



CALIFORNIA
High-Speed Rail Authority

2015 Year-End Close Process Audit

August 2016

Prepared by the Audit Office

Report Number 15-04

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EXECUTIVE SUMMARY

The California High-Speed Rail Authority's (Authority) Audit Office has completed an audit of the Authority's Financial Office's (FINO) fiscal year 2014-15 accounting year-end close process.

- The Audit Office evaluated the accounting year-end close process and examined departmental accounting records maintained by FINO to determine whether the year-end close process is adequate to ensure there are no material misstatements in the 2015 financial statements, as well as review the accrual procedures for compliance with Governmental Accounting Standards Board (GASB) pronouncements and State year-end close process.
- We interviewed employees for job responsibilities, and reviewed existing internal controls and current business practices over state assets to determine whether FINO is in compliance with state rules and regulations.

Based on our examination, we noted internal control weaknesses and provided recommendations to improve the year-end close processes and compliance with applicable state rules and regulations. We noted no material misstatements in the accounting information reviewed.

All levels of management must provide active, ongoing oversight and monitoring processes for the prevention and early detection of fraud and errors in program administration, and must routinely monitor, evaluate, and improve internal controls when necessary. Internal accounting controls comprise the methods and procedures directly associated with safeguarding assets and assuring the reliability of accounting data. Internal administrative controls comprise the methods and procedures that address operational efficiency and adherence to management policies. The Audit Office identified three specific findings (A, B, C) that directly or indirectly affected all the reported findings, and if corrected would alleviate or correct the remaining findings (D, E, F, G, H, I, J, K) identified in this report.

- Finding A - FINO did not create a budgetary plan for charging encumbrances and subsequent expenditures when issuing multi-year agreements, which can affect the validity of the reported and recorded encumbrances during fiscal year 2014-15.
- Finding B - Four of six Fiscal Month 13 (FM 13) year-end adjustments reviewed were labeled as revisions or corrections with either a vague or no description of why the adjustment was made. While six of the six FM 13 adjustments reviewed were incorrectly labeled as A-4, A-8 or not identified as FM 13 adjustments. The accounting period FM 13 is used to post all year-end adjusting entries.
- Finding C - FINO relied strictly on CALSTARS, the State's accounting system, to identify all fiscal errors, however CALSTARS only identifies system-generated errors and not internal errors. Four of the six year-end adjustments were labeled as revisions or corrections, and included either a vague or no description why the adjustment was made or how the error was identified.

These three findings revealed a lack of internal controls, which caused concern to the Audit Office as the reported figures for Year-End 2014-15 were based on multiple revisions, corrections and inconsistent procedures.

FINO must strengthen internal controls, specifically, ensure encumbrances are properly budgeted and reconciled monthly, internal errors not detected by CALSTARS are properly identified, documented and corrected, and Fiscal Month 13 year-end adjustments are reviewed for accuracy.

BACKGROUND

The Authority is responsible for overall management, oversight, and monitoring of state and federal funds received. This function requires accountability and transparency, and must provide a means of tracking and monitoring program goals, accomplishments, and compliance with ARRA grant requirements, which includes reviewing Report of Expenditures of Federal Funds (Report 13), the Federal Schedule of Expenditures of Federal Awards (SEFA), to determine if the year-end amounts are reconciled.

FINO used CALSTARS, the State of California accounting system, during the period audited and makes year end adjustment in the accounting period referred to as Fiscal Month 13. The Authority presently has both internal staff and contract staff performing financial management activities.

The Department of Finance (DOF) provides all agencies with the State's uniform accounting system setting statewide fiscal accounting policies and procedures pursuant to Government Code section 13300 and 13310, and contained in the State Administrative Manual (SAM) sections 7110-19464. It is important that Authority provide accurate year-end financial statements to the State Controller's Office (SCO) to ensure that the Budgetary/Legal Basis Annual Report reflects reliable financial information. The State of California Budgetary/Legal Basis annual report is prepared in accordance with state laws and regulations and reflects the past execution of the State's budget. The report does not fully conform to the standards set by the Governmental Accounting Standards Board (GASB); therefore, the SCO must make adjustments and revisions, based on the standards prescribed by GASB to convert into a Generally Accepted Accounting Principle (GAAP) basis of reporting. The adjustments include reclassifying the Budgetary/Legal basis of accounts to GAAP balance sheet and operating statements and adding additional note disclosure, statistical data, and GAAP adjustments¹. Included in the GAAP adjustments are encumbrances, which are the recognition of commitments that will subsequently become expenditures when goods and services are received. Encumbrances are posted for documents such as purchase estimates, purchase orders, and contracts.

AUDIT SCOPE AND METHODOLOGY

Our office conducted an internal control audit of the fiscal year 2014-15 accounting year-end close process covering the period from July 1, 2014 through June 30, 2015. During the audit period, the Authority received funds from ARRA grants (federal funds), as well as High-Speed Passenger Train Bond Fund, Greenhouse Reduction Fund, and relied on the accounting records for these funds that were maintained by FINO in CALSTARS. We did not perform a financial audit of the year-end 2014-15 financial statements to obtain reasonable assurance about whether the financial statements are free from material misstatements; however, we performed tests of the year-end processes for the purpose of this

¹ Year-End Financial Reports Information GAAP Basis For the Fiscal Year Ended June 30, 2015 California State Controller's Office Pg.13

audit. Providing an opinion on the financial statements taken as a whole was not an objective of our audit, and accordingly, we do not express such an opinion.

FINO is responsible for ensuring accurate financial reporting and compliance with the applicable laws, regulations and program requirements.

The objectives of the audit were to evaluate the year-end close process and determine whether the process is adequate to provide reasonable assurance that there are no material misstatements in the year-end 2014-15 financial reports and to perform a general review of the accrual procedures to determine adherence with the Governmental Accounting Standards Board (GASB) and the State year-end close requirements.

FINO's accounting records and other related supporting documents relating to our audit objectives were reviewed. The following procedures were performed:

- Discussed FINO's accounting and reporting systems with key personnel in order to gain an understanding of the procedures related to administering the year-end close process.
- Reviewed applicable policies and procedures to gain an understanding of FINO's internal controls related to compliance with the applicable standards, rules and regulations.
- Analyzed FINO's methodology and supporting documentation for adjustments and accrual amounts recorded in the general ledger to determine whether transactions were accurately recorded in the appropriate general ledger accounts and amounts were adequately documented and supported.

Except as noted, we conducted our audit in accordance with government auditing standards for fiscal compliance as issued by the Comptroller General of the United States. The Authority's Audit Office has not undergone a peer review as required by the standards due to the recent formation of the Audit Office and the lack of a body of work to be reviewed. The Audit Office is not yet eligible for a peer review for the reasons stated.

FINDINGS AND RECOMMENDATIONS

INTERNAL CONTROL WEAKNESSES

Based on our analysis of the accounting records and process performed by FINO, we identified the following internal control weaknesses that need to be addressed by FINO management in order to improve the effectiveness of the year-end process and the efficiency of the Authority's accounting operations:

- A. FINO did not have a budgetary plan for the establishment of encumbrances and was not reconciling encumbrance balances on a monthly basis during fiscal year 2014-15. The State Administrative Manual, Section 8340, requires all state departments to determine the budgetary plan for charging encumbrances and subsequent expenditures when issuing multi-year agreements. Departments have discretion as to which fiscal year appropriation to charge; however, the budgetary plan is the predominant factor in making the determination. Three of the three contracts reviewed had encumbrance revisions without justifications or explanations. FINO was made aware of the lack of a budgetary plan in the Year-End 2013-14 Close Process Audit.

FINO functional areas should develop a budgetary plan for charging encumbrances and subsequent expenditures when entering into multi-year agreements. Management should also identify and articulate clear lines of organizational authority and responsibility and develop an internal review system to ensure budgeted amounts are accurate and adjustments are properly documented and justified.

- B. Four of the six year-end adjusting entries reviewed were labeled as "revisions" or "corrections" and included either a vague or no description of why the revision or correction occurred. We were unable to verify that the revisions or corrections were necessary or done accurately. In addition, a review of six of six FM 13 year-end adjustments revealed that all the batch headers were incorrectly labeled. Batch headers under "Special Instructions" indicate A-4, A-8, or were not labeled as adjustments. The A-4 adjustment is not applicable to the Authority according to FINO. The original batches were reviewed and approved as identified in FINO's procedures. However, the review process was not effective in identifying and detecting errors.

Adjusting entries should include required supporting documentation and methodology used to determine amounts of the adjusting entries. FINO staff performing year-end adjustments should correctly complete batch header information and provide a brief but detailed description of the entry.

- C. Six of the six year-end entries reviewed were incorrectly labeled or identified as revisions or corrections with no detailed description of what caused the error or how the error was identified. Per FINO, they rely on CALSTARS to identify all errors. However, CALSTARS only identifies system-generated errors. FINO currently identifies non-system generated errors when staff inadvertently discovers, then independently corrects, the error. CALSTARS Manual Volume 4 requires a pre-audit or review and approval of source documents before transactions are recorded.

FINO should develop an effective system of internal controls to ensure errors not detected by CALSTARS are identified, tracked, accurately corrected, and brought to the attention of management in a timely manner.

- D. In our review of financial statement balances we noted federal expenditures (Report No.13) and Receivables Due from Other Governments were not reconciled. The State Administrative Manual, Sections 7974 and 7974.1, requires all supporting documentation used to prepare Report No.13 (Report of Expenditures of Federal Funds) must reconcile to the year-end financials and must be made available when requested. State Administrative Manual, Section 8776, requires all accounts receivables be reconciled and proper recordkeeping be maintained to substantiate the account receivable. Year-end 2014-15 Report No. 13 disclosed federal expenditures of \$159,029,394.37, while the Schedule of Expenditures of Federal Awards (SEFA) amount reported a total of \$134,559,368, which is a difference of nearly \$25 million. FINO indicated the difference is related to encumbrances; however, no reconciliation was conducted during fiscal year 2014-15 to identify the details of the \$25 million difference. In addition, Due from Other Governments reported an ending balance of \$156,331,214.51 and was not reconciled during fiscal year 2014-15. FINO was unable to provide supporting documentation or methodology used to ensure amounts reported for expenditures and receivables was correct. We were not provided sufficient documentation to ensure the ending balances reported were substantiated.

FINO should reconcile all federal expenditures and receivables as required by the State Administrative Manual. FINO should maintain all supporting documents and identify methodology used to reconcile expenditures and receivables.

- E. The Authority's policy and procedural or operational manuals were not maintained or available to demonstrate compliance with applicable laws, regulations, and rules. According to the State Administrative Manual, Section 20050, all levels of management must provide active, ongoing oversight and monitoring processes for the prevention and early detection of fraud and errors in program administration, and must routinely monitor, evaluate, and improve internal controls when necessary. Internal accounting controls comprise the methods and procedures directly associated with safeguarding assets and assuring the reliability of accounting data. Internal administrative controls comprise the methods and procedures that address operational efficiency and adherence to management policies. Our engagement letter requested FINO provide any policies and procedures manuals. In response FINO provided four. However, on the Web-Based knowledge management system for the Authority we identified that FINO has over 35 policies and procedures.

FINO should review all developed policies and procedures or operational manuals and ensure appropriate staff is aware of requirements related to their specific job function. FINO should periodically review and revise policies, procedures and operational manuals when necessary.

- F. The Office Revolving Fund was not reconciled within 30 days per the State Administrative Manual, Section 7901. Initially Office Revolving Fund reconciliations were prepared, however, they were incorrect. All Office Revolving Fund reconciliations were revised in June and July of 2015.

FINO should develop an effective system of internal review to ensure compliance with applicable State Administrative Manual requirements.

- G. High-Speed Passenger Train Bond Fund (Fund 6043) reconciliations were missing support documents for multiple transactions. The State Administrative Manual, Section 7901, requires departments to reconcile account balances to supporting documentation such as invoices, receipts, reports, etc., to ensure the accuracy and completeness of transactions posted to the departmental accounts. In addition, a unit supervisor or unit manager should review all reconciliations to ensure supporting documentation is maintained and reviewed for completeness and accuracy. FINO was able to provide the support after it was requested by the auditor; however, the support was not referenced with the final reconciliation. FINO was made aware of this issue in the Year-End 13-14 Close Process Audit.

FINO should develop an effective system of internal review to ensure reconciliations are supported with all required documents.

- H. High-Speed Passenger Train Bond Fund (Fund 6043) and Greenhouse Gas Reduction (Fund 3228) had outstanding accounts payables amounts of 73% and 60% two months into fiscal-year 2015-16. Eight months into FY 15-16 outstanding accounts payables amounts were 21% and 17.5%. CALSTARS Manual, Chapter 7, requires accounts payable be reviewed at year-end for validity and the State Administrative Manual, Section 10440, requires that payables be identified as actual and accrued expenditures. FINO did not provide supporting documentation indicating outstanding payables were reviewed at year-end or provide actual and accrued expenditure support. Per FINO, the accounts payable had not been reconciled in February 2016, while our audit fieldwork was in progress. We could not determine the validity of the payables or determine if payments were made promptly. The Authority is responsible for expenses associated with late payments (late charges, accrued interest, etc.) so it is imperative that payments be made promptly.

FINO should develop an effective system of internal review to ensure accounts payables are reviewed and validated. FINO should also ensure that payments are made in a prompt manner.

- I. More than one hundred employee accounts receivable over 4 months old with a value of \$43,049.17 are outstanding. Of these 17, had outstanding balances greater than \$500. We tested for collection efforts 12 employee accounts receivable which totaled \$28,293, or 65%, of the outstanding balance. We found 11 were for separated employees totaling \$27,448, no amounts were collected and no documentation of efforts to collect from employees was provided by FINO or the Human Resources Branch The State Administrative Manual, Sections 8776 thru 8776.7, provides state agencies with the minimum procedures for recording, reconciling and collecting of

accounts receivable, which are claims against a debtor, such as a person (employee or non-employee), business, or government entity for money owed to the state. The Authority has contracted with the California Department of Transportation for human resources services, specifically payroll related services. FINO, the Human Resources Branch, and Caltrans were not consistently communicating to reconcile and collect outstanding employee accounts receivable, especially for employees who separate from the Authority.

FINO and the Human Resources Branch should identify and articulate clear lines of organizational authority and responsibilities. In addition, FINO and the Human Resources Branch should assess amounts owed to the Authority and when the amounts are expected to be collected.

- J. FINO provided auditor with an original year-end Work Plan for fiscal year 2014-15. Four months later FINO provided a revised year-end Work Plan. CALSTARS, Volume 7, Chapter 1, requires that agencies create and customize a year-end work plan specifically based on their activities. In addition, departments should identify a person to perform the roll of year-end activity coordinator to ensure activities are completed timely and correctly. Tasks 68, 70, 73 and 74 on the year-end Work Plan are not applicable to the Authority, according to FINO, but were identified on the original year-end Work Plan with a responsible person. FINO did not customize the original year-end Work Plan and did not identify an activity coordinator. The revised, undated year-end Work Plan, provided four months after the beginning of the audit, properly identified the same reviewed tasks as not applicable to the Authority.

FINO should comply with CALSTARS requirements of creating and customize a year-end work plan based on Authority activities. In addition, the activity coordinator should ensure documentation is maintained to support each completed task.

- K. FINO did not have properly designed controls or a clear methodology surrounding the year-end GAAP (Generally Accepted Accounting Principles) adjustment. The Authority's financial information is accounted for and reported on a budgetary/legal basis (modified accrual basis according to state laws and regulations) and must be reported on a GAAP basis at year end. The GAAP adjustment provides the standard for financial presentation and is submitted to SCO (State Controller's Office). The entry included Accounts Payable of \$17.48 Million, Due to other Funds of \$7.73 Million and Due to Other Governments of \$7.96 Million. GAAP indicates that encumbrances should not be recognized as expenses until the goods or services are received. FINO submitted the GAAP adjustment to SCO, however, the supporting documents and methodology used to calculate the reported balance was not provided to the Audit Office.

FINO should implement controls to maintain all supporting documentation used to calculate the GAAP adjustment and to document the methodology used to determine the reported ending balances.

August 24, 2016

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Paula Rivera
Chief Auditor
California High-Speed Rail Authority

Dear Ms. Rivera,

Attached you will find the California High-Speed Rail Authority (Authority) Financial Office's response to the 2015 Year-End Close Process Audit draft report.

The draft report contains eleven findings. Mitigation methods and policies for the recommendations are already implemented and resolved.

The recommendations from the draft audit report have a common theme of more robust documentation, enhanced standardization of internal controls and review procedures, and better communication from our office. The Financial Office understands the importance of timely and effectively addressing the findings. As such, we implemented the necessary corrective actions and control procedures required to ensure each of the issues were adequately resolved.

Importantly, we note there were no material misstatements identified in the draft audit report. This highlights the already strong internal processes in place in the Financial Office. Coupled with the enhancements enacted through these audit findings, the Financial Office considers its year-end close and day-to-day accounting processes meet the rigorous standards that the High-Speed Rail Project requires.

Please contact Russell Fong, Chief Financial Officer, at (916) 431-2929 with any questions or concerns.

Sincerely,



Russell Fong
Chief Financial Officer
California High-Speed Rail Authority

EDMUND G. BROWN JR.
GOVERNOR



Response to 2015 Year-End Close Process Audit of the Authority Financial Office

- A. FINO did not have a budgetary plan for the establishment of encumbrances and was not reconciling encumbrance balances on a monthly basis during fiscal year 2014-15. The State Administrative Manual, Section 8340, requires all state departments to determine the budgetary plan for charging encumbrances and subsequent expenditures when issuing multi-year agreements. Departments have discretion as to which fiscal year appropriation to charge; however, the budgetary plan is the predominant factor in making the determination. Three of the three contracts reviewed had encumbrance revisions without justifications or explanations. FINO was made aware of the lack of a budgetary plan in the Year-End 2013-14 Close Process Audit.

FINO functional areas should develop a budgetary plan for charging encumbrances and subsequent expenditures when entering into multi-year agreements. Management should also identify and articulate clear lines of organizational authority and responsibility and develop an internal review system to ensure budgeted amounts are accurate and adjustments are properly documented and justified.

Response:

Agree, FINO implemented a new process to develop a budgetary plan for charging encumbrances and subsequent expenditures to multi-year agreements (effective September 2015). Additionally FINO has implemented its encumbrance policy (POLI-FIS-25, effective July 2015 and revised December 2015). This issue has been resolved.

FINO has also implemented clear lines of organizational authority and responsibility regarding the multi-year encumbrance approach (September 2015). This issue has been resolved.

To ensure encumbrances are properly budgeted and reconciled monthly, FINO's implemented process captures and documents encumbrances for multi-year contracts in a 36-Month Plan, a Capital Outlay Report, and a Funding Contribution Plan. The encumbrance policy outlines roles of authority and responsibility, and states that the Budget Officer is responsible for monitoring and reporting the budget updates to the Chief Financial Officer (CFO). This process also includes a monthly review of open contracts and a reconciliation between expenditures and encumbrances.

Individual Responsible: Jamey Matalaka, Assistant Chief Financial Officer, Financial Office

- B. Four of the six year-end adjusting entries reviewed were labeled as “revisions” or “corrections” and included either a vague or no description of why the revision or correction occurred. We were unable to verify that the revisions or corrections were necessary or done accurately. In addition, a review of six of six FM 13 year-end adjustments revealed that all the batch headers were incorrectly labeled. Batch headers under “Special Instructions” indicate A-4, A-8, or were not labeled as adjustments. The A-4 adjustment is not applicable to the Authority according to FINO. The original batches were reviewed and approved as identified in FINO’s procedures. However, the review process was not effective in identifying and detecting errors.

Adjusting entries should include required supporting documentation and methodology used to determine amounts of the adjusting entries. FINO staff performing year-end adjustments should correctly complete batch header information and provide a brief but detailed description of the entry.

Response:

Agree, FINO implemented, for the FY2015-16 Year-End process and ongoing, an effective system to ensure that required supporting documentation is maintained for adjusting entries, based on documented policy (POLI-FIS-07, July 2015). This issue has been resolved.

FINO has also implemented a management review process to identify and detect errors, which was in place for the FY2015-16 Year-End process and ongoing. This issue has been resolved.

FINO has reviewed, validated, and implemented all CalSTARS batch header slip forms for adjusting entries, beginning the FY2015-16 Year-End process. This issue has been resolved.

Individual Responsible: Jamey Matalka, Assistant Chief Financial Officer, Financial Office

- C. Six of the six year-end entries reviewed were incorrectly labeled or identified as revisions or corrections with no detailed description of what caused the error or how the error was identified. Per FINO, they rely on CALSTARS to identify all errors. However, CALSTARS only identifies system-generated errors. FINO currently identifies non-system generated errors when staff inadvertently discovers, then independently corrects, the error. CALSTARS Manual Volume 4 requires a pre-audit or review and approval of source documents before transactions are recorded.

FINO should develop an effective system of internal controls to ensure errors not detected by CALSTARS are identified, tracked, accurately corrected, and brought to the attention of management in a timely manner.

Response:

Agree, FINO has implemented, for the FY2015-16 Year-End process and ongoing, a procedure to ensure an effective system of internal controls and to ensure that errors are identified, tracked, accurately corrected, and brought to the attention of FINO management in a timely manner, based on documented policy (POLI-FIS-07, July 2015). This issue has been resolved.

FINO acknowledges that it uses CalSTARS' edit file (or "error file") to identify system-generated errors. Non-system generated errors/manual adjustments are identified through monthly reconciliations between the Authority's records (CalSTARS) and the State Controller's Office records, and the State Treasurer's Office records. This process generates a monthly list of potential errors and adjustments, which are reviewed and addressed by accounting managers.

Individual Responsible: Jamey Mataalka, Assistant Chief Financial Officer, Financial Office

- D. In our review of financial statement balances we noted federal expenditures (Report No.13) and Receivables Due from Other Governments were not reconciled. The State Administrative Manual, Sections 7974 and 7974.1, requires all supporting documentation used to prepare Report No.13 (Report of Expenditures of Federal Funds) must reconcile to the year-end financials and must be made available when requested. State Administrative Manual, Section 8776, requires all accounts receivables be reconciled and proper recordkeeping be maintained to substantiate the account receivable. Year-end 2014-15 Report No. 13 disclosed federal expenditures of \$159,029,394.37, while the Schedule of Expenditures of Federal Awards (SEFA) amount reported a total of \$134,559,368, which is a difference of nearly \$25 million. FINO indicated the difference is related to encumbrances; however, no reconciliation was conducted during fiscal year 2014-15 to identify the details of the \$25 million difference. In addition, Due from Other Governments reported an ending balance of \$156,331,214.51 and was not reconciled during fiscal year 2014-15. FINO was unable to provide supporting documentation or methodology used to ensure amounts reported for expenditures and receivables was correct. We were not provided sufficient documentation to ensure the ending balances reported were substantiated.

FINO should reconcile all federal expenditures and receivables as required by the State Administrative Manual. FINO should maintain all supporting documents and identify methodology used to reconcile expenditures and receivables.

Response:

Agree, FINO has implemented a procedure to reconcile all federal expenditures and receivables including SCO to CalSTARS and SEFA to CalSTARS (Report 13) to ensure that expenditures are reconciled and supporting documentation is included, in accordance with SAM and based on documented policy (POLI-FIS-07, July 2015). This issue has been resolved.

FINO acknowledges that there was no reconciliation conducted during FY2014-15 to identify the details of the \$25 million difference between SEFA and CalSTARS. FINO did perform a reconciliation between CalSTARS and SCO for FY2015-16 in order to account for the differences between SCO's cash-based reporting and the Authority's accrual-based reporting (CalSTARS). At fiscal year-end close, the "Due From" receivable account was reconciled to the federal grants expenditure detail and was accurately reported for the fiscal year.

To ensure Fiscal Month 13 year-end adjustments are reviewed for accuracy and properly documented, FINO reviewed all CalSTARS entries prior to input. In addition, FINO completes expenditure and revenue monthly reconciliation of federal expenditures between the Authority's records (CalSTARS) and the SCO's records. Also, FINO has conducted an annual reconciliation between SEFA and CalSTARS for the FY2015-16.

- E. The Authority's policy and procedural or operational manuals were not maintained or available to demonstrate compliance with applicable laws, regulations, and rules. According to the State Administrative Manual, Section 20050, all levels of management must provide active, ongoing oversight and monitoring processes for the prevention and early detection of fraud and errors in program administration, and must routinely monitor, evaluate, and improve internal controls

when necessary. Internal accounting controls comprise the methods and procedures directly associated with safeguarding assets and assuring the reliability of accounting data. Internal administrative controls comprise the methods and procedures that address operational efficiency and adherence to management policies. Our engagement letter requested FINO provide any policies and procedures manuals. In response FINO provided four. However, on the Web-Based knowledge management system for the Authority we identified that FINO has over 35 policies and procedures.

FINO should review all developed policies and procedures or operational manuals and ensure appropriate staff is aware of requirements related to their specific job function. FINO should periodically review and revise policies, procedures, and operational manuals when necessary.

Response:

Agree, by December 2015, FINO had implemented over 35 policies and procedures. These policies and procedures are updated and maintained regularly, and are available to staff via the Authority's web-based document repository. FINO provides training on updated policies and procedures to staff. This issue has been resolved.

FINO acknowledges that it did not physically provide all of its 35 FINO policies and procedures to the auditor. FINO also acknowledges that its staff follows the policies and procedures, as well as the State Administrative Manual (SAM), and that they have electronic access to the documentation.

Individual Responsible: Jamey Matalka, Assistant Chief Financial Officer, Financial Office

- F. The Office Revolving Fund was not reconciled within 30 days per the State Administrative Manual, Section 7901. Initially Office Revolving Fund reconciliations were prepared, however, they were incorrect. All Office Revolving Fund reconciliations were revised in June and July of 2015.

FINO should develop an effective system of internal review to ensure compliance with applicable State Administrative Manual requirements.

Response:

Agree, FINO implemented an effective system of internal review to ensure compliance with applicable State Administrative Manual requirements. The new system includes a new process and schedule to ensure that Office Revolving Fund (ORF) account reconciliations are performed monthly (effective May 2015). This issue has been resolved.

FINO acknowledges that in FY2014-15, the ORF account was not reconciled timely. However, FINO did perform the review past the 30-day requirement and ensured there were no errors to reporting. The General Ledger Supervisor also tracks reconciliations, and supervisory reviews are logged within 30 days.

Individual Responsible: Jamey Matalka, Assistant Chief Financial Officer, Financial Office

- G. High-Speed Passenger Train Bond Fund (Fund 6043) reconciliations were missing support documents for multiple transactions. The State Administrative Manual, Section 7901, requires departments to reconcile account balances to supporting documentation such as invoices, receipts, reports, etc., to ensure the accuracy and completeness of transactions posted to the departmental accounts. In addition, a unit supervisor or unit manager should review all reconciliations to ensure supporting documentation is maintained and reviewed for completeness and accuracy. FINO was able to provide the support after it was requested by the auditor; however, the support was not referenced with the final reconciliation. FINO was made aware of this issue in the Year-End 13-14 Close Process Audit.

FINO should develop an effective system of internal review to ensure reconciliations are supported with all required documents.

Response:

Agree, FINO has implemented an effective system of internal review to ensure reconciliations are supported with all required documentation, consistent with the State Administrative Manual and documented policy (POLI-FIS-07, July 2015). The issue has been resolved.

FINO acknowledges that it did not initially provide the auditor with all detailed supporting documentation for the High-Speed Passenger Train Bond Fund (Fund 6043) reconciliations. Instead, FINO initially provided CalSTARS reports that include summary information. As noted by the audit, supporting detail was provided after the initial request.

Individual Responsible: Jamey Matalka, Assistant Chief Financial Officer, Financial Office

- H. High-Speed Passenger Train Bond Fund (Fund 6043) and Greenhouse Gas Reduction (Fund 3228) had outstanding accounts payables amounts of 73% and 60% two months into fiscal year 2015-16. Eight months into FY 15-16 outstanding accounts payables amounts were 21% and 17.5%. CALSTARS Manual, Chapter 7, requires accounts payable be reviewed at year-end for validity and the State Administrative Manual, Section 10440, requires that payables be identified as actual and accrued expenditures. FINO did not provide supporting documentation indicating outstanding payables were reviewed at year-end or provide actual and accrued expenditure support. Per FINO, the accounts payable had not been reconciled in February 2016, while our audit fieldwork was in progress. We could not determine the validity of the payables or determine if payments were made promptly. The Authority is responsible for expenses associated with late payments (late charges, accrued interest, etc.) so it is imperative that payments be made promptly.

FINO should develop an effective system of internal review to ensure accounts payables are reviewed and validated. FINO should also ensure that payments are made in a prompt manner.

Response:

Agree, FINO has implemented an effective system of internal review to ensure accounts payables are reviewed and validated, and that payments are made in a prompt manner, based on documented policy (POLI-FIS-07, July 2015). This issue has been resolved.

FINO acknowledges that it did not reconcile Accounts Payable in February 2016 in a timely manner. However, the reconciliation was completed the following month, March 2016, as allowed per the CalSTARS Manual, Volume 7.

FINO accrues Accounts Payable and ensures the amounts are reviewed and validated as required per the CalSTARS Manual, Volume 7. Due to the nature of vendor's billing schedules, the Authority must estimate a portion of Accounts Payable and some items remain on Authority records for multiple months. These accruals are valid expenses as the services have been rendered from the vendors.

Individual Responsible: Jamey Matalka, Assistant Chief Financial Officer, Financial Office

- I. More than one hundred employee accounts receivable over 4 months old with a value of \$43,049.17 are outstanding. Of these 17, had outstanding balances greater than \$500. We tested for collection efforts 12 employee accounts receivable which totaled \$28,293, or 65%, of the outstanding balance. We found 11 were for separated employees totaling \$27,448, no amounts were collected and no documentation of efforts to collect from employees was provided by FINO or the Human Resources Branch. The State Administrative Manual, Sections 8776 thru 8776.7, provides state agencies with the minimum procedures for recording, reconciling and collecting of accounts receivable, which are claims against a debtor, such as a person (employee or non-employee), business, or government entity for money owed to the state. The Authority has contracted with the California Department of Transportation for human resources services, specifically payroll related services. FINO, the Human Resources Branch, and Caltrans were not consistently communicating to reconcile and collect outstanding employee accounts receivable, especially for employees who separate from the Authority.

FINO and the Human Resources Branch should identify and articulate clear lines of organizational authority and responsibilities. In addition, FINO and the Human Resources Branch should assess amounts owed to the Authority and when the amounts are expected to be collected.

Response:

Agree, FINO and the Human Resources Branch have defined and implemented new organizational roles and responsibilities related to employee accounts receivable, based on documented policy (POLI-FS-19, July 2015). The Authority has also implemented new tracking and reporting processes to consistently monitor outstanding employee account receivable balances. The issue regarding clear lines of organizational authority and responsibilities has been resolved.

The Authority acknowledges that many accounts had employee receivables outstanding and that documentation was not provided to the auditor. The Authority started contracting with the Department of Transportation (Caltrans) for human resource services in March 2014. Due to some resource issues, the Authority faced some challenges retrieving the necessary information in order to collect on the outstanding account receivables. However, since June 2016, Caltrans' Human Resources Division, the Authority's Human Resources Branch, and the Authority's Accounting Branch have been working together to collect on these outstanding Accounts Receivable by clearly defining roles and responsibilities, reporting on the status of

this information on a monthly basis, and adequately notifying active and separated employees regarding their outstanding Accounts Receivable in a more timely manner. The monthly tracking report also enables the Authority to consistently monitor the outstanding Accounts Receivable balance owed to the Authority and the amounts that we can expect to collect or write-off.

Individual Responsible: Mahsa Patton, Assist Chief Administrative Officer, Administration Office; and Jamey Matalka, Assistant Chief Financial Officer, Financial Office

- J. FINO provided auditor with an original year-end Work Plan for fiscal year 2014-15. Four months later FINO provided a revised year-end Work Plan. CALSTARS, Volume 7, Chapter 1, requires that agencies create and customize a year-end work plan specifically based on their activities. In addition, departments should identify a person to perform the roll of year-end activity coordinator to ensure activities are completed timely and correctly. Tasks 68, 70, 73 and 74 on the year-end Work Plan are not applicable to the Authority, according to FINO, but were identified on the original year-end Work Plan with a responsible person. FINO did not customize the original year-end Work Plan and did not identify an activity coordinator. The revised, undated year-end Work Plan, provided four months after the beginning of the audit, properly identified the same reviewed tasks as not applicable to the Authority.

FINO should comply with CALSTARS requirements of creating and customize a year-end work plan based on Authority activities. In addition, the activity coordinator should ensure documentation is maintained to support each completed task.

Response:

Agree, FINO acknowledges that it utilizes a standard template, which is pre-populated with common, potentially necessary tasks to complete the year-end process. For FY2014-15, several tasks were not initially identified as not applicable to that fiscal year (Tasks 68, 70, 73 and 74). Rather than deleting them from the template, FINO flagged the tasks as not applicable, and therefore did not execute those tasks. FINO made additional customizations to the workplan, adding in newly required tasks, for FY2014-15. This issue has been resolved.

For FY2015-16, the Authority further customized its year-end close workplan, based specifically on FINO's activities that are FY-specific, and included the role of an activity coordinator who will continue to ensure documentation is maintained to support each completed task.

Individual Responsible: Jamey Matalka, Assistant Chief Financial Officer, Financial Office

- K. FINO did not have properly designed controls or a clear methodology surrounding the year-end GAAP (Generally Accepted Accounting Principles) adjustment. The Authority's financial information is accounted for and reported on a budgetary/legal basis (modified accrual basis according to state laws and regulations) and must be reported on a GAAP basis at year-end. The GAAP adjustment provides the standard for financial presentation and is submitted to SCO (State Controller's Office). The entry included Accounts Payable of \$17.48 Million, Due to other Funds of \$7.73 Million and Due to Other Governments of \$7.96 Million. GAAP indicates that

encumbrances should not be recognized as expenses until the goods or services are received. FINO submitted the GAAP adjustment to SCO, however, the supporting documents and methodology used to calculate the reported balance was not provided to the Audit Office.

FINO should implement controls to maintain all supporting documentation used to calculate the GAAP adjustment and to document the methodology used to determine the reported ending balances.

Response:

Agree, FINO has implemented controls to ensure that all required supporting documentation used to calculate the GAAP adjustments is maintained for all entries, adjustments, and reconciliations, based on documented policy (POLI-FIS-07, July 2015). This issue has been resolved.

FINO acknowledges that it did not provide the individual supporting documents and the detailed methodology used to calculate the reported adjustment, but instead provided a summary report that provided references. All numbers are properly supported and reviewed, there are no unverified amounts submitted to SCO.

FINO also acknowledges that it follows SCO's GAAP Basis procedural manual and maintains compliance with GAAP. FINO prepares the Year-End GAAP adjustments based on final, reconciled, and reviewed CalSTARS reports and the SCO's Budgetary Legal Basis Report. In addition, FINO confirms, in accordance with GAAP, that no Authority encumbrances were recognized as expenses. Finally, to ensure accurate GAAP adjustments, FINO reconciles encumbrances on a monthly basis.

Individual Responsible: Jamey Matalka, Assistant Chief Financial Officer, Financial Office