



State of Ohio

Financial Reporting Enterprise Audit

Audit period: February 1, 2009 to April 30, 2009



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Executive Summary

Background

As part of the Fiscal Year 2009 State of Ohio Enterprise Audits, the OBM Office of Internal Audit (OIA) conducted an audit of State and Federal Financial Reporting processes. The audit of the State Financial Reporting process was conducted at the Office of Budget and Management (OBM) Financial Reporting Section. At the time of the audit, the OBM Financial Reporting Section was for the first time, completing the fiscal year 2008 financial statements utilizing the State's new Ohio Administrative Knowledge System (OAKS).

The Federal Financial Reporting is a decentralized process which is completed at the individual state agency. Audit work was performed at a detail level at the Department of Job & Family Services and the Department of Transportation. Additionally, inquiries of processes were made at the other 19 state agencies within the OIA oversight.

The governance structure for OAKS and the financial application was modified in early 2009. The OAKS enterprise resource planning (ERP) system is managed by three governing bodies:

- The OAKS Executive Board meets quarterly and consists of the department directors at DAS, OBM, Insurance, and Job & Family Services and the OAKS Steering Committee Chair. They are responsible for business oversight, risk management escalation, and approval of large projects.
- The OAKS Steering Committee is a nine member body which meets monthly and has overall strategic IT oversight. Additionally, they are responsible for issue and risk management as well as large discretionary change requests.
- The OAKS Change Control Board is an 11 member body which meets bi-weekly to serve as a central point for logging system changes and approving small discretionary change requests.

The OAKS financial application is overseen by OBM.

During the audit, OIA identified opportunities for OBM to strengthen internal controls and improve business operations. Summary and detailed observations have been provided. OIA would like to thank OBM staff and management for their cooperation and time in support of this audit.



Scope and Objectives

Crowe Horwath, LLP, was engaged by OIA to review enterprise risks related to the State and Federal Financial Reporting processes. This work was completed between March 13, 2009 and May 27, 2009 with an update completed by OIA in July 2009. The scope of this audit included the following areas:

- State Financial Reporting
 - Cash transaction activity roll up in State’s financial statements;
 - OAKS’s general ledger to Treasurer of State cash balance reconciliation process;
 - GAAP package process to gather state agency financial information; and
 - Journal entry process to record accrual entries in OAKS general ledger
- Federal Financial Reporting
 - Federal reports accurately and timely submitted to appropriate Federal agency

The following summarizes the objectives of the review along with a conclusion on the effectiveness of management’s internal controls.

Objective	Conclusion ¹
Evaluate the design and effectiveness of controls over the OAKS general ledger amounts compared with sub ledger totals	Major Improvements Needed – See Observation 1
Evaluate the completeness and accuracy of the OAKS general ledger reconciliation to the Treasurer of State’s bank balance.	Improvements Needed – See Observation 2
Evaluate the design and effectiveness of the GAAP package process used by the OBM Financial Reporting Section to gather accrual information from various state agencies.	Well-Controlled
Evaluate the design and effectiveness of the journal entry process used by the OBM Financial Reporting Section to enter accrual information into the OAKS general ledger.	Well-Controlled
Evaluate the completeness and accuracy of Federal report submission by selected state agencies.	Well-Controlled with Improvements Needed

¹ Refer to [Appendix A](#) for classification of audit objective conclusions.



Summary of Observations and Recommendations

The Summary of Observations and Recommendations includes only those risks which were deemed high or moderate. Low risk observations and recommendations were discussed with individual agency management and are not part of this report. However, the low risk observations and recommendations were considered as part of the audit objective conclusions above.

No.	Observation	Recommendation	Risk ²
1.	<p>OAKS General Ledger Reconciliation to Sub Ledgers - The OAKS general ledger revenue and expense totals did not agree to the sub ledgers for fiscal year 2008. Although the variance amounts are being identified, the reconciliation variances for revenue were .6% and expenses were 2.5% of their respective totals. The majority of the expense variances occurred when submitted payroll amounts exceed individual fund budgetary or allotment levels. The variances are created by adjustments to the transaction data after entry in OAKS.</p>	<p>Develop a process to require adjustments be made to the sub ledgers and the OAKS general ledger. If this is not possible, a detailed listing should be maintained to identify individual adjustments not included in each sub ledger.</p>	<p>High</p>
2.	<p>Cash Reconciliation - The OBM reconciliation as of December 31, 2008, identified two areas between the State’s cash position as maintained by the Treasurer of State and the OAKS general ledger that were not reconciled. The first area relates to approximately \$27 million in cancelled and voided warrants which were not posted. The second area relates to a design error in OAKS for intra-state transfer vouchers (ISTV) where approximately \$19 million of pending ISTV transactions remain unresolved.</p>	<p>The OBM reconciliation team should research and close the cancelled/voided warrant differences. Additionally, an OAKS system edit needs to be in place to hold incomplete ISTV transactions until resolved.</p>	<p>Moderate</p>

Due to the limited nature of our audit, we have not fully assessed the cost-benefit relationship of implementing the observations and recommendations suggested above. However, these observations reflect our continuing desire to assist your agencies in achieving improvements in internal controls, compliance, and operational efficiencies.

² Refer to [Appendix A](#) for classification of audit observations.



Detailed Observations and Recommendations

Observation 1 – OAKS General Ledger Reconciliation to Sub Ledgers

The OAKS general ledger represents the revenue and expense transaction activity which is used to produce the State of Ohio financial statements. The OAKS general ledger entries summarize multiple state agency transactions. OAKS produces detailed transactions from the accounts receivable, accounts payable, and payroll sub ledgers to produce general ledger entries.

The OAKS general ledger revenue and expense totals did not agree to the sub ledgers for fiscal year 2008. Although the variance amounts are being identified, the reconciliation variances for revenue were .6% and expenses were 2.5% of their respective totals. The variances were created by adjustments to the transaction data after entry in OAKS. The majority of the expense variances occurred when submitted payroll amounts exceed individual fund budgetary or allotment levels. Due to the time sensitivity of the payroll processing, OAKS general ledger entries are made to correct these errors; however, the detailed payroll records maintained in the payroll sub ledger are not subsequently corrected.

Adjusting the OAKS general ledger without adjusting the corresponding sub ledger entry creates a risk that some detailed transactions will present fund sources or uses, which were not ultimately presented in the State's financial statements. The State's book of record for both summary and detailed ledgers should agree.

Recommendation

A process should be developed to require adjustments be made to the sub ledgers and the OAKS general ledger. If this is not possible, a detailed listing should be maintained to identify individual adjustments not included in each sub ledger.

Management Response

The OAKS General Ledger Team and State Accounting have completed an initial review of these variances. The majority of these entries occur to reclassify payroll expense from the initial distribution in the HCM Payroll system to the appropriate accounting stream in order to clear budget checking and properly report in the general Ledger. This process is necessary to sync up chart fields between the systems due to the initial configuration of FIN and HCM. Because HCM went live prior to FIN, HCM was programmed to interface into CAS, a non PeopleSoft application. When the system integration is properly configured HCM and FIN share common chart field values so that interfacing entries are validated prior to entering the GL. The OAKS Quality Assurance team is working with Oracle to determine the size of this remediation effort.

In the interim the GL team and State Accounting have developed a reconciliation process using a variety of queries to validate the payroll interfaces. This reconciliation is completed prior to year end close, however, there are plans to complete it on a more timely basis.



Additionally, there are a finite number of non-payroll journal entries that bypass the sub ledgers and post directly to the OAKS general ledger. These occur for error corrections and reclassification of large subsidy payments where reversal and correction through the sub-modules is impractical. A policy is being developed by State Accounting that will further limit this activity.

Risk	Remediation Owner	Estimated Completion Date
High	OBM Deputy Director of State Accounting	June 2010



Observation 2 – Cash Reconciliation

OBM records the State’s book balance through the OAKS general ledger while the Treasurer of State maintains the State’s bank balance. On a monthly basis, OBM performs a reconciliation of the book and bank balance.

The OBM reconciliation as of December 31, 2008, identified two areas between the State’s cash position as maintained by the Treasurer of State and the OAKS general ledger that were not reconciled. The first area relates to approximately \$27 million in cancelled and voided warrants, which predominately occurred prior to the OAKS application in July, 2007, that were not posted. These are transactions recorded as expenses in the State’s book balance but were not later removed.

The second area relates to a design error in OAKS for intra-state transfer vouchers (ISTV). ISTVs are paper entries that occur between state agencies but do not impact the bank balance. An ISTV should have a debit entry with agency, fund, and amount; and, a corresponding credit entry with agency, fund, and amount. However, during fiscal year 2008 and the course of this audit, state agencies were not required by OAKS to identify the credit entry agency or fund prior to processing the transaction. This resulted in an ISTV debit entry to process and the corresponding credit entry to fail and create a book balance error. As of December 31, 2008, approximately \$19 million of pending ISTV transactions remain unresolved.

These two reconciliation issues must be resolved even though the risk is lessened slightly by the fact the State’s bank balance is higher than the State’s book balance.

Recommendation

We recommend the OBM reconciliation team research and close the cancelled/voided warrant differences. Additionally, an OAKS system edit needs to be in place to hold incomplete ISTV transactions while the processed pending ISTVs can be investigated and completed.

Management Response

State Accounting has developed a comprehensive reconciliation process to reconcile daily cash receipts and disbursements with the Treasurer of State. While it is possible to verify daily activity we lack certain information related to ISTV’s and outstanding warrants to completely reconcile to beginning and ending TOS balances.

The appropriate edit checks have been activated in OAKS, requiring agencies to match their ISTV transactions to the corresponding transaction from other agencies. This should rectify the problem going forward, although the existing un-reconciled ISTVs need to be researched and resolved in the sub ledgers. We are actively working to acquire the staff to perform this function.

We have formally requested an outstanding warrants report that is in the functional design process by the RACM team. This is a complicated report since it must capture the warrants issued by FIN and HCM that share the common bank account.



Once these tools and personnel are in place, a standard reconciliation can be completed and variances investigated. The goal is to net the identified \$27million cancelled/voided warrants difference occurring prior to July 2007 with any differences discovered since go live and process a one-time appropriate adjustment which we believe will be an increase to the General Revenue Fund.

Risk	Remediation Owner	Estimated Completion Date
Moderate	OBM Deputy Director of State Accounting	June 2010



Appendix A – Classification of Audit Objective Conclusions and Observations

Classification of Audit Objective Conclusions

Conclusion	Description of Factors
Major Improvements Needed	Weaknesses are present that could potentially compromise achievement of its overall purpose. The impact of weaknesses on management of risks is widespread due to the number or nature of the weaknesses.
Improvements Needed	Weaknesses are present that compromise achievement of one or more control objectives but do not prevent the process from achieving its overall purpose. While important weaknesses exist, their impact is not widespread.
Well-controlled with Improvements Needed	The processes have design or operating effectiveness deficiencies but do not compromise achievement of important control objectives.
Well-Controlled	The processes are appropriately designed and are operating effectively to manage risks. Control issues may exist, but are minor.

Classification of Audit Observations

Rating	Description of Factors	Reporting Level
High	Observation has broad (state or agency wide) impact and possible or existing material exposure requiring immediate agency attention and remediation.	Audit Committee, Senior Management, Department Management
Moderate	Observation has moderate impact to the agency. Exposure may be significant to unit within an agency, but not to the agency as a whole. Compensating controls may exist but are not operating as designed. Requires near-term agency attention.	Audit Committee, Senior Management, Department Management
Low	Observation poses relatively minor exposure to an agency under review. Represents a process improvement opportunity.	Department Management, Senior Management (Optional), Audit Committee (Not reported)



Appendix B – Audit Follow-up Procedures

OIA will periodically follow-up on management's plans to remediate high and moderate risk audit observations. Follow-up activities may generally be broken down into three categories:

- Detailed** Detailed follow-up is usually more time-consuming and can include substantial audit customer involvement. Verifying and testing procedures implemented as well as substantiating records are examples. The more critical audit observations usually require detailed follow-up.

- Limited** Limited follow-up typically involves more audit customer interaction. This may include actually verifying procedures or transactions and, in most cases, cannot be accomplished through memos or telephone conversations with the audit customer but requires onsite observation or testing.

- Informal** This is the most basic form of follow-up and may be satisfied by review of the audit customer's procedures or an informal telephone conversation. Memo correspondence may also be used. This is usually applicable to the less critical observations.

Low risk audit observations will not result in an OIA audit follow-up, although these observations will be factored into the continuous risk assessment process for future OIA engagements.