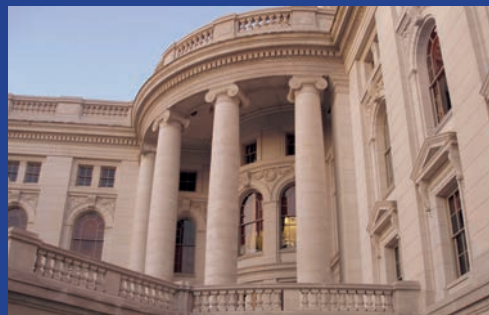
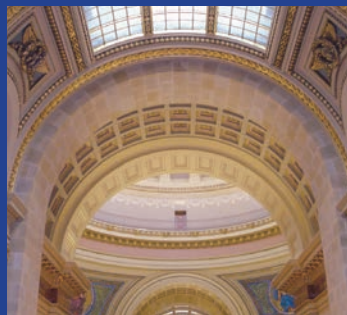


**Report 17-4
March 2017**

State of Wisconsin

Fiscal Year 2015-16 Financial Statements

STATE OF WISCONSIN



Legislative Audit Bureau ■

State of Wisconsin

Fiscal Year 2015-16 Financial Statements

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Contact the Bureau at 22 East Mifflin Street, Suite 500, Madison, Wisconsin 53703;
AskLAB@legis.wisconsin.gov; or (608) 266-2818.

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Independent Auditor's Report on Internal Control over
Financial Reporting and on Compliance and Other Matters

OPINIONS PUBLISHED SEPARATELY

The financial statements and our opinions on them are included in the
State of Wisconsin's Comprehensive Annual Financial Report (CAFR)
for the fiscal year ended June 30, 2016



STATE OF WISCONSIN | Legislative Audit Bureau

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Joe Chrisman
State Auditor

March 31, 2017

Senator Robert Cowles and
Representative Samantha Kerkman, Co-chairpersons
Joint Legislative Audit Committee
State Capitol
Madison, Wisconsin 53702

Dear Senator Cowles and Representative Kerkman:

We have completed our financial audit of the State of Wisconsin as of and for the fiscal year (FY) ended June 30, 2016, and issued unmodified opinions dated March 30, 2017 on the State's financial statements. These financial statements were prepared by the Department of Administration (DOA) in accordance with generally accepted accounting principles (GAAP) and are included in the State's FY 2015-16 Comprehensive Annual Financial Report (CAFR), which may be found on DOA's website.

The CAFR is typically published by DOA each December. However, in October 2016 DOA indicated the FY 2015-16 CAFR would be published in early 2017. On December 30, 2016, the DOA Secretary issued a memorandum to the members of the Joint Legislative Audit Committee, the Joint Committee on Finance, and the Joint Committee on Information Policy and Technology. This memorandum offered an update on the implementation of the State's new enterprise resource planning (ERP) system called STAR and stated, "As with any new system or process, the first year end close requires additional time for training, development of new procedures, and system adjustments." Similarly, new audit work associated with these new procedures and system adjustments in STAR affected the audit timeline. Although we audited information presented in the financial statements derived from STAR that was sufficient to provide our audit opinions, we did not perform an audit of the implementation of STAR.

The CAFR helps to describe the State's fiscal condition and contains information on over 90 funds. In the remainder of this letter, we discuss the financial condition of the General Fund and Transportation Fund, which are the State's two largest governmental funds; the amount of the State's long-term debt; the State's net pension liability; describe our findings related to internal controls over financial reporting; and report two matters of statutory noncompliance.

General Fund

As reported on a GAAP basis, the General Fund deficit remained at \$1.7 billion as of June 30, 2016, as shown on page 44 of the CAFR. In its Management's Discussion and Analysis (MD&A) on page 29, DOA noted that total General Fund revenue, which was derived from taxes and federal revenues, increased by \$405.8 million and totaled \$24.9 billion for FY 2015-16. Total General Fund expenditures and transfers increased by \$183.3 million primarily due to increases in Medical Assistance costs and school aids payments, and totaled \$23.3 billion for FY 2015-16.

Transportation Fund and Transportation Expenditures

On a GAAP basis, the balance of the Transportation Fund decreased from \$777.5 million as of June 30, 2015, to \$717.3 million as of June 30, 2016, as shown on page 44 of the CAFR. The majority of the Transportation Fund's balance (96.1 percent) was "restricted" on the Balance Sheet due to the November 2014 constitutional amendment related to uses of the Transportation Fund. DOA indicated in its MD&A on page 31 that 2013 Wisconsin Act 20 authorized a one-time transfer in FY 2014-15 of \$133.3 million from the General Fund to the Transportation Fund. Total transportation-related expenditures decreased by \$11.6 million to \$2.6 billion in FY 2015-16. The expenditures reported in the Transportation Fund were funded largely by motor fuel taxes, registration fees, and federal revenues. Transportation revenue bonds and general obligation bonds, which are reported in separate funds, funded the remaining \$227.0 million in transportation-related expenditures.

Long-term Debt

The State's long-term debt increased from \$13.6 billion as of June 30, 2015, to \$13.7 billion as of June 30, 2016, as shown in the MD&A on page 34. The amount of outstanding annual appropriation bonds decreased and the amount of outstanding revenue bonds increased. During FY 2015-16, \$1.2 billion in new general obligation bonds and notes were issued.

Net Pension Liability

The Wisconsin Retirement System (WRS) reported a net pension liability of \$1.6 billion, as we discussed in report 16-10. The State's proportionate share of the WRS net pension liability reported on June 30, 2016, was \$455.5 million. This decrease of \$1.1 billion from the \$686.9 million net pension asset reported for FY 2014-15 is generally related to the decline in investment performance for WRS assets in 2015. The net pension liability for the State is reported in the noncurrent portion of long-term liabilities on the Statement of Net Position, as shown in the CAFR on page 39. Additional information on the net pension liability is presented in the CAFR in Note 14 on page 124.

Findings Related to Internal Control over Financial Reporting

We identified internal control weaknesses during our audit that are required to be reported under *Government Auditing Standards*. Specifically, we identified one material weakness and six significant deficiencies in internal control. The Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters, which begins on page 7, discusses each concern and includes the response from management of the responsible agency.

We identified weaknesses in information technology (IT) security policies and procedures related to security that resulted in weaknesses in the administration of the State's new enterprise resource planning system called STAR, which was implemented by DOA (Finding 2016-001). We also identified weaknesses in security standards and procedures, as well as in current IT practices and settings, for IT controls at DOA (Finding 2016-002) and we continued to identify

weaknesses in IT security policies, procedures, and controls at several University of Wisconsin (UW) institutions (Finding 2016-003). We considered Finding 2016-001 to be a material weakness in internal control, and Findings 2016-002 and 2016-003 to be significant deficiencies in internal control. We include recommendations for DOA and UW System to address these concerns.

In addition, we found DOA's State Controller's Office (SCO) had not performed or documented complete monthly reconciliations that included all components and reconciling items of the cash balance on the accounting records to the bank records, nor had it prepared a monthly bank reconciliation statement since implementation of STAR in October 2015 (Finding 2016-004). We discussed this finding in report 16-10 and in a letter to the Joint Legislative Audit Committee in December 2016. We considered this finding to be a significant deficiency in internal control and made recommendations to DOA to address this concern.

Other significant deficiencies in internal control include financial reporting concerns for the Capital Improvement Fund (Finding 2016-005), the allocation of expenditures to the incorrect fiscal year at the Department of Transportation (Finding 2016-006), and the financial reporting process at the Office of the Commissioner of Insurance (OCI) for the Injured Patients and Families Compensation Fund (Finding 2016-007).

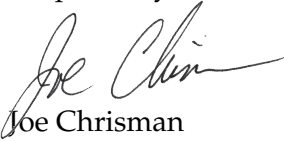
Statutory Noncompliance Matters

We identified two matters of statutory noncompliance that are not material to the CAFR, but relate, in part, to the State's implementation of STAR in October 2015. First, we found that the Department of Health Services (DHS) exceeded available general purpose revenue (GPR) spending authority in FY 2015-16 within eight appropriations totaling \$6.8 million. At the time SCO closed STAR for FY 2015-16, DHS had not yet completed its reconciliation for these appropriations. To address this matter, DHS plans to lapse \$6.8 million in FY 2016-17 GPR spending authority. DOA indicated that adjustments were made to reflect the expenditures in the *2016 Annual Fiscal Report*.

Second, DOA is statutorily required to report at least monthly on receipts and disbursements by statutory fund. We found DOA did not prepare this monthly report from October 2015 through June 2016. DOA prepared the reports going back to October 2015 and published them after the end of FY 2015-16.

We appreciate the courtesy and cooperation extended to us by DOA and other state agencies during the audit. During the FY 2016-17 audit, we will follow up on the progress in implementing our recommendations.

Respectfully submitted,


Joe Chrisman
State Auditor

JC/CS/ss

Auditor's Report ■



Report 17-4

Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters

Honorable Members of the Legislature

The Honorable Scott Walker, Governor

We have audited the financial statements and the related notes 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, which collectively comprise the State's basic financial statements, as of and for the year ended June 30, 2016, and have issued our report thereon dated March 30, 2017.

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*, which is issued by the Comptroller General of the United States. The basic financial statements and related auditor's opinions have been included in the State of Wisconsin's Comprehensive Annual Financial Report (CAFR) for the fiscal year ended June 30, 2016.

Our report includes a reference to other auditors who audited the financial statements of 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 report on the State of Wisconsin's basic financial statements. The financial statements of the Environmental Improvement Fund, the College Savings Program Trust, the Wisconsin Housing and Economic Development Authority, and the University of Wisconsin Hospitals and Clinics Authority were audited in accordance with auditing standards generally accepted in the United States of America and *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 were reported on separately by those auditors. Although the financial statements of the University of Wisconsin Foundation were audited in accordance with auditing standards generally accepted in the United States of America, they were not audited in accordance with *Government Auditing Standards* and, accordingly, this report does not include reporting on internal control over financial reporting or instances of reportable noncompliance associated with the University of Wisconsin Foundation.

Internal Control over Financial Reporting

Management of the State of Wisconsin is responsible for establishing and maintaining effective internal control over financial reporting (internal control). In planning and performing our audit of the financial statements, we considered the State's internal control to determine the

audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the 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 misstatements, or to detect and correct misstatements on a timely basis. A *material weakness* is a deficiency or a combination of deficiencies in internal control such that there is a reasonable possibility that a material misstatement of the State's basic financial statements will not be prevented, or that a material misstatement will not be 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 over financial reporting that might be material weaknesses or significant deficiencies and, therefore, material weaknesses or significant deficiencies may exist that were not identified. However, we identified certain deficiencies in internal control that we consider to be material weaknesses or significant deficiencies.

We consider the deficiency in internal control, described in the accompanying Findings and Responses Schedule as Finding 2016-001, to be a material weakness. We consider the deficiencies in internal control, described in the accompanying Findings and Responses Schedule as Findings 2016-002, 2016-003, 2016-004, 2016-005, 2016-006, and 2016-007, to be significant deficiencies. Because the University of Wisconsin (UW) System's financial activity is also reported separately from the State's CAFR, Finding 2016-003 will also be included in the Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters for UW System's financial statements.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the State's basic financial statements are free from material misstatement, we performed tests of 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*.

We noted an additional matter related to financial reporting errors that did not rise to the level of a significant deficiency. This matter is discussed on page 24 of the accompanying Findings and Responses Schedule.

Responses to Findings

Agency-specific responses, including corrective action plans, to the findings identified in our audit are described in the accompanying Findings and Responses Schedule. The responses were not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on them.

Purpose of This Report

This report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be used when considering the State's internal control and compliance. 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. Accordingly, this report is not suitable for any other purpose.

LEGISLATIVE AUDIT BUREAU



Joe Chrisman
State Auditor

March 30, 2017

FINDINGS AND RESPONSES SCHEDULE

This schedule includes one material weakness and six 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*. One additional matter related to financial reporting follows these findings. Findings 2015-001, 2015-003 and 2015-004 from the prior year (report 16-2) were resolved.

Finding 2016-001: STAR Security Concerns

Criteria:

Section 16.97, Wis. Stats., specifies the Department of Administration's (DOA) responsibilities for the State's information technology (IT) services. One important IT service provided by DOA is the development and maintenance of the accounting and payroll computer systems for the State of Wisconsin. To modernize, consolidate, and improve accounting and payroll processes, DOA implemented a new enterprise resource planning (ERP) system called STAR. The implementation included three releases between October 1, 2015, and July 1, 2016.

Executive Order 99, which was issued on April 26, 2013, created the Information Technology Executive Steering Committee (ITESC). ITESC consists of the State of Wisconsin Chief Information Officer and the deputy secretaries of the departments of Administration, Children and Families, Corrections, Health Services, Natural Resources, Revenue, Transportation, Workforce Development, and Agriculture, Trade and Consumer Protection. One of ITESC's goals is to "create and maintain" statewide IT policies. ITESC's responsibility for major decisions with STAR included:

- policy decisions, such as the decision to consolidate vendor payments; and
- implementation decisions, such as the decision to approve or deny each requested customization of STAR.

To provide proper internal control, IT security policies and procedures are necessary to ensure data stored and processed in STAR are protected from accidental or intentional misuse or destruction. IT controls should be established to prevent inappropriate or inadvertent access to STAR and its related databases, and to provide staff with a consistent methodology for performing their job functions. Finally, the National Institute of Standards and Technology's *Special Publication 800-53r4* discusses the importance of creating policies and procedures, ensuring proper separation of duties, and maintaining a standard for access that seeks to provide users least privilege, which requires that only the minimum necessary rights are assigned to complete a task.

Condition:

As part of our audit of STAR for the State of Wisconsin's financial statement audit for FY 2015-16, we identified weaknesses in policies, standards, and procedures related to security that resulted in weaknesses in the administration of STAR. We determined the detailed results of our review were too sensitive to communicate publicly. Therefore, we communicated the results in confidential interim memoranda to the DOA STAR Program Office.

Questioned Costs:

None.

Context:

STAR functions include processing vendor payments, accounting for cash receipts, tracking and maintaining employee information, tracking employee time, and processing payroll. STAR is used by the DOA State Controller's Office and most state agencies to report financial information, monitor budgets, administer federal grants, process payroll, process transactions, and manage assets.

Effect:

Although it can be difficult to determine how IT concerns such as those we identified affect the financial statements and material federal compliance areas, ineffective general IT controls in areas such as these may permit controls over individual systems to operate improperly and may allow financial statement misstatements and noncompliance to occur and not be detected.

Weaknesses in IT security policies, procedures, and controls increase the risk that unauthorized or erroneous transactions could be processed or changes could be made to accounting, payroll, and other data. In addition, failure to provide an appropriate level of protection for systems and data increases the risk that personally identifiable information could be accidentally or maliciously exposed.

Cause:

The implementation of STAR was a large and complex project, and it could have been expected that some procedures would not have been fully developed at the time of implementation. However, it would have been expected that the State would have already established policies and standards upon which procedures would have been developed for STAR. Further, during the implementation, Gartner Consulting, who was hired by DOA to provide risk assessments throughout implementation, recommended the development of "enterprise policies and procedures as soon as possible."

 Recommendation

We recommend the Department of Administration develop a timeline and plans, as described in our interim memoranda communications, to:

- *establish policies, standards, and procedures for the administration of STAR security that follow best practices;*
- *ensure controls over security conform to the policies, standards, and procedures;*
- *provide for regular review and updates to the policies, standards, and procedures to ensure a well-controlled environment; and*
- *address specific concerns identified in the interim memoranda.*

In addition, we recommend the Department of Administration:

- *implement the plans according to the developed timelines; and*
- *report at least quarterly to the Information Technology Executive Steering Committee on the status of its timelines and plans, and progress in implementing the detailed recommendations included in our confidential interim memoranda.*

Response from the Department of Administration: The Department of Administration agrees with the recommendations.

Corrective Action Plan from the Department of Administration: DOA has begun developing plans and a timeline to update STAR security policies, standards, and procedures to ensure that they follow best practices as defined in the Division of Enterprise Technology's *IT Security Policy Handbook* and National Institute of Standards and Technology's (NIST) *Special Publication 800-53r4*. The plans will include the controls that will be put in place to ensure that STAR security conforms to the updated policies and procedures and will provide for a comprehensive periodic review process to ensure a well-controlled environment. DOA will present the timeline and plan to the Information Technology Executive Steering Committee for approval no later than June 30, 2017, and will report on the same at least quarterly, thereafter. DOA will implement the plans according to the approved timeline.

Also as recommended by the auditors, DOA immediately undertook activities to address the specific concerns raised by the auditors in the interim audit memoranda. DOA will continue to address these concerns until they have been resolved in a manner consistent with the updated policies, standards, and procedures.

Anticipated Completion Date: June 30, 2017

Finding 2016-002: Information Technology Controls at the Department of Administration

Criteria:

Because the mainframe computer and servers may contain both financial data and confidential information, it is important that the Division of Enterprise Technology (DET) within DOA manage and maintain a secure environment. A secure environment begins by developing, approving, and following good policies, standards, and procedures. It is also important that DET establish settings that enforce its policies, standards, and procedures. Section 16.97, Wis. Stats., specifies DOA's responsibilities for the State's IT services, including DOA's responsibility to ensure that all state data processing facilities develop proper privacy and security procedures and safeguards.

Condition:

As part of our limited security review for the State of Wisconsin's financial statement audit for FY 2015-16, we identified weaknesses in security standards and procedures, as well as in DET's

current IT practices and settings. We determined the detailed results of our review were too sensitive to communicate publicly. Therefore, we communicated the results in a confidential interim audit memorandum to DET.

Questioned Costs:

None.

Context:

DET provides a variety of services to state agencies, including managing the mainframe computer for all agencies and managing servers for DOA and other agencies, including the departments of Corrections, Children and Families, Health Services, Natural Resources, and Revenue. DET is in the process of taking over responsibility for managing the servers for additional agencies, including the Department of Workforce Development.

DET also maintains DOA-related systems and performs programming and security functions, including maintaining the infrastructure for STAR, which includes statewide accounting and payroll functions.

Effect:

Although it can be difficult to determine how IT concerns such as those we identified affect the financial statements and material federal compliance areas, ineffective general IT controls in areas such as these may permit controls over individual systems to operate improperly and may allow financial statement misstatements and noncompliance to occur and not be detected.

Weaknesses in IT security procedures and controls increase the risk that unauthorized or erroneous transactions could be processed or changes could be made to accounting, payroll, and other data. In addition, failure to provide an appropriate level of protection for systems and data increases the risk that personally identifiable information could be accidentally or maliciously exposed.

Cause:

The development of security policies, standards, and procedures is complex and time consuming and must consider the needs of all agencies. During FY 2015-16, DET's Bureau of Security started a project to review DET's high-level policies and standards and is currently working to improve the controls within DET operations. At the time of our review, policies had been established and approved. However, the project to establish and approve standards and procedures was not yet completed.

Recommendation

We recommend the Department of Administration, Division of Enterprise Technology:

- *review and update, by June 30, 2017, its plans and timelines for development and implementation of standards and procedures;*
- *implement the plan to establish Division of Enterprise Technology standards and procedures according to the developed timeline;*

- *review practices and settings used at the Division of Enterprise Technology to ensure controls conform to the approved policies, standards, and procedures; and*
- *address the concerns identified in this security review.*

Response from the Department of Administration, Division of Enterprise Technology:
DET is in agreement with the recommendations.

Corrective Action Plan from the Department of Administration, Division of Enterprise Technology: DET has begun the process of documenting procedures. DET will review and update its plans and timelines for the development and implementation of standards and procedures. DET currently has 18 draft IT Standards with an anticipated completion and effective date on or before June 30, 2017. DET will develop a timeline and plan to implement the standards and procedures including the review of settings to ensure controls conform to DET policies, standards, and procedures. DET will develop a plan and timeline to review the practices that will ensure controls conform to the approved policies, standards, and procedures. DET will develop a plan and timeline to address the concerns identified in this security review.

Anticipated Completion Date: June 30, 2017

Finding 2016-003: Information Technology Controls at the University of Wisconsin System

Criteria:

The University of Wisconsin (UW) System consists of 13 four-year universities, 13 two-year colleges, UW-Extension, and UW System Administration. UW System Administration maintains the Shared Financial System (SFS), which is UW System's accounting system, and the Human Resource System (HRS), which is UW System's payroll and personnel system. These systems are used by all UW institutions. In addition, each institution maintains its own student information system (SIS) to administer federal student financial aid programs, as well as other computer applications. To provide proper internal control, IT security policies and procedures are necessary to ensure software and data stored and processed by the institutions are protected from accidental or intentional misuse or destruction. In addition, IT controls should be established to prevent inappropriate or inadvertent access to systems and data.

Condition:

During the FY 2014-15 audit (report 16-2), we identified weaknesses in IT security policies, procedures, and controls for several computer applications at several UW institutions. We recommended UW System Administration work with the chief information officers, chief business officers, and others as appropriate to assist UW institutions in implementing timely corrective actions related to our institution-specific concerns. In addition, we recommended UW System Administration develop systemwide IT security policies and procedures and provide guidance and training on them to all UW institutions (Finding 2015-002).

In December 2015, the UW System Board of Regents approved a high-level policy on information security that required UW System to develop and maintain a comprehensive information security program. Further, subsequent to the end of our audit period, systemwide IT policies were established in September 2016 through the UW Information Assurance Council. The Council, which is made up of IT, legal, and audit staff representing different institutions, including UW System Administration, was created to identify and analyze risks related to IT security, develop policies to address these risks, and review the performance of the UW System IT security program. Chancellors and chief information officers at each institution are responsible for ensuring compliance with the new policies.

During the FY 2015-16 audit, we continued to identify weaknesses in IT security policies, procedures, and controls at several institutions. We determined the detailed results of our review were too sensitive to communicate publicly. Therefore, we communicated these results in confidential interim memoranda to the institutions involved. Further, we did not audit the IT security policies and procedures at all UW institutions or the IT controls over all computer applications used by the institutions. However, we believe there is a potential that similar weaknesses may exist at those institutions we did not review.

Questioned Costs:

None.

Context:

UW institutions operate in a highly computerized environment and are responsible for maintaining confidential and sensitive information, such as student data.

Effect:

Although it can be difficult to determine how IT concerns such as those we identified affect the financial statements and material federal compliance areas, ineffective general IT controls in areas such as these may permit controls over individual systems to operate improperly and may allow financial statement misstatements and noncompliance to occur and not be detected.

Weaknesses in IT security policies, procedures, and controls increase the risk that unauthorized or erroneous transactions could be processed or changes could be made to accounting, payroll, and student data. In addition, failure to provide an appropriate level of protection for UW systems and data increases the risk that personally identifiable information could be accidentally or maliciously exposed.

Cause:

IT staff at each UW institution are responsible for ensuring that IT security policies, procedures, and controls are properly developed and maintained. Those institutions that have smaller IT staff may find challenges in meeting these responsibilities, maintaining proper separation of duties, and monitoring sufficiently all security policies and procedures. In addition, with changing technologies, monitoring and assessment of current processes are necessary to evaluate changing data security risks. Some of the institutions indicated that corrective action on prior-year findings was delayed in some areas as the institutions awaited the development of systemwide IT policies by the UW Information Assurance Council.

☑ Recommendation

In addition to recommendations we made to individual UW institutions, we recommend UW System Administration continue to work with the UW Information Assurance Council and individual institutions to:

- *plan for and implement the new information technology policies and procedures, including providing guidance and training regarding information technology security policies and settings, as needed;*
- *assist the institutions in implementing timely corrective actions related to our institution-specific recommendations; and*
- *develop procedures for assessing the level of protection provided for UW systems and data.*

Response from the University of Wisconsin System: UW System agrees with this finding.

Corrective Action Plan from the University of Wisconsin System:

- UW System institutions are actively implementing information security policies and procedures. The majority of these policies will be implemented by January 2018.
- Systemwide policies and procedures for Data Handling and Asset Inventory are under development and should be approved by June 2017.
- UW System Administration is providing and funding security awareness training modules to be used by all institutions. This will comply with the systemwide training compliance requirements by June 30, 2017. Some institutions may have previously acquired their own training programs.
- UW System Administration will work with institutions to safeguard information technology settings in student information systems. This may include sharing of practices across institutions, procedural changes, and instituting compensating controls.
- UW System Administration will assist the institutions in addressing institution-specific corrective actions. These efforts will be led by the Chief Information Security Officer (CISO) of UW System.
- UW System Administration will develop procedures for assessing the level of protection provided for UW system and data by December 2017.

UW System will continue to enhance its information security policies, procedures and practices. The specific actions below form the basis of the corrective action plan that will be advanced by UW System Administration.

Anticipated Completion Date:

Action	Anticipated Completion Date
Review of first five foundational Information Security Policies and Procedures related to authentication, security awareness, data classification, incident response, and acceptable use	April 30, 2017
Complete Procurement of Multi-factor Authentication Tool	May 30, 2017
Complete UWiac Comprehensive Information Security Plan	May 30, 2017
Approve Data Handling Policy	June 30, 2017
Approve Asset Inventory Policy	June 30, 2017

Finding 2016-004: Bank Account Reconciliations at the Department of Administration

Criteria:

Proper reconciliation of a bank account is a standard internal control procedure used by entities to ensure the accuracy of cash balances in the accounting records and with the bank, to prevent fraud or errors, and for financial reporting purposes. A bank reconciliation identifies the difference between the cash balance reported by the bank and the cash balance in an entity's own accounting records at a particular point of time.

To minimize the amount of work involved, it is good practice to carry out such reconciliations at reasonably frequent intervals. Further, to ensure consistency in preparation of bank account reconciliations and to aid in the event of staff turnover, it is important that an entity have written policies and procedures that document the process of preparing the bank reconciliation.

Condition:

At the time of our audit fieldwork in spring 2016, the State Controller's Office (SCO) within DOA had not performed or documented complete monthly reconciliations that included all components and reconciling items of the cash balance on the accounting records to the bank records, nor had it prepared a monthly bank reconciliation statement since implementation of STAR in October 2015. Further, SCO staff had not developed written policies and procedures for preparing complete monthly bank reconciliations of cash balances.

Questioned Costs:

None.

Context:

SCO is the custodian of the State's cash assets and is responsible for a complex and broad set of responsibilities that include implementing proper internal controls to ensure cash assets are properly managed.

Effect:

Without preparation of a complete and timely monthly bank account reconciliation and preparation of a bank reconciliation statement, the State is not assured that cash balances are accurate and free from error or fraud. In addition, without this control in place, SCO does not have assurances over the accuracy of cash reported in the financial statements for the various funds of the State.

Without written policies and procedures for preparing complete and timely bank reconciliations, inconsistencies may occur in preparing the monthly bank reconciliation statement. Further, turnover in staff may result in new staff having difficulty in completing the required processes if written procedures are not available to guide their work.

Cause:

SCO management believed that other processes implemented within STAR were sufficient. At the time of our audit, SCO had not anticipated the need to prepare a complete monthly bank reconciliation statement to demonstrate that the cash balances reported by the bank reconciled to the cash balances reported in STAR, and to provide needed assurances for financial reporting.

 Recommendation

We recommend the Department of Administration:

- *prepare a monthly bank reconciliation statement, beginning with October 2015, to ensure accurate financial reporting and security of cash;*
- *process adjustments needed to accounting records, as identified in the reconciling process, in a timely manner; and*
- *develop written policies and procedures for preparation of the monthly reconciliation of cash balances between the bank records and the State's accounting records.*

Response from Department of Administration, State Controller's Office: The State Controller's Office agrees with the recommendations.

Corrective Action Plan from the Department of Administration, State Controller's Office:

As of late March 2017, SCO has completed the monthly bank reconciliations of cash balances through December 2016, and is working on various components of these reconciliations for January and February 2017. It is important to note that SCO has maintained timely controls over the daily cash balances since the implementation of STAR on October 1, 2015:

- daily importing of all bank deposits into STAR and automatic matching with accounting entries;

- daily monitoring of all cash receipts and disbursements within the enterprise bank account;
- redundant daily monitoring and reconciliation of all disbursements by statutory fund;
- daily monitoring of enterprise cash float balances;
- monthly reconciliation of cash by statutory fund between STAR and the State Investment Fund; and
- monthly disbursement reconciliation.

SCO will continue to make adjustments to the accounting records as identified in the reconciliation processes. In addition, SCO will develop an additional monthly analysis to review all bank and book transactions, identify any necessary adjustments, and prepare a document summarizing those adjustments. That process will be implemented no later than June 1, 2017.

In September 2016, SCO provided the Legislative Audit Bureau with an initial set of procedures for the monthly bank to book reconciliation process. On an annual basis, the SCO will review those procedures and make any necessary updates.

Anticipated Completion Date: June 1, 2017

Finding 2016-005: Financial Reporting Concerns for the Capital Improvement Fund

Criteria:

The Capital Accounting Section (Capital Accounting) within DOA's SCO is responsible for preparing financial statements for the Capital Improvement Fund (CIF) that are in accordance with generally accepted accounting principles (GAAP). In addition, Capital Accounting is responsible for preparing the government-wide entries related to capital assets. The CIF financial statements and the government-wide entries are provided to SCO's Financial Reporting Section for use in compiling the State of Wisconsin's financial statements.

To assist state agencies in preparing the necessary information, SCO has developed the *Uniform GAAP Conversion Policies and Procedures Manual*, which outlines the State's financial reporting policies and procedures. Capital Accounting has also established procedures that require state agencies to review project classifications on a quarterly basis and to report any changes in a project classification to Capital Accounting. In addition, Capital Accounting should have sufficient procedures and controls in place, including a secondary review of the financial statement preparation process, to ensure that all appropriate adjustments are included in the financial statements and that the statements are materially correct.

Condition:

We identified errors in the project classifications for four projects. One project was inappropriately classified as a non-capital project, and three non-capital projects were inappropriately classified as capital projects.

Questioned Costs:

None

Context:

The CIF accounts for revenues from general obligation bond proceeds, which are primarily used for the acquisition or construction of major capital facilities and for repair and maintenance projects.

Effect:

As a result of the misclassification of the four projects, we identified the following errors in the financial statements:

- Capital Outlay was overstated by \$6.4 million and Other General Expenditures was understated by \$6.4 million in the Capital Improvement Fund financial statements;
- Nondepreciable Capital Assets—Other was overstated by \$20.2 million in the government-wide Statement of Net Position; and
- Net Investment in Capital Assets was overstated by \$24.4 million in the government-wide Statement of Net Position, and Unrestricted Net Assets was understated by \$24.4 million.

After we brought these concerns to its attention, Capital Accounting agreed to correct the financial statements for these errors.

Cause:

State agencies misclassified projects and Capital Accounting did not have procedures in place to identify the misclassifications to ensure accurate financial reporting. The complexity of the classification of outstanding debt, the number of projects involved, and the availability of Capital Accounting staff to perform secondary reviews of adjusting entries further contributed to the errors identified.

 Recommendation

We recommend the Department of Administration, Capital Accounting Section:

- *perform a reasonableness review of the classifications of capital projects used in preparation of the Capital Improvement Fund financial statements and government-wide adjusting entries;*
- *develop and document procedures for a secondary review of the process for preparation of the Capital Improvement Fund financial statements and government-wide adjusting entries; and*

- *for those projects that were misclassified, determine whether state agencies need additional guidance in determining the project classifications.*

Response from the Department of Administration State Controller's Office, Capital Accounting Section: The Department of Administration, State Controller's Office, Capital Accounting Section agrees with the recommendations.

Corrective Action Plan from the Department of Administration State Controller's Office, Capital Accounting Section: Upon receipt of new project classifications from state agencies, the Capital Accounting Section will perform independent reviews of these new projects by referencing the Division of Facilities Development information system, WisBuild, and reviewing chapter 20 of the state statutes and incurred expenditures in STAR. If differences with agency classifications are identified, the Capital Accounting Section will contact the agencies and differences will be resolved. Contacts with the agencies will also serve to ascertain whether the agencies need additional guidance in determining their project classifications. This new process will be instituted in March 2017.

Additionally, a secondary review of the GAAP reporting process resulting in the preparation of fund financial statements for the Capital Improvement Fund will be performed annually. Along with this, a secondary review of the government-wide financial statements adjusting entries will be performed. Both of these secondary reviews will be performed by the Capital Accounting Section chief effective with fiscal year 2017. Corrective actions will be the responsibility of John Martin of the Capital Accounting Section.

Anticipated Completion Date: March 2017 for Capital Accounting Section's review of projects and during the FY 2016-17 financial statement preparation for secondary review of GAAP reporting process

Finding 2016-006: Allocating Expenditures to the Correct Fiscal Year in the Transportation Fund

Criteria:

The Department of Transportation (DOT) is responsible for maintaining effective internal controls to ensure that expenditures are recorded in the correct fiscal year. DOT accounts payable staff are responsible for reviewing information to determine in which fiscal year the goods or services were received and charge the payment to the correct fiscal year. The information that must be reviewed could include information from construction project managers and details of the approved invoice.

Condition:

During the audit, we reviewed 22 construction transactions DOT paid in July 2016. We found that 6 of the 22 payments, totaling \$17.9 million, that were recorded in FY 2015-16 were for goods or services received in FY 2016-17. For example, we identified a payment for services performed from July 5, 2016, through July 8, 2016, that was recorded in FY 2015-16 instead of FY 2016-17.

Questioned Costs:

None

Context:

The Transportation Fund is a major fund for the State's Comprehensive Annual Financial Report (CAFR). DOT records construction activities in the Transportation Fund and is responsible for ensuring the information entered is accurately recorded in the correct fiscal year.

Effect:

Payments we identified that were recorded in the incorrect fiscal year resulted in a \$17.9 million overstatement in transportation expenditures reported in the Transportation Fund financial statements for FY 2015-16. After we identified the transactions that resulted in this error, DOT revised the expenditures recorded in the Transportation Fund financial statements for FY 2015-16.

Cause:

Due to the large volume of transactions and the limited number of DOT staff involved in the payment and review process, these errors appear to have been caused by human error. In addition, the timing of these payments coincided with DOT's implementation of STAR on July 1, 2016.

 Recommendation

We recommend the Department of Transportation improve its review of transactions near the end of the fiscal year to determine the correct fiscal year to which the payments should be recorded.

Response from the Department of Transportation: The Department of Transportation agrees with the audit finding and recommendation.

Corrective Action Plan from the Department of Transportation: The Department of Transportation will require a second approval on payment transactions throughout the year. Payment processors will be trained and instructed to pay particular attention to the date of service or the date that goods are delivered, and to assign the fiscal year of payment accordingly. As the fiscal year end approaches, a memo outlining the criteria for assigning the fiscal year of payment will be sent to payment processors, and the concept will be discussed and reiterated in section meetings. Payment approvers will be instructed to verify the period of performance and confirm that the fiscal year of the payment corresponds.

It is important to note that the conversion of the Department of Transportation's purchase order system to STAR in July 2016 limited the time frame in which it was possible to assign payment to purchase orders from the prior fiscal year. No such unusual limitation is expected in July 2017.

Anticipated Completion Date: Second approval of invoice voucher payments was implemented with conversion to STAR, July 1, 2016. Memo reviewing criteria for assigning fiscal year of payment will be sent prior to July 1, 2017

Finding 2016-007: Financial Reporting Process for the Injured Patients and Families Compensation Fund*Criteria:*

The Injured Patients and Families Compensation Fund (IPFCF), which is administered by the Office of the Commissioner of Insurance, is responsible for maintaining effective internal controls to ensure the financial information submitted to DOA's SCO for inclusion in the State's basic financial statements is fairly presented and that misstatements are prevented, or detected and corrected in a timely manner. As a proprietary fund, IPFCF is responsible for preparing the Statement of Cash Flows. Generally accepted accounting principles require that, in general, the Statement of Cash Flows present the amounts of cash receipts and disbursements at gross and that the amounts of cash receipts and disbursements are not netted together.

Condition:

Inaccurate information was used to prepare the Statement of Cash Flows. Although IPFCF staff indicated that they had identified discrepancies in the investment activity information and were working to resolve them, IPFCF did not properly report cash receipts and disbursements in the investing activities section of the Statement of Cash Flows.

Questioned Costs:

None

Context:

IPFCF insures participating physicians and other health care providers in Wisconsin against medical malpractice claims that exceed the primary malpractice insurance thresholds established by statutes. IPFCF's investments are managed by the State of Wisconsin Investment Board (SWIB). IPFCF uses investment activity information it receives from SWIB for financial reporting purposes.

Effect:

Although there was no effect on the total of the Cash Flows from Investing Activities section of the Statement of Cash Flows, the amounts reported for Proceeds from Sale and Maturities of Investment Securities was understated by approximately \$744 million, Purchase of Investment Securities was understated by approximately \$721 million, and Investment and Interest Receipts was understated by approximately \$23 million. Staff subsequently adjusted IPFCF's Statement of Cash Flows to correct the error and submitted a final version to SCO.

Cause:

IPFCF staff indicated that the investment activity information they received from SWIB did not provide the level of detail necessary to enable them to report the gross amounts of investing activities. IPFCF staff also indicated that SWIB did not provide the necessary information to enable them to properly account for a transfer of IPFCF's investments.

☑ Recommendation

We recommend the Injured Patients and Families Compensation Fund take steps to ensure that investment activity is properly reported in its Statement of Cash Flows.

Response from the Office of the Commissioner of Insurance: OCI agrees the *Condition* finding is accurate due to insufficient reporting from SWIB and the substantial portfolio transfers performed by SWIB and their third party managers. OCI was aware that the transfer of the management of the portfolio was occurring in December 2015 and January 2016, however was not made aware that the transfers were actual sales and purchases of the entire investment portfolio. Work product received by OCI from SWIB did not indicate any sales or purchase activity within the entire month of December 2015.

As noted under the *Condition, Context, Effect, and Cause* sections of the finding, OCI staff discovered and alerted the auditors the investment disbursements and receipts were not properly reconciling for the Statement of Cash Flows, which is forwarded to SCO for the State of Wisconsin CAFR. It was discovered the inaccuracies were due to a lack of proper documentation being forwarded to IPFCF from SWIB. OCI initiated corrective action during the audit in 2016 and corrected the investment reporting errors created by lack of information from SWIB. OCI staff was able to obtain the appropriate documentation directly from the Custodian to perform these duties accurately. The procedure for future reporting of investments is being documented and was immediately implemented by OCI.

The finalized financial Statement of Cash Flows was forwarded to the auditors and SCO January 26, 2017.

Corrective Action Plan from the Office of the Commissioner of Insurance: There is no corrective action plan necessary going forward. IPFCF staff corrected the years-long practice in which SWIB reported investments to OCI as a "net" purchase and/or sale fees to a "gross" purchase and/or sale fees with the current FY 2015-16 audit and the CAFR this year. IPFCF staff is documenting the current procedure for future Statement of Cash Flows preparation and incorporating the "gross" investment activities versus the previously utilized "net" for investment activities.

Anticipated Completion Date: IPFCF completed the CAFR and Statement of Cash Flows entries and submitted to DOA in January 2017

Additional Matter

DOT is responsible for maintaining effective internal controls to ensure the financial information it prepares for inclusion in the State's CAFR is accurate. For the FY 2015-16 CAFR, we again found that DOT did not have sufficient procedures and controls in place to ensure that all appropriate financial information was prepared for transportation activities. For example, DOT did not prevent, or detect and correct in a timely manner, misstatements in classifying transportation activities reported in the Capital Improvement Fund. We further communicated our concerns and recommendation to DOT management.