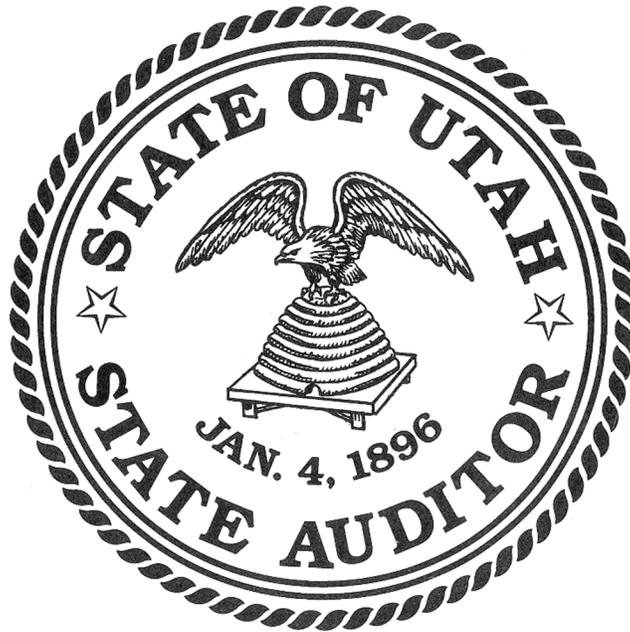


DEPARTMENT OF ADMINISTRATIVE SERVICES

Management Letter
For the Year Ended June 30, 2020

Report No. 20-29



OFFICE OF THE STATE AUDITOR

AUDIT LEADERSHIP:

John Dougall, State Auditor
Hollie Andrus, CPA, Deputy State Auditor
Ryan Roberts, CPA, Audit Supervisor

DEPARTMENT OF ADMINISTRATIVE SERVICES
FOR THE YEAR ENDED JUNE 30, 2020

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<u>Finding Type:</u>	<u>Applicable To:</u>
MW Material Internal Control Weakness	s State Financial Statements
SD Significant Deficiency of Internal Control	f Federal Program
MN Material Noncompliance	e Entity Financial Statements
RN Reportable Noncompliance or Illegal Acts	



OFFICE OF THE
STATE AUDITOR

MANAGEMENT LETTER NO. 20-29

March 22, 2021

Ms. Jenney Rees, Executive Director
Department of Administrative Services
4315 South 2700 West, 3rd Floor
Taylorsville, UT 84129-2128

Dear Ms. Rees:

This management letter is issued as a result of our audit of the basic financial statements of the State of Utah as of and for the year ended June 30, 2020. It is also issued as a result of the Department of Administrative Service's (the Department's) portion of the statewide single audit for the year ended June 30, 2020. Our audit was conducted 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.

Our final reports on compliance and on internal control at the financial statement and major federal program level required under Government Auditing Standards and/ or federal Uniform Guidance, will be issued under a separate cover. These reports will also provide further detail as to considerations made during the course of the audit regarding internal controls and compliance, both at the financial statement and at the federal program level, and the limited purposes of those considerations. The purpose of this letter is to communicate with Department management concerns identified during the course of our audit.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees to prevent or to detect and correct on a timely basis misstatements, errors, or instances of noncompliance. *A material weakness in internal control* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that material misstatements, errors, or noncompliance are not prevented or are not detected and corrected on a timely basis.

Based on the audit procedures performed, we identified certain deficiencies in internal control (Findings 1–3) which we consider to be significant enough to merit the further attention of management and those charged with governance. We also identified Finding 4 as an instance of noncompliance which we are required to report under *Uniform Guidance*.

The Department's written responses to and Corrective Action Plans for these findings will be included in the final reports identified in the second paragraph above.

The purpose of this communication is solely to describe the scope of our testing of internal control over compliance and the results of that testing and not to provide an opinion on the effectiveness of the Department's internal control over compliance. Accordingly, this communication is not suitable for any other purpose. However, pursuant to *Utah Code* Title 63G Chapter 2, this report is a matter of public record, and as such, its distribution is not limited.

We appreciate the courtesy and assistance Department personnel extended to us during the course of our audit, and we look forward to a continuing professional relationship. If you have any questions, please contact me.

Sincerely,

A handwritten signature in black ink that reads "Hollie Andrus". The signature is written in a cursive, flowing style.

Hollie Andrus, CPA
Deputy State Auditor
801-808-0467
handrus@utah.gov

cc: Marilee Richins, Deputy Director, Department of Administrative Services
Janica Gines, CPA, Director, Division of Finance
Patricia Nelson, CPA, Assistant State Comptroller
Cory Weeks, Accounting Operations Manager
Christopher Hughes, Director, Division of Purchasing and General Services
Brian Nelson, Director, Division of Risk Management

FINDINGS AND RECOMMENDATIONS

1. **ERRORS IN PREPARATION OF STATE'S COMPREHENSIVE ANNUAL FINANCIAL REPORT IDENTIFIED & CORRECTED**

The Department of Administrative Services' Division of State Finance (Finance) does not have adequate internal controls to ensure that the State's Comprehensive Annual Financial Report (CAFR) is properly prepared in accordance with generally accepted accounting principles. As a result, three significant audit adjustments were made to properly present the State's financial position and results of operations, as follows:

- One audit adjustment to include Utah Valley University's Foundation, increasing total net position for Discrete Component Units by \$138.3 million.
- One audit adjustment to reclassify \$105.6 million of "unrestricted net position" to "restricted net position" for "transit services" in the Discrete Component Units' net position.
- One audit adjustment to remove receivable and payable accruals associated with the State Trust Lands Administration, a non-major enterprise fund.

Finance should have adequate internal controls to ensure new personnel have adequate oversight to ensure the financial statements are prepared in accordance with generally accepted accounting principles. Inadequate controls may result in undetected misstatements in the State's financial statements.

Recommendation:

We recommend that Finance establish internal controls to ensure the State's financial statements properly reflect the financial position and results of operations of the State as a whole.

Entity's Response:

We agree with the findings and recommendations outlined in your Management Letter.

Corrective Action Plan:

The Division of Finance (the Division) is in the process of re-evaluating our internal controls over financial reporting for continued improvement by identifying potential internal control weaknesses and inefficiencies with the Annual Report process. Additional monitoring, reconciling, and analytical procedures will be added to the Annual Report process where needed to address the weaknesses which allowed the errors found in the audit and to help ensure we accurately capture, record, and report financial transactions and balances in accordance with generally accepted accounting principles. Additionally, we will also follow up on all audit adjustments to ensure that the underlying issues are resolved and future errors prevented.

Contact Person: Patricia Nelson, Assistant State Comptroller, State Division of Finance,
patriciarnelson@utah.gov

Anticipated Correction Date: June 30, 2021

2. UNTIMELY IDENTIFICATION AND RESOLUTION OF HOME LOAN RECONCILIATION DIFFERENCES

Federal Agencies: **Department of Housing & Urban Development (HUD)**

CFDA Numbers and Titles: **CFDA 14.239 Home Investment Partnership Program**

Federal Award Numbers: **M19-SG490100**

Questioned Costs: **N/A**

Pass-through Entity: **N/A**

Prior Year Single Audit Report Finding Numbers: **N/A**

Finance services Home Investment Partnership Program (HOME) loans on behalf of the Department of Workforce Services (DWS). Finance did not properly identify and resolve reconciling items between the State's loan tracking system and general ledger (FINET) for the HOME loans. DWS did not adequately monitor Finance's reconciliation to ensure differences were properly identified and resolved in a timely manner. Reconciling differences from the November 2019 and/or May 2020 reconciliations include the following:

- 29 items which spanned from fiscal year 2009 to 2019 and totaled \$1,169,228
- 18 unusual items which included "unknown differences" or amounts that did not appear to be HOME loan related and totaled \$1,368,151
- 1 unusual current fiscal year item left unresolved for a majority of the fiscal year in the amount of \$745,000.

Adequate internal controls over cash receipts, disbursements, and financial reporting rely upon the performance of monthly reconciliations between the loan system and the general ledger. This reconciliation procedure also ensures the correct use and reporting of the HOME loan principal and interest payments (program income). Reconciling differences should be investigated and resolved in a proper and timely manner.

Finance's focus on prioritizing current transactions rather than previous transactions combined with constraints of setting up loans in the loan system caused these errors to occur. Additionally, DWS, who is primarily responsible for compliance with HOME loan requirements, did not actively monitor loan servicing performed by Finance.

DWS uses program income to award and disburse new HOME loan funds prior to drawing additional funds from federal sources. Failure to properly identify and resolve loan fund transactions in a timely manner can result in undetected errors, fraud, or noncompliance with federal program income requirements.

Recommendation:

We recommend the following:

- 1. Finance and DWS work together to investigate and resolve the reconciling differences in a timely manner;**
- 2. Finance and DWS resolve loan system constraints to ensure accurate and proper recording and reporting of transactions; and**
- 3. DWS actively monitor loan servicing performed by Finance to ensure proper handling of HOME loan principal and interest payments (program income).**

Entity's Response:

We agree with the findings and recommendations outlined in your Management Letter.

Corrective Action Plan:

The net effect of the errors identified by the auditor totaled \$569,262. Reconciling the loans for the HOME program is complex due to the use of multiple subaccounts for the HOME program and a significant amount of activity between those subaccounts by both the Division and the Department of Workforce Services. The majority of the unreconciled items noted by the auditor occurred in years prior to the employment of current Division staff. Many items require extensive research to resolve due to the lack of evidence and documentation on old reconciliations. The Division has made it a priority to complete and resolve any remaining fiscal year 2020 reconciliations and reconciling items while also establishing additional controls and procedures to ensure that the loan management system (CLCS) is reconciled timely to the State's general ledger system (FINET) going forward. Additional process improvements include:

- Division management review of monthly loan fund reconciliations.*
- Regularly scheduled meetings between the Division and HOME program staff to resolve outstanding items or issues.*
- Division staff distributing monthly reports from CLCS to HOME program staff in order to verify correct coding and amount of disbursements.*
- The Division continuing to modify/update/develop policies and procedures surrounding the reconciliation process.*

Contact Person: Patricia Nelson, Assistant State Comptroller, State Division of Finance, patriciarnelson@utah.gov

Anticipated Correction Date: June 30, 2021

3. **MULTIPLE CORRECTIONS REQUIRED TO ACCURATELY REPORT SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS AND SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS**

Federal Agencies: **Various**

CFDA Numbers and Titles: **Various**

Federal Award Numbers: **Various**

Questioned Costs: N/A

Pass-through Entity: N/A

Prior Year Single Audit Report Finding Numbers: **N/A**

Schedule of Expenditures of Federal Awards (SEFA):

The State of Utah's (State) SEFA required multiple corrections to accurately reflect amounts expended under federal awards as of June 30, 2020. The State's Division of Finance (Finance) compiles the Schedule using information provided by multiple state agencies. Several agencies provided inaccurate information to the Division, information which Finance did not detect and correct. For instance,

- The Department of Workforce Services (DWS) initially did not include \$447,269,147 of State-funded Unemployment Insurance expenditures.
- Finance did not report \$23,512,157 of COVID-19 funding for the Supplemental Nutrition Assistance Program (SNAP) separate from the regular SNAP funding.
- The Utah State Board of Education (USBE) and DWS misreported \$48,843,003 in pass-through expenditures for 6 awards.
- USBE incorrectly reported the federal award number for 6 of 70 awards reviewed.

Finance and the entities noted above did not have written procedures to assist personnel in the SEFA preparation and have not established internal controls to ensure the accuracy of the information provided and used in the SEFA. Finance and the state entities should coordinate efforts to ensure accurate information is reflected in the SEFA.

Summary Schedule of Prior Audit Findings:

The Summary Schedule of Prior Audit Findings also required multiple corrections to accurately reflect those findings which still required corrective action by various state agencies. Finance prepares this schedule which spans multiple years of audits and tracks the agencies' progress in implementing previous audit findings and recommendations. New personnel at Finance did not understand the appropriate way to compile the schedule and included 8 findings for which corrective actions had been taken. Finance had not developed written procedures or established internal controls to ensure the schedule included the proper information.

Incomplete and inaccurate information and amounts reported in the SEFA and Summary Schedule of Prior Audit Findings result in improper federal reporting.

Recommendation:**We recommend:**

- **Finance, DWS, and USBE develop written procedures for the SEFA preparation and establish internal controls to ensure the accuracy of the information provided to the Division of Finance;**
- **Finance develop written procedures and establish internal controls to ensure the proper reporting of findings in the Summary Schedule of Prior Audit Findings.**

Entity's Response:

We agree with the findings and recommendations outlined in your Management Letter.

Corrective Action Plan:

During fiscal year 2020, the Division re-evaluated the process of the compilation of the State's SEFA and determined that individual departments, rather than the Division, were better positioned to report complete and accurate SEFA information in compliance with each individual federal grant. This change in philosophy in combination with turnover in a key role over federal reporting in the Division, resulted in these errors. The Division will provide additional training to the departments and Division personnel as well as increased communication throughout the SEFA compilation process to ensure accurate and complete reporting. Additional monitoring and analytical procedures will also be added to the Division's SEFA compilation process to further address the weaknesses identified. Finally, the Division will continue to develop comprehensive written procedures for SEFA preparation.

Contact Person: Patricia Nelson, Assistant State Comptroller, State Division of Finance, patriciarnelson@utah.gov

Anticipated Correction Date: June 30, 2021

Auditor's Note:

See Report No. 20-34 and Report No. 20-39 for DWS and USBE responses, respectively.

4. WORKING CAPITAL RESERVES IN EXCESS OF FEDERAL GUIDELINESFederal Agencies: **Various**CFDA Numbers and Titles: **Various**Federal Award Numbers: **Various**Questioned Costs: **Undeterminable**

Pass-through Entity: N/A

Prior Year Single Audit Report Finding Numbers: **2019-023; 2018-033; 2017-021; 2016-037; 2015-048; 2014-040; 2013-049; 2012 12-51; 2011 11-56**

As of June 30, 2020, two funds within the Department of Administrative Services held working capital reserves in excess of federal guidelines as follows:

<u>Fund Description</u>	<u>Excess # of Days in Reserve</u>	<u>Excess Amount in Reserve</u>
Division of Purchasing and General Services		
Cooperative Contract Management	180	\$ 1,767,683
Print Services	6	\$ 22,303
State Surplus Property	179	\$ 336,372
Division of Risk Management		
Workers' Compensation Fund	35	\$ 683,186
Property Liability Self-Insurance Fund	162	\$ 7,295,104

2 CFR part 200, Appendix V, paragraph G.2, generally allows a working capital reserve as part of retained earnings of up to 60 days cash expenses for normal operating purposes in each internal service fund. The excess reserves were due to the inherent difficulty of accurately estimating expenses when setting rates. Excess reserves could result in a federal liability since federal programs share an interest in the reserves.

Recommendation:

Depending on the business requirements, we recommend that the Department of Administrative Services reduce excess working capital reserves within each of the respective funds, or obtain a waiver from the federal cost negotiator allowing for an increase in the number of days of working capital allowed to comply with federal guidelines.

Entity's Response:

Annually, the Department of Administrative Services (Department) analyzes reserves and estimated costs to determine a rate that reduces and minimizes excess reserves. However, these

rates are determined and legislatively approved months in advance of the rate being applied and cannot be changed until the next annual rate setting cycle. Due to these timing differences, rates applied may not reflect new and unforeseen circumstances, resulting in excess or insufficient reserves. The Department makes every effort to adjust future rates to reflect changing circumstances and to minimize potential excess reserves.

Corrective Action Plan:

Division of Purchasing and General Services

Cooperative Contract Management – Public entities in Utah rely on the Division of Purchasing (State Purchasing) to maintain the cooperative contract program to help with public procurement in Utah. The usage of state cooperative contracts by public entities increased each year over the past seven years resulting in a corresponding increase in the collection of administrative fees. However, State Purchasing continues to decrease the administrative fees on state cooperative contracts as each contract expires and is rebid. This is a slow process since State Purchasing has nearly 1,100 cooperative contracts that expire only every five years and are then rebid. Although State Purchasing is allowed under law to collect up to a 1.0 % administrative fee on each cooperative contract, currently, the average administrative fee is 0.38 %. As a result, while spending on cooperative contracts increased 28% from fiscal year 2018 through fiscal year 2020, administrative fees increased only 22% during that same period.

In addition, State Purchasing hired two additional employees and invested in a new contract usage system and analytics tool to improve management of cooperative contracts. The system will also assist in anticipating usage and decreasing the administrative fees of appropriate contracts.

Print Services – Print Services reviewed and decreased administrative fees. This resulted in a net operating loss for fiscal year 2020. Additionally, as a result of the COVID-19 pandemic, reserve funds were utilized to remain operational. While this combination was not sufficient to reduce the excess reserves to established guidelines, Print Services is expecting a continued use of portions of reserves in fiscal year 2021 due to the pandemic as more employees telework, reducing the use of copiers.

State Surplus Property – State Surplus Property anticipates relocating in fiscal year 2021 at the completion of the Utah State Prison relocation. At that time, State Surplus will use excess reserve funds to relocate and furnish the new location.

Contact Person: Christopher Hughes, Director of Purchasing & General Services,
christopherhughes@utah.gov

Anticipated Completion Date: Cooperative Contract Management – June 30, 2023; Print Services – June 30, 2021; State Surplus Property – June 30, 2022

Division of Risk Management

Workers' Compensation Fund – This fund experienced a \$1 million increase in premiums paid to the Workers Compensation Fund of Utah (separate entity) during fiscal year 2021 due to the COVID-19 pandemic, without a compensating increase in rates charged (funding received) for

the current year. This increase in costs is expected to reduce and/or eliminate the excess reserve balance.

Property Liability Self- Insurance Fund – During fiscal year 2021, this fund experienced an unexpected \$5.96 million increase in excess premiums paid and anticipates an operating loss for the year, reducing excess fund balances. Risk Management will continue to observe claim levels and set future rates to reduce excess balances to appropriate levels.

*Contact Person: Brian Nelson, Director, Division of Risk Management, benelson@utah.gov
Anticipated Correction Date: June 30, 2021*