. However, collectively, they represent control weaknesses that could be significant to the State's SEFA.

Department of State Health Services

The Department of State Health Services (DSHS) overstated expenditures on its fiscal year 2018 SEFA by $22,625,885 for 43 Catalog of Federal Domestic Assistance (CFDA) programs. That occurred because DSHS incorrectly included prior year accruals and excluded current year accruals. As a result, DSHS overstated federal revenues by $22,625,885 in Note 2 to its SEFA.

Recommendation

DSHS should strengthen its SEFA preparation and review process to help ensure that it prepares its SEFA correctly, including recording accruals in the appropriate fiscal year.

Views of Responsible Officials

The Department of State Health Services (DSHS) agrees with the finding. DSHS is aware of the exceptions identified in the audit. DSHS responsible parties notified KPMG when the issue was discovered by DSHS staff. DSHS will work to develop and implement corrective action to ensure the issue is corrected for future Comprehensive Annual Financial Reports (CAFRs).

Corrective Action Plan

DSHS will update processes to ensure all accruals are entered correctly for the Schedule of Expenditures of Federal Awards (SEFA) for FY 2019. Accounts have been added in CAPPS 9.2 to enable the entry of payables for FY 2019 and to enable reversal of FY 2018 accruals for the preparation of the FY 2019 SEFA. The responsible area will update written processes for reporting accruals in Note 2 to the DSHS's SEFA.

Implementation Date:	*March 31, 2019*
Responsible Person:	*Accounting Director*

The University of Texas at Austin

On its fiscal year 2018 SEFA, the University of Texas at Austin (UT Austin):

- Incorrectly classified $2,280,241 in expenditures related to 2 generic CFDA programs.
- Incorrectly classified $12,976 in expenditures related to 3 CFDAs as part of the Research and Development cluster of federal programs. Those expenditures should not have been classified as part of the Research and Development cluster of federal programs.

Recommendation

UT Austin should strengthen its SEFA preparation and review process to help ensure that it prepares its SEFA correctly, including ensuring that it reports correct CFDAs for each federal award and classifies expenditures in the appropriate clusters.

Views of Responsible Officials

The University concurs with the finding.

Corrective Action Plan

In preparation for the SEFA process, responsible parties will review CFDAs to ensure that the correct CFDA has been used. The review process will occur during the summer so that errors regarding generic CFDAs can be addressed. In addition, CFDA Research and Development clusters will be reviewed to ensure the correct classification of sponsored activities. SEFA procedures have been updated reflecting changes to the review process.

Implementation Date: February 2019

Responsible Person: Assistant Director for Sponsored Projects

The University of Texas Health Science Center at Houston

On its fiscal year 2018 SEFA, the University of Texas Health Science Center at Houston (UT Health):

- Overstated federal revenue by $327,845 and incorrectly included a reconciling item related to that revenue in Note 2 to its SEFA. That occurred because UT Health incorrectly included revenue received on non-fixed fee contracts in its calculation of the reconciling item for federal revenue received on fixed fee basis contract in Note 2 to its SEFA.

- Incorrectly classified $1,295,576 in expenditures related to 2 CFDAs as non-Research and Development expenditures. Those expenditures should have been classified as part of the Research and Development cluster of federal programs.

Recommendation

UT Health should strengthen its SEFA preparation and review process to help ensure that it prepares its SEFA correctly, including ensuring that it (1) reports federal revenues and reconciling items correctly and only when appropriate in the notes to its SEFA and (2) classifies expenditures in the appropriate clusters.

Views of Responsible Officials

The University acknowledges and agrees with both of the findings noted.

Corrective Action Plan

Finding 1: Overstatement of revenue in Note 2 of the SEFA calls for a development by leadership of a revised methodology to ensure future compliance in line with reporting and audit expectations. Management will be meeting to revise the revenue reporting methodology for future SEFAs, and will outline that process in a new procedure for the annual report.

Implementation Date: *April 1, 2019*

Responsible Person: *Director, Post Award Finance*

Finding 2: The coding of the two CFDAs referenced was due to two state entities identifying pass-through funds as non-research during the negotiation process, though based on activity outlined in the award we had correctly represented them in our financial system as Research. Process expectation is agreement with the primary recipient, and thus we reflected non-research in the SEFA. We have educated additional individuals on the report and its requirements. We will review our designations on all negotiated agencies and ask for further support if they indicate a contrary classification.

Implementation Date: *Immediately*

Responsible Person: *Director, Post Award Finance*

The University of Texas M.D. Anderson Cancer Center

On its fiscal year 2018 SEFA, the University of Texas M.D. Anderson Cancer Center (M.D. Anderson):

- Incorrectly excluded $26,696,473 in expenditures because it did not include expenditures paid from program income for 6 CFDAs. As a result, M.D. Anderson (1) understated expenditures on its SEFA by $26,696,473 and (2) understated federal revenue by $26,696,473 in Note 2 to its SEFA.
- Incorrectly classified $3,877,918 in expenditures related to 1 CFDA as part of the Research and Development cluster of federal programs. Those expenditures should not have been classified as part of the Research and Development cluster of federal programs.
- Incorrectly classified $83,808 in expenditures for 2 CFDA programs on its SEFA.
- Incorrectly based its SEFA on revenues rather than expenditures for the Disaster Grants – Public Assistance (Presidentially Declared Disasters) program. As a result, M.D. Anderson could not determine whether Note 8, a required disclosure related to that program, applied to expenditures for that program.

Recommendations

M.D. Anderson should:

- Strengthen its SEFA preparation and review process to help ensure that it prepares its SEFA correctly, including ensuring that it:
  - Includes all applicable federal expenditures, including expenditures paid with program income.
  - Classifies expenditures in the appropriate clusters.
  - Reports correct CFDAs for each federal award.
- Correctly report its expenditure information for the Disaster Grants – Public Assistance (Presidentially Declared Disasters) program by:
  - Preparing its SEFA based on expenditures as described by Title 2, U.S. Code of Federal Regulations, Part 200, Appendix XI.
  - Reporting a Note 8, when appropriate.

Views of Responsible Officials

The Cancer Center agrees with SAO's findings. We wish to highlight that, though program income was excluded from initial SEFA preparation, all program income accounts are appropriately coded as federal funding, managed to federal compliance requirements and audited as part of the Single Audit. Given the manual nature of entering and maintaining award data in the financial system, complete accuracy in data capture is an ongoing goal and objective of MDACC.

Corrective Action Plan

- *The Cancer Center will include program income expenditures in future SEFA preparation. The Cancer Center will also revise its quality control process to ensure the SEFA is submitted as accurately as possible.*
- *The Cancer Center is conducting training, developing processes, and developing supporting tools to reduce the likelihood that award set-up and amendment transactions are entered into the financial system incorrectly.*
- *The Cancer Center will conduct training and develop processes with the Facilities, Grants and Contracts Accounting, and Financial Reporting teams to report expenditures for Disaster Grants – Public Assistance and to report a Note 8 when required.*

Implementation Dates:

SEFA Preparation – March 2019

Award Set-Up Training and Processes – March 2019

Disaster Grants – Public Assistance – July 2019

Responsible Person: Vice President and Chief Accounting Officer

The University of Texas Medical Branch at Galveston

On its fiscal year 2018 SEFA, the University of Texas Medical Branch at Galveston (UTMB):

- Overstated federal revenue by $415,789 and incorrectly included a reconciling item related to that revenue in Note 2 to its SEFA. That occurred because UTMB incorrectly included revenue received on non-fixed fee contracts in its calculation of the reconciling item for federal revenue received on the fixed fee basis contract in Note 2 to its SEFA.

- Incorrectly classified $878,548 in expenditures related to 6 CFDAs as part of the Research and Development cluster of federal programs. Those expenditures should not have been classified as part of the Research and Development cluster of federal programs.

Recommendation

UTMB should strengthen its SEFA preparation and review process to help ensure that it prepares its SEFA correctly, including ensuring that it (1) reports federal revenues and reconciling items correctly and only when appropriate in the notes to its SEFA and (2) classifies expenditures in the appropriate clusters.

Views of Responsible Officials

The University of Texas Medical Branch acknowledges and agrees with the findings.

Corrective Action Plan

The University of Texas Medical Branch has already implemented significant process enhancements to ensure it correctly reports federal revenues and reconciling items in the SEFA notes. The Office of Sponsored Programs will reeducate staff regarding classifications for awards. A QA report will be developed and ran on a quarterly basis to monitor improper classifications.

Implementation Date: May 2019

Responsible Person: Director Grants and Contracts Accounting and Associate Vice President Research Administration

The University of Texas Southwestern Medical Center

On its fiscal year 2018 SEFA, the University of Texas Southwestern Medical Center (UT Southwestern):

- Overstated expenditures by $1,247,151 for 1 Student Financial Assistance CFDA program. UT Southwestern did not make any disbursements for this program in fiscal year 2018. Instead, that amount represented the entire balance of the program. As a result, UT Southwestern

(1) overstated the outstanding balance of loans by $1,236,735 in Note 3a to its SEFA, (2) understated the beginning balance of outstanding loans by $10,416 in Note 3a to its SEFA, and (3) overstated new loans processed amount by $1,247,151 in Note 2 and Note 3a to its SEFA.

- Incorrectly classified $360,220 in expenditures using a generic CFDA (43.000) instead of the CFDA identified in the award agreement (43.003).
- Overstated federal revenue by $112,085 in Note 2 to its SEFA and incorrectly included a reconciling item (specifically, federal revenue received under a vendor relationship between the agency and the federal government) related to that revenue in Note 2 to its SEFA. That occurred because UT Southwestern incorrectly reported federal revenue received from vendor relationships with non-federal government entities.
- Incorrectly included $212,064 in expenditures related to 2 CFDAs on its SEFA; it should have included those expenditures as a reconciling item (specifically, federal revenue received under a vendor relationship between the agency and the federal government) in Note 2 of its SEFA. As a result, UT Southwestern overstated expenditures on its SEFA by $212,064.
- Overstated $176,270 in expenditures related to 2 CFDAs. That occurred because UT Southwestern included non-federal expenditures on its SEFA. As a result, UT Southwestern overstated federal revenue by $176,270 in Note 2 to its SEFA.

Recommendation

UT Southwestern should strengthen its SEFA preparation and review process to help ensure that it prepares its SEFA correctly, including ensuring that it:

- Prepares its SEFA beginning and outstanding balances and new loans processed correctly in the notes to its SEFA.
- Reports appropriate expenditures for each federal award and cluster of federal programs.
- Reports correct CFDAs for each federal award.
- Reports federal revenues and reconciling items correctly and only when appropriate in the notes to its SEFA.

Views of Responsible Officials

- *Overstated expenditures by $1,247,151 for 1 Student Financial Assistance CFDA program. UT Southwestern did not make disbursements for this program in fiscal year 2018. Instead, that amount represented the entire balance of the program. As a result, UT Southwestern (1) overstated the outstanding balance of loans by $1, 236,735 in Note 3a to its SEFA (2) understated the beginning balance of outstanding loans by $10,416 in Note 3a to its SEFA, and (3) overstated new loans processed amount by $1,247,151 in Note 2 and Note 3a to its SEFA.*

UT Southwestern acknowledges and agrees that a data entry error occurred that resulted in an overstatement of expenditures. We have added an additional step to our review process to reduce the risk of future errors – see detail below.

Corrective Action Plan

We have updated our report review procedures to include the Financial Aid Office as a reviewer. This will allow the business owner to provide an additional review of the report to ensure accuracy.

Implementation Date: February 8, 2019

Responsible Person: Director of Fiscal Reports and Accounting Operations

Views of Responsible Officials

- *Incorrectly classified $360,220 in expenditures using a generic CFDA (43.000) instead of the CFDA identified in the award agreement (43.003).*

UT Southwestern acknowledges and agrees that a data entry error of CFDA 43.000 rather than 43.003 resulted in classifying the respective expenditures to the National Aeronautics and Space Administration (NASA) generic CFDA, rather than to NASA's specific program, Exploration.

Corrective Action Plan

We recently realigned SPA personnel to create a dedicated award set-up team, and have reiterated the importance for each person to review their entries carefully and assure all CFDA entries are accurate and directly represent the CFDA provided within the NOA—original or as amended. Further, we are reviewing options as to how we can enhance system controls and quality reviews within the entry process.

Implementation Date: February 8, 2019 – June 01, 2019

Responsible Person: Director of Post Award Accounting

Views of Responsible Officials

- *Overstated federal revenue by $112,085 in Note 2 to its SEFA and incorrectly included a reconciling item (specifically, federal revenue received under a vendor relationship between the agency and the federal government) related to that revenue in Note 2 to its SEFA. That occurred because UT Southwestern incorrectly reported federal revenue received from vendor relationships with non-federal government entities.*

UT Southwestern acknowledges and agrees that revenue recognized under an agreement(s) with the Dallas VA Research Corporation was incorrectly reported on UT Southwestern's SEFA.

Corrective Action Plan

We recently realigned SPA personnel to create a dedicated award set-up team, and have reiterated the importance for each individual to assure any assignment of a CFDA requires sufficient and appropriate support narrated within the award—original and/or as amended. Further, we are reviewing options as to how we can enhance system controls and quality reviews within the entry process.

Implementation Date: February 8, 2019 – June 01, 2019

Responsible Person: Director of Post Award Accounting

Views of Responsible Officials

- *Incorrectly included $212,064 in expenditures related to 2 CFDAs on its SEFA; it should have included those expenditures as a reconciling item (specifically, federal revenue received under a vendor relationship between the agency and the federal government) in Note 2 of its SEFA. As a result, UTSW overstated expenditures on its SEFA by $212,064*

UT Southwestern acknowledges that expenditures incurred under an agreement with the VA North Texas Health Care System to support residents and fellows in training was incorrectly reported on its SEFA.

Corrective Action Plan

We recently realigned SPA personnel to create a dedicated award set-up team, and have reiterated the importance for each individual to assure any assignment of a CFDA requires sufficient and appropriate support narrated within the award—original and/or as amended. Further, we are reviewing options as to how we can enhance system controls and quality reviews within the entry process.

Implementation Date: February 8, 2019 – June 01, 2019

Responsible Person: Director of Post Award Accounting

Views of Responsible Officials

- *Overstated $176,270 in expenditures related to 2 CFDAs. That occurred because UT Southwestern included non-federal expenditures on its SEFA. As a result, UT Southwestern overstated federal revenue by $176,270 in Note 2 to its SEFA.*

UT Southwestern acknowledges that the above referenced expenditures were reported on its SEFA, with likely insufficient support. In particular and for the respective expenditures, the correlating agreement included a multitude of federal requirements, typically required and present within a federal flow through agreement. However, UT Southwestern acknowledges that there was also no specific reference to a CFDA therein.

Corrective Action Plan

We recently realigned SPA personnel to create a dedicated award set-up team, and have reiterated the importance for each individual to assure any assignment of a CFDA requires sufficient and appropriate support narrated within the award—original and/or as amended. Further, we are reviewing options as to how we can enhance system controls and quality reviews within the entry process.

Implementation Date: February 8, 2019 – June 01, 2019

Responsible Person: Director of Post Award Accounting

Federal Award Findings and Questioned Costs

A finding regarding the Schedule of Expenditures of Federal Awards for fiscal year 2018 was included in Chapter 2-A of this report. All other fiscal year 2018 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, 2018*, 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, 2018

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, March 2016).

State of Texas Financial Portion of the Statewide Single Audit Report for the Year Ended August 31, 2016 (State Auditor's Office Report No. 17-555, February 2017).

State of Texas Financial Portion of the Statewide Single Audit Report for the Year Ended August 31, 2017 (State Auditor's Office Report No. 18-555, February 2018).

The Summary Schedule of Prior Audit Findings (for the year ended August 31, 2018) has been prepared to address these responsibilities.

Chapter 4-A

The Office of the Comptroller of Public Accounts Should Strengthen 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. 18-555-01
(Prior Audit Issue 17-555-01 and 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 2017 financial statements and financial data in the State's accounting system. As a result, auditors concluded that there was a material weakness in the internal control processes for financial reporting 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 misstated the fiscal year 2017 fund balances by $4.2 billion on its fund financial statements and in the State's accounting system. That occurred because the Comptroller's Office incorrectly recorded in its own financial records adjusting journal entries that incorrectly recorded $4.2 billion in fund balance.

The Comptroller's Office's review process for adjusting journal entries and 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.

After auditors brought the issue discussed above to the Comptroller's Office's attention, the Comptroller's Office corrected the balances reported on its financial statements during the preparation of the State's Comprehensive Annual Financial Report. As a result, the issue discussed above did not affect the accuracy 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 accurately reports balances on its financial statements.

Views of Responsible Officials and Corrective Action Plan

Corrective action was taken.

Chapter 4-B

The Texas Workforce Commission Should Strengthen Certain Controls Over Financial Reporting

Issue 1

The Texas Workforce Commission Should Strengthen Its Financial Reporting Processes

Reference No. 18-555-02
(Prior Audit Issue 17-555-02)

Type of finding: Significant Deficiency

The Texas Workforce Commission (Commission) strengthened its process to help ensure that the financial information it reported to the State's accounting system reconciled to the Commission's internal accounting system. The Commission developed policies and procedures related to financial reporting; however, those policies and procedures did not ensure that its fiscal year 2017 financial information was accurately reported to the State's accounting system.

The Commission misclassified $143.2 million in net position balances for the Unemployment Trust Funds that it submitted to the State's accounting system. That $143.2 million amount was the sum of two classification errors that the Commission made. Specifically, the Commission:

- Incorrectly classified $243.5 million in net position for one fund as unrestricted when those funds should have been reclassified as restricted for unemployment.
- Incorrectly classified a negative $100.3 million in net position for one fund as unrestricted when those funds should have been reclassified as restricted for debt retirement.

The Office of the Comptroller of Public Accounts' (Comptroller's Office) *Reporting Requirements for Fiscal Year 2017 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, 2017, 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 published fiscal year 2017 annual financial report; however, its financial reporting processes did not ensure that its net position balances were accurately reported 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 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 continue to strengthen its process for reviewing the financial information that it submits to the State's accounting system to ensure that it submits accurate financial information.

Views of Responsible Officials and Corrective Action Plan

Corrective action was taken.

Chapter 4-C

The Health and Human Services Commission Should Strengthen Controls Over Information Technology

Issue 1

The Health and Human Services Commission Should Strengthen Controls Over Its Management and Monitoring of Certain Information Technology

Reference No. 18-555-03
(Prior Audit Issues 17-555-03, 16-555-03, 15-555-02, and 14-555-03)

Type of finding: Significant Deficiency

Auditors identified significant weaknesses in controls over the information technology that the Health and Human Services Commission (Commission) used to process claims from the Home and Community Based Services Program and the Texas Home Living Waiver Program (Programs) (see text box for additional information on those Programs and the agencies that administered them). The Commission did not fully implement recommendations to strengthen information technology controls that the State Auditor's Office made in its audit reports starting in fiscal year 2013. Specifically, the Commission:

- 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.

> **Home and Community Based Services Program and the Texas Home Living Waiver Program (Programs)**
>
> The Department of Aging and Disability Services (Department) originally administered the Home and Community Based Services Program and the Texas Home Living Waiver Program (Programs). The Department was abolished effective September 1, 2017, and all of the Department's functions were transferred to the Health and Human Services Commission (Commission).
>
> Prior to the abolition of the Department, the Commission was responsible for certain aspects of the Department's information technology.
>
> Source: Senate Bill 200, 84th Legislature.

To protect the integrity of its information, the Commission should strengthen its management and monitoring of the information technology controls.

User Access

The Commission took steps to remove some inappropriate user accounts that auditors identified in the prior-year audit; however, it has not corrected certain user access weaknesses. 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.

As discussed below, auditors identified various access issues related to Program operations.

Mainframe Accounts. Auditors reviewed all active user accounts associated with the mainframe that houses the ID CARE system. ID CARE is the claims adjudication system for the Programs, and the information in ID CARE feeds into the payment process. A total of 39 percent of those user accounts were inactive. Specifically:

- No individuals had ever logged into 17 percent of those user accounts.
- No individuals had logged into 22 percent of those user accounts during the 90-day period preceding October 17, 2017.

Accounts Associated with Centralized Program Operations. Auditors reviewed active user accounts discussed above that were associated with centralized Program operations. During that review, auditors identified active user accounts for individuals who were not current employees.

To minimize the risks associated with public disclosure, auditors provided the details of control weaknesses related to logical access discussed above, in addition to other logical access weaknesses, separately to the Commission in writing.

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

Some passwords did not comply with the requirements in the Commission’s policies and procedures for passwords. Policies and procedures provide guidance for user password requirements and not ensuring the policies and procedures are followed increases the potential risk of unauthorized access to IT systems.

Recommendations

The Commission 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 passwords comply with requirements in the Commission policies and procedures.

Views of Responsible Officials and Corrective Action Plan

Corrective action was taken.

Chapter 4-D

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

Reference No. 18-555-04
(Prior Audit Issues 17-555-04, 16-555-04, 15-555-05, 14-555-07, 13-555-02, 11-555-17, and 10-555-26)

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, U.S. 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 higher education institutions and agencies discussed below did not appropriately prepare or adequately review their fiscal year 2017 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 higher education institutions and agencies discussed below reported $2,646,460,940 in federal expenditures, or 5 percent of the total federal expenditures the State of Texas reported for fiscal year 2017. The errors listed below were not material to the fiscal year 2017 SEFA for the State of Texas or to the fiscal year 2017 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 Houston

The University of Houston (U of H) incorrectly excluded from its fiscal year 2017 SEFA $70,115 in administrative costs related to 1 Student Financial Assistance Catalog of Federal Domestic Assistance program (CFDA). That occurred because U of H did not record those expenditures as federal funds. As a result, U of H (1) understated expenditures on its SEFA by $70,115 and (2) understated federal revenue by $70,115 in Note 2 to its SEFA.

Corrective Action:

Corrective action was taken.

The University of North Texas

The University of North Texas (UNT) (1) incorrectly excluded from its fiscal year 2017 SEFA $3,516 in expenditures for 1 Student Financial Assistance CFDA program and (2) incorrectly included on its fiscal year 2017 SEFA $415,856 in expenditures for a different Student Financial Assistance CFDA program. Those errors occurred because UNT incorrectly included on its SEFA adjustments that were not associated with fiscal year 2017 disbursement activity. As a result, UNT (1) overstated expenditures on its SEFA by $412,340 and (2) overstated federal revenue by $412,340 in Note 2 to its SEFA.

Corrective Action:

Corrective action was taken.

The University of Texas at Arlington

On its fiscal year 2017 SEFA, the University of Texas at Arlington (UT-Arlington) (1) overstated federal revenue by $1,632,899 for 1 CFDA program and (2) incorrectly included a reconciling item related to that revenue in Note 2 to its SEFA. That occurred because UT-Arlington incorrectly included $1,632,899 in non-federal revenue as federal revenue in the notes to its fiscal year 2017 SEFA.

Corrective Action:

Corrective action was taken.

The University of Texas at El Paso

The University of Texas at El Paso (UTEP) understated expenditures on its fiscal year 2017 SEFA by $967,373 for 4 Student Financial Assistance CFDA programs. That occurred because UTEP (1) incorrectly excluded fiscal year 2017 expenditures from its SEFA and (2) incorrectly included prior period adjustments not associated with fiscal year 2017 disbursement activity on its SEFA. As a result, UTEP understated federal revenue by $967,373 in Note 2 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 in the appropriate fiscal year.

Implementation Status

Partially implemented.

Views of Responsible Officials 2017

The University acknowledges and agree 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 2017

The University has already implemented process enhancements to ensure that the timing differences between the Student and Accounting Systems are addressed during the AFR process. Additionally, the Office of Student Financial Aid and Financial Reporting Office will identify all Federal Programs not subject to prepaid calculations to ensure the expenditures are reported accurately.

Responsible Person: Director Financial Reporting

Implementation Date: February 28, 2018

Views of Responsible Officials 2018

The University acknowledges and agree 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 2018

As previously stated, the University already implemented the necessary process enhancements that ensured that the timing differences between the Student and Accounting Systems were properly addressed during the AFR process. Additionally, the Office of Student Financial Aid and Financial Reporting Office will continue identifying all Federal Programs not subject to prepaid calculations to ensure the expenditures are reported accurately.

Implementation Date:	*February 28, 2018.* *Reviewed February 11, 2019.*
Responsible Person:	*Director Financial Reporting*

The University of Texas at San Antonio

The University of Texas at San Antonio (UTSA) understated expenditures on its fiscal year 2017 SEFA by $198,775 for 1 Student Financial Assistance CFDA program. That occurred because UTSA incorrectly excluded fiscal year 2017 expenditures from its SEFA. As a result, UTSA understated federal revenue by $198,775 in Note 2 to its SEFA.

Recommendation

UT-San Antonio should strengthen its SEFA preparation and review process to help ensure that it prepares its SEFA correctly, including ensuring that it reports expenditures in the appropriate fiscal year.

Implementation Status

Partially implemented.

Views of Responsible Officials 2017

The University acknowledges and agree 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 2017

The University will take the following actions to improve the process. The Controller's Office works closely with Student Financial Aid to reconcile the awards during the fiscal year and will continue to do so during the preparation of the SEFA. Financial Aid will ensure proper project IDs for the appropriate project year are used. To help ensure the expenditures are recorded in the fiscal year incurred, the Controller's Office will collaborate with the Accounting Office to ensure that non-exchange expenditures like TEACH are not deferred until the related academic year but are recognized at disbursement.

Responsible Person: Assistant Vice President of Financial Affairs and Controller

Implementation Date: August 31, 2018

Views of Responsible Officials 2018

The University acknowledges and accepts the repeated finding. The University and UT System had already finalized fiscal year 2017 reporting and could not make the change in fiscal year 2017. Therefore, the University's fiscal year 2018 reporting could not be changed because the expenditure had already been reported and changing the amount would have either misstated the University's cumulative expenditures under this program or caused a difference in the SEFA reconciliation footnote (Note 2).

Corrective Action Plan 2018

As noted in the prior year Corrective Action Plan, the University has already taken the following actions to improve the process. The Controller's Office works closely with Student Financial Aid to reconcile the awards during the fiscal year and will continue to do so during the preparation of the SEFA. Financial Aid ensures proper project IDs for the appropriate project year are used. To help ensure the expenditures are recorded in the fiscal year incurred, the Controller's Office collaborates with the Accounting Office to ensure that non-exchange expenditures like TEACH are not deferred until the related academic year but are recognized at disbursement.

Implementation Date:	*September 1, 2018*
Responsible Person:	*Associate Vice President of Financial Affairs and Controller*

Department of Aging and Disability Services

The Department of Aging and Disability Services (DADS) incorrectly excluded from its fiscal year 2017 SEFA $36,975,024 in expenditures for 3 CFDA programs. That occurred because of errors related to DADS's preparation process for its SEFA. As a result, DADS (1) understated expenditures on its SEFA by $36,975,024 and (2) understated federal revenue by $36,975,024 in Note 2 to its SEFA. Effective September 1, 2017, the Legislature abolished DADS and transferred all of DADS's services to the Health and Human Services Commission (HHSC).

Corrective Action:

Corrective action was taken.

Department of Family and Protective Services

On its fiscal year 2017 SEFA, the Department of Family and Protective Services (DFPS) (1) incorrectly classified $23,816,721 in direct expenditures as pass-through expenditures for 3 CFDA programs and (2) incorrectly classified $1,584,882 in pass-through expenditures as direct expenditures for 1 CFDA program. That occurred because DFPS misclassified certain expenditures on its fiscal year 2017 SEFA.

Corrective Action:

Corrective action was taken.

During fiscal year 2018, one higher education institution had uncorrected recommendations from issues identified during the audit of its fiscal year 2015 Schedule of Expenditures of Federal Awards (SEFA). Auditors conducted limited procedures to follow up on the status of the findings related to the preparation of its SEFAs in fiscal years 2016, 2017, and 2018. The University fully implemented the recommendations from the prior audit.

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

The higher education institution discussed below did not appropriately prepare or adequately review its fiscal year 2015 SEFA.

Sam Houston State University

Sam Houston State University (SHSU) incorrectly excluded expenditures for three Student Financial Assistance CFDAs from its SEFA. Specifically, it incorrectly excluded $2,380,458 for 3 CFDAs. As a result, SHSU (1) understated expenditures on its SEFA by $2,380,458 for 3 CFDAs; (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.

Corrective Action:

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, 2018.

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, 2018, was dated February 21, 2019.

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 Year Ended August 31, 2018,* by KPMG.

Methodology

The audit methodology included collecting information, verifying certain information collected, 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 the audit.

Sampling Methodology

As part of the audit procedures performed at Texas A&M University System, auditors selected 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 2018 depreciable capital assets beginning balances contained misstatements that materially affected the current period's financial statements.
- Appropriate accounting policies reflected in the fiscal year 2018 beginning balances had been consistently applied in the current period's financial statements and any changes were appropriately accounted for and adequately presented and disclosed in accordance with the applicable financial reporting framework.

Auditors determined that the fiscal year 2018 beginning balances for depreciable capital assets described above were fairly presented.

As part of the audit procedures performed on the SEFA, auditors selected a risk-based sample of generic Catalog of Federal Domestic Assistance numbers (CFDAs) to test that the correct unique identifying number was reported.

<u>Information collected and reviewed</u> 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, which consisted of accounting data from agency and higher education institution internal accounting systems and accounting data from the Uniform Statewide Accounting System.
- Agency and higher education institution year-end accounting adjustments.
- Agency and higher education institution fiscal year 2018 annual financial reports.
- Agency and higher education institution fiscal year 2018 SEFA submissions to the Office of the Comptroller of Public Accounts.

Information systems reviewed included the following:

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

Procedures and tests conducted included the following:

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

Criteria used included the following:

- Texas Statutes.
- Texas Administrative Code.
- General Appropriations Act (85th Legislature).
- The Office of the Comptroller of Public Accounts' policies and procedures.
- The Office of the Comptroller of Public Accounts' *Reporting Requirements for the Annual Financial Reports of State Agencies and Universities*.
- Agency and higher education institution policies and procedures.

- Title 2, U.S. Code of Federal Regulations, Section 200, *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 Govermental Accounting Standards Board and the Financial Accounting Standards Board.

Project Information

Audit fieldwork was conducted from August 2018 through February 2019. 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)
- Philip Stringer, CPA (Assistant Project Manager)
- Robert H. (Rob) Bollinger, CPA, CGMA, CFE
- Morgan Burandt, CPA
- Chase Dierschke, MAcy
- Lauren Futch, CPA
- Elizabeth Gallegos, MAcc
- Jennifer Grant, MPA
- Taylor L. Huff, CFE
- Joyce Inman, CGFM

- Douglas Jarnagan, MAcc
- Alana Montoro
- Anca Pinchas, CPA, CISA, CIDA
- Melissa M. Prompuntagorn, CFE
- Sarah-Jane M. Puerto, CIA, CFE, CGAP
- Fabienne Robin, MBA
- Nakeesa Shahparasti, CPA, CFE,CISA
- Nathan Stein
- Alexander Sumners
- Michelle Ann Duncan Feller, CPA, CIA (Quality Control Reviewer)
- Michael Owen Clayton, CPA, CISA, CFE, CIDA (Audit Manager)

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

- Bianca F. Pineda (Project Manager)
- Adam K. Ryan (Assistant Project Manager)
- Kirstin Adamcik, MBA
- Ro Amonett, MPA
- Adam Berry
- Charlotte Carpenter, CPA
- Brandy Corbin
- Rebecca Franklin, CFE, CISA, CGAP
- Ann E. Karnes, CPA (Quality Control Reviewer)
- Audrey O'Neill, CFE, CGAP, CIA (Audit Manager)

Agencies and Higher Education Institutions Audited

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

- Health and Human Services Commission.
- Office of the Comptroller of Public Accounts.
- Texas A&M University System.
- 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:

- Commission on Environmental Quality.
- Department of Family and Protective Services.
- Department of State Health Services.
- Department of Transportation.
- General Land Office.
- Health and Human Services Commission.
- Higher Education Coordinating Board.
- Sam Houston State University (auditors performed only prior-year finding follow-up work).
- Texas Education Agency.
- Texas Workforce Commission.
- The University of Texas at Arlington (auditors performed only prior-year finding follow-up work).
- The University of Texas at Austin.
- The University of Texas at El Paso (auditors performed only prior-year finding follow-up work).

- The University of Texas at San Antonio (auditors performed only prior-year finding follow-up work).
- The University of Texas Health Science Center at Houston.
- The University of Texas M.D. Anderson Cancer Center.
- The University of Texas Medical Branch at Galveston.
- The University of Texas Southwestern Medical Center.
- University of Houston (auditors performed only prior-year finding follow-up work).
- University of North Texas (auditors performed only prior-year finding follow-up work).

Copies of this report have been distributed to the following:

Legislative Audit Committee

The Honorable Dan Patrick, Lieutenant Governor, Joint Chair
The Honorable Dennis Bonnen, 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 Dustin Burrows, 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

Commission on Environmental Quality
Department of Family and Protective Services
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
Sam Houston State University
Texas A&M University System
Texas Education Agency
Texas Workforce Commission
University of Houston
University of North Texas
The University of Texas at Arlington
The University of Texas at Austin
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 M.D. Anderson Cancer Center
The University of Texas Medical Branch at Galveston
The University of Texas Southwestern Medical Center