



STATE OF WISCONSIN  
Legislative Audit Bureau

22 East Mifflin Street, Suite 500  
Madison, Wisconsin 53703  
(608) 266-2818  
Fax (608) 267-0410  
[www.legis.wisconsin.gov/lab](http://www.legis.wisconsin.gov/lab)

Janice Mueller  
State Auditor

February 2, 2010

Mr. Michael L. Morgan, Secretary  
Department of Administration  
101 East Wilson Street, 10<sup>th</sup> Floor  
Madison, Wisconsin 53702

Mr. Stephen Censky, State Controller  
Department of Administration  
101 East Wilson Street, 5<sup>th</sup> Floor  
Madison, Wisconsin 53702

Dear Mr. Morgan and Mr. Censky:

We have completed a financial audit of the State of Wisconsin as of and for the fiscal year ended June 30, 2009. The financial statements and related opinion are included in the State of Wisconsin's Comprehensive Annual Financial Report, which is published by the Department of Administration.

During the course of our audit, we identified a variety of internal control concerns at various state agencies that are required to be reported under *Government Auditing Standards*. As provided for in those standards, we are furnishing you with the Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters. The state agencies' responses to our concerns and recommendations are summarized in the text of the report so that readers may see the State's intended resolution of the matters discussed. In future audits, we will determine the extent to which findings in the report have been resolved.

We appreciate the courtesy and cooperation extended to us by the Department of Administration and other state agencies during the audit.

Sincerely,

Janice Mueller  
State Auditor

JM/BN/ss



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**INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER  
FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS  
BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN  
ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS**

We have audited the financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the State of Wisconsin as of and for the year ended June 30, 2009, and have issued our report thereon dated December 11, 2009. The basic financial statements and related auditor's opinions have been included in the State of Wisconsin's Comprehensive Annual Financial Report for fiscal year 2008-09. Our report includes a reference to other auditors.

We conducted our 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. Other auditors audited the financial statements of the Wisconsin Department of Transportation Revenue Bond Program and Commercial Paper Program; the Badger Tobacco Asset Securitization Corporation; the Environmental Improvement Fund; the College Savings Program Trust; the Wisconsin Housing and Economic Development Authority; the University of Wisconsin Hospitals and Clinics Authority; and the University of Wisconsin Foundation as described in our opinion on the State of Wisconsin's financial statements. The financial statements of the Wisconsin Department of Transportation Revenue Bond Program and Commercial Paper Program, the College Savings Program Trust, and the Wisconsin Housing and Economic Development Authority were audited in accordance with auditing standards generally accepted in the United States of America and *Government Auditing Standards*. The financial statements of the other entities audited by other auditors were audited in accordance with auditing standards generally accepted in the United States of America, but not in accordance with *Government Auditing Standards*. This report does not include the results of the other auditors' testing of internal control over financial reporting or compliance and other matters that may have been reported on separately by those auditors.

**Internal Control over Financial Reporting**

In planning and performing our audit, we considered the State's internal control over financial reporting (internal control) as a basis for designing our auditing procedures for the purpose of expressing our opinion on the State's basic 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 State's financial statements will not be prevented or will not be detected and corrected on a timely basis.

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 deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control that we consider to be material weaknesses as defined above. However, we consider the deficiencies described in the accompanying schedule of findings and responses to be significant deficiencies. 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.

### **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the State of Wisconsin's basic financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

The State's responses to findings identified during our audit are summarized in the accompanying schedule of findings and responses. We did not audit the responses and, accordingly, express no opinion on them.

We noted certain additional matters, which we will report or have already reported to the management of certain state agencies in separate communications.

This independent auditor's report is intended for the information and use of the management of the State of Wisconsin, the Wisconsin Legislature, federal awarding agencies, and pass-through entities. This report is a matter of public record and its distribution is not limited. However, because we do not express an opinion on the effectiveness of the State's internal control or on compliance, this report is not intended to be used by anyone other than these specified parties.

LEGISLATIVE AUDIT BUREAU

December 11, 2009

by



Bryan Naab  
Deputy State Auditor for Financial Audit

## SCHEDULE OF FINDINGS AND RESPONSES

This schedule includes all significant deficiencies related to internal control over financial reporting that are required to be reported by auditing standards generally accepted in the United States of America and *Government Auditing Standards*. Repeat findings from the prior year are indicated with an asterisk (\*).

### **Finding: Internal Control Weaknesses in Financial Reporting by State Agencies**

#### *Criteria:*

The Department of Administration's State Controller's Office (SCO) is responsible for preparing and maintaining the Uniform GAAP Conversion Policies and Procedures Manual, which includes the State's policies and procedures used to prepare financial statements in accordance with generally accepted accounting principles (GAAP). The management of each state agency and the University of Wisconsin (UW) System is responsible for maintaining effective internal controls to ensure the Uniform GAAP Conversion Policies and Procedures Manual is followed, that the information provided to SCO for inclusion in the State's financial statements is fairly presented in accordance with GAAP, and that misstatements are prevented or detected in a timely manner. SCO is responsible for performing limited reviews of the reasonableness of information submitted by other state agencies and UW System. In addition, SCO is responsible for developing certain information that is incorporated into the financial statements.

#### *Condition:*

In some instances, state agencies, including SCO and UW System, do not have sufficient procedures and controls in place to properly report financial statement balances in compliance with the Uniform GAAP Conversion Policies and Procedures Manual. In other instances, staff and management did not fully consider how to most appropriately report the information, or agencies did not appropriately review financial information for significant errors prior to submitting the information for inclusion in the State's financial statements.

#### *Questioned Costs:*

None

#### *Context:*

The State's financial statements present financial activity for the State as a whole, in accordance with GAAP. Financial reporting for the State is complex, with many technical accounting issues.

#### *Effect and Cause:*

Some agencies did not prevent or detect and correct in a timely manner misstatements in the financial information included in the State's financial statements. Agencies generally agreed to make corrections after the auditors brought the errors to their attention. Although adjustments were generally made to the financial statements, there remains a risk of potentially significant errors in the financial statements. Examples of significant errors or potential errors identified by auditors, and the causes of these errors, are presented in the following table:

<b>Agency</b>	<b>Fund</b>	<b>Misstatement<sup>1</sup></b>	<b>Cause</b>
<b><i>Department of Revenue*</i></b>	<b><i>General Fund and Government-wide Governmental Activities</i></b>	On the Statement of Revenues, Expenditures, and Changes in Fund Balance, the Tax Relief and Other General Expenditures account was understated by \$53.0 million, and Tax Revenues was overstated by \$8.5 million. On the Balance Sheet, Due to Other Governments was understated by \$53.0 million, Tax Refunds Payable was understated by \$8.5 million, Taxes Receivable was understated by \$22.5 million, and Deferred Revenue was understated by \$22.5 million. In addition, a prior-period adjustment was necessary because the Net Assets–Beginning balance on the Statement of Activities was overstated by \$98.1 million.	Department of Revenue staff have not fully documented year-end procedures, and supervisory review was not sufficient to detect these errors.
<b><i>Department of Children and Families</i></b>	<b><i>General Fund</i></b>	On the Statement of Revenues, Expenditures, and Changes in Fund Balance, the Intergovernmental Revenues account was understated by \$18.0 million and the Human Relations and Resources Expenditures account was understated by \$5.4 million. On the Balance Sheet, Due from Other Governments was understated by \$18.0 million, Due to Other Governments was understated by \$4.7 million, Accounts Payable and Other Accrued Liabilities was understated by \$0.7 million, Fund Balance–Unreserved was overstated by \$6.2 million, and Fund Balance–Reserved for Encumbrances was understated by \$6.2 million.	Department of Children and Families staff are new to the financial reporting process and did not sufficiently plan for and take care in the preparation of the financial information submitted to SCO.
<b><i>University of Wisconsin System</i></b>	<b><i>UW System</i></b>	Potential misclassification of revenue between the Federal Grants and Contracts account and the Local and Private Grants and Contracts account.	UW-Madison did not reconcile revenue-clearing accounts to ensure federal, local, and private grants and contracts were recorded and reported in the appropriate accounts.
<b><i>Department of Administration, State Controller’s Office</i></b>	<b><i>General Fund and Government-wide Governmental Activities</i></b>	On the Statement of Revenues, Expenditures, and Changes in Fund Balance, the Tobacco Settlement Revenues account was overstated by \$71.6 million. On the Balance Sheet, the Other Receivables account was overstated by \$71.6 million. In addition, on the Statement of Net Assets, Interest Payable was understated by \$19.8 million and on the Statement of Activities, Interest on Debt was understated by \$19.8 million.	SCO’s procedures to develop and report financial information related to the accrual of tobacco settlement revenues and receivables and the accrual for interest payable on bonds were not sufficient to prevent or detect and correct these errors.

<sup>1</sup> The misstatements generally affect the State’s fund-level financial statements. These misstatements may also affect the government-wide financial statements.

*Recommendation:*

We recommend the identified agencies improve their internal controls, including those over the financial reporting process.

*Management's Response:*

Agency management agreed to implement improvements.

**Finding: Programmer Access to the State's Central Accounting System and Central Payroll System Data and Programs\***

*Criteria:*

To provide proper internal control, computer programmers ideally should not have the ability to access or update production data and programs. If this is not possible, proper oversight, review, and documentation should be provided to minimize risk of unauthorized changes to computer programs and data.

*Condition:*

Programmers for the State's central accounting systems and central payroll systems have access to production data and programs, which could allow them to make unauthorized or inadvertent changes to the data. The Department of Administration began projects that, if completed, may mitigate risks in some areas. For example, in fiscal year (FY) 2007-08, the Department started a project to limit programmers' ability to directly access several accounting and payroll-related datasets. Changes to those datasets are now made through the use of a new log-on identification, for which access is logged. However, the Department of Administration has not established sufficient monitoring procedures to ensure that all logged changes to datasets are reasonable. Further, the Department continues to allow programmers to directly access other accounting and payroll-related datasets. Finally, some programmers continue to have the ability to modify the production programs, which could allow them to change the programs or output in order to avoid detection of unauthorized changes. Although the Department has taken limited steps to improve controls, accounting and payroll-related data remained at risk during FY 2008-09.

*Questioned Costs:*

None

*Context:*

The State's central accounting system maintains the State's official accounting records. The system processes financial data for all state agencies and is the main source of information for financial schedules and statements, including the State of Wisconsin's financial statements. The State's central payroll systems process the biweekly payroll for most state employees. Both of these systems generate checks.

*Effect:*

Programmers with access to and extensive knowledge of the computer programs in the systems could make unauthorized changes to data and conceal those changes. This risk is increased because some of these programmers also have access to the production programs for these systems.

*Cause:*

As of the end of FY 2008-09, the Department of Administration has not fully implemented compensating controls in this area. The Department notes that it believes it would be difficult for a programmer to conceal inappropriate transactions without detection.

*Recommendation:*

We recommend the Department of Administration continue to implement compensating controls related to computer programmer access to data and programs to reduce the risk of unauthorized transactions.

*Management's Response:*

The Department of Administration's State Controller's Office agrees with the recommendation and will continue to work with the Department's Division of Enterprise Technology to implement compensating controls over programmer access to data and programs.

**Finding: Programmer Access to Critical Production Programs and Data at the Department of Transportation\***

*Criteria:*

To provide proper internal control, computer programmers should not have the ability to access or update production data and programs.

*Condition:*

Computer programmers at the Department of Transportation have access to programs in production, and some are allowed to move programs from the test environment to production. In addition, some computer programmers have access to production data through access to the Control-M job scheduling program.

*Questioned Costs:*

None

*Context:*

The Department of Transportation maintains accounting and other systems critical to agency operations. These systems enable the Department to collect and expend \$2.3 billion annually, to issue driver's licenses and vehicle titles and registrations, to track drivers' records and traffic violations, and to oversee the State's construction of roads and bridges.

*Effect:*

Programmers with extensive knowledge of the computer programs and datasets could make unauthorized changes to the programs or data and conceal those changes, resulting in undetected erroneous or fraudulent changes.

*Cause:*

The Department of Transportation believes it can more efficiently complete program changes and job scheduling by allowing programmers access to the production environment and to Control-M. To manage production system security, it uses a combination of Changeman staging

controls, user verification procedures, periodic access reviews, and supervisory oversight. The Department of Transportation believes these factors somewhat mitigate the risk of programmers having access to production data and programs, and has decided to accept any remaining risk.

*Recommendation:*

In prior audits, we have expressed our concerns regarding programmers' ability to access or update production data and programs and have recommended removal of programmers' access to critical production programs and to the Control-M job scheduling program. We continue to believe programmers should not have access to production data and programs. The Department of Transportation is aware of our concerns but accepts the risks in this area.

**Finding: Mainframe Computer Program Change Controls at the University of Wisconsin\***

*Criteria:*

To provide proper internal control, procedures should be established to prevent computer programs from being altered and/or put into production without proper oversight, review, and documentation.

*Condition:*

The program change process for UW System's critical financial systems operating on the mainframe computer does not include an independent review of program changes to assess the reasonableness of the changes or compliance with users' requests. Further, programmers have the ability to move programs into production. Thus, even if such reviews were performed, programmers could circumvent these procedures and make changes without oversight, review, or documentation.

*Questioned Costs:*

None

*Context:*

UW-Madison maintains critical financial systems on the mainframe computer, including the UW-Madison legacy accounting system and the UW System legacy payroll systems.

*Effect:*

Programmers with extensive knowledge of the legacy accounting and payroll systems' computer programs could make unauthorized changes to the programs and conceal those changes, resulting in undetected erroneous or fraudulent information.

*Cause:*

Controls were not originally developed to ensure proper oversight before programs are moved to production. For the legacy payroll system, UW staff are reviewing procedures and planning to make changes to the program change control process; however, this project is not yet complete. Further, UW System is planning to replace its legacy payroll systems over the next several years and, therefore, extensive changes to the program change process may not be a priority. The legacy accounting system has been phased out and was no longer being used as of the end of FY 2008-09.

*Recommendation:*

We recommend UW System ensure a well-controlled program change process is established when its new payroll system is implemented, and continue the project to improve the program change process for its legacy payroll systems.

*Management's Response:*

Management of UW System and UW-Madison acknowledges that there continues to be a risk that unauthorized or erroneous changes could be made to the legacy payroll processes on the mainframe computer. The UW-Madison payroll service center will commence program change control discussions with UW-Madison's Division of Information Technology to determine the feasibility of implementing the same program change control process established for the Shared Financial System. Given the plans to replace the legacy payroll system within the next two years, and potential costs to implement program change control procedures, management of UW System and UW-Madison believes the level of risk to be low and of limited duration. Thus, while potential program change controls procedures are being examined, management accepts this risk.

**Finding: Lack of Adequate Oversight of the Financial Reporting Process at the Department of Employee Trust Funds\***

*Criteria:*

Department of Employee Trust Funds management is responsible for ensuring that it accurately compiles and fairly presents financial information for benefit programs it administers that are included in the State's financial statements. In addition, Department management is responsible for providing sufficient oversight over the compilation process to ensure that misstatements are prevented or detected in a timely manner.

*Condition:*

A prior-period adjustment was necessary to accurately present the Active and Retiree Health Insurance programs in compliance with Governmental Accounting Standards Board (GASB) Statement 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*. While GASB Statement 43 was first implemented for the State's FY 2006-07 financial statements, adjustments to certain accounts were necessary to correctly reflect the division of assets among the Active Health Insurance and Retiree Health Insurance plans as of June 30, 2008. The prior-period adjustment included a \$22.5 million increase to the Active Health Insurance plan's beginning fund equity and decreases of \$20.3 million and \$2.2 million to the beginning net assets of the State Retiree Health and Local Retiree Health Insurance plans, respectively.

*Questioned Costs:*

None

*Context:*

The Department of Employee Trust Funds is responsible for compiling financial information for a number of the State's fiduciary funds, enterprise funds, and other fund types presented in the State's financial statements. In addition, the Department is responsible for providing information for the State's note disclosures, including the State's pension plan, public-entity risk pools, and other postemployment benefit plans.

*Effect:*

The Active Health Insurance and Retiree Health Insurance plans were not fairly presented in the State's FY 2007-08 financial statements.

*Cause:*

The Department of Employee Trust Funds received inaccurate data from a third-party administrator of the Health Insurance program, and it did not fully review the data to ensure accuracy.

*Recommendation:*

We recommend the Department of Employee Trust Funds continue to take steps to improve the attention and oversight given to its financial reporting process, including reconciling key balances between the financial statements, notes, and required supplemental information, and increasing the overall level of care applied to completing its financial information.

*Management's Response:*

The Department of Employee Trust Funds has initiated efforts to improve the oversight over the preparation of financial statements. These efforts include, but are not limited to, the addition of one full-time accountant position, increasing a part-time position to full-time, and having the Department's internal audit staff perform a preliminary review. The Department believes substantial progress has been made. Finally, it should be noted that the Department identified and reported the error that resulted in the prior-period adjustment. This suggests that Department efforts to improve oversight are having a positive effect.

**Finding: Business Resumption Planning\***

*Criteria:*

To minimize disruption that may occur in an emergency, Wisconsin state government should have effective business resumption plans in place.

*Condition:*

The Department of Administration is coordinating a project to develop a statewide business resumption plan. However, although state agencies have made progress, some do not have complete and tested business resumption plans and, therefore, a statewide plan is not available.

*Questioned Costs:*

None

*Context:*

The State provides a variety of critical services to citizens, local governments, and others in the State.

*Effect:*

Without effective business resumption plans in place, an emergency could disrupt the State's ability to provide critical services; process the related accounting transactions, including delaying payments to vendors, citizens, and other governmental entities; and prepare financial statements in an accurate and timely manner.

*Cause:*

Development of a comprehensive plan is a large project requiring significant resources. Because of budget restrictions and the limited availability of staff, the State has not been able to devote sufficient ongoing resources to complete development and testing in the short term. However, it does continue to work toward a comprehensive plan.

*Recommendation:*

We recommend the State continue to move forward to complete and test its business resumption plan.

*Management's Response:*

Wisconsin's Continuity of Government project, led by the Department of Administration, has continued to make substantial progress in developing and testing Continuity of Operations (COOP) plans for state agencies with time-sensitive business services.

Since October 20, 2008, a major focus has been on pandemic continuity planning and since April 2009, on actual response planning for the H1N1 pandemic. Fifty-five agencies, campuses, and the UW-Extension have completed pandemic COOP plans. Pandemic COOP-focused "Badger Flu" exercises have been conducted at 24 agencies to date. The Badger Flu exercises were developed, organized, and conducted by Department of Administration Continuity of Government personnel. In addition, two agencies have conducted agency-developed pandemic COOP exercises. While pandemic preparedness has some unique aspects, the core of pandemic planning is ensuring the availability of critical employees, planning for backups when the primary people are not available, and communications. These are also key components of all COOP planning. The experience and knowledge gained by agency participants in these exercises supports overall continuity preparedness.

While the major focus has been on pandemic preparedness, additional COOP plans have been completed in six agencies (two state agencies, three UW System campuses, and the UW-Extension) and the total completed service plans now stands at 286, an increase of 34 from this time in 2008.

In addition to the pandemic COOP exercises, seven agency command center COOP exercises and 37 service COOP exercises were conducted since October 20, 2008. Two of those agencies, the Department of Health Services and UW-Madison, conducted full-scale exercises.

In the October 2008 to October 2009 period, almost as many agency exercises have been successfully conducted as were conducted in the entire 2006 to October 2008 period.

Continuity preparedness also requires multi-agency coordination and communication. Since October 2008, the Department of Administration Continuity of Government personnel have organized and conducted multi-agency, statewide pandemic COOP communication drills on December 18, 2008, and June 4, 2009.

Additionally, the Department of Administration Continuity of Government personnel participated in and organized the COOP component of the June 12, 2009 "Red Badger" exercise. The Red Badger State Emergency Operations Center (EOC) exercise simulated a dirty bomb

explosion in Milwaukee and subsequent radiological contamination. A follow-on exercise involved actual deployment of National Guard and active duty military units to provide decontamination support to local governments and hospitals. The COOP portion of the exercise involved testing communications and coordination between the State COOP representative in the State EOC, the State Continuity Coordination Center (SCCC) personnel operating from the Department of Administration building, three agency COOP incident commanders (UW System, Department of Children and Families, and Department of Workforce Development) operating from their respective agency headquarters in Madison, and actual and simulated officials at agency offices in the Milwaukee metropolitan area. This was the first State EOC exercise with active State COOP involvement as the exercise scenario presented a potential challenge to the continued operations of state agency offices in the Milwaukee metropolitan area. The COOP official in the State EOC successfully provided and received information from the SCCC personnel and participating agency incident commanders and, in turn, the three agencies' incident commanders successfully provided and received information from their agency's offices in Milwaukee County. This was an important step in perfecting coordination and communication for such an event.

The Department of Administration appreciates that the auditors' review of the preparedness program recognizes that budget restrictions and staff availability do affect how much can be accomplished in the short term. The Department believes that it has demonstrated that very considerable progress has been made in the last twelve months and the Department will continue to move forward to complete planning within the UW System and to strengthen, improve, and test all COOP plans on an annual basis.

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