OFFICE OF AUDITOR OF STATE
STATE OF IOWA

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Rob Sand
Auditor of State

NEWS RELEASE

Contact: Brian Brustkern
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FOR RELEASE February 18, 2025

Auditor of State Rob Sand today released an Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters on the State of Iowa for the year ended June 30, 2024. The State of Iowa previously released its annual comprehensive financial report (ACFR) for the year ended June 30, 2024.

AUDIT FINDINGS:

Sand reported fourteen findings related to the receipt and disbursement of taxpayer funds of the State of Iowa. The findings address issues such as lack of controls over contracts, service organizations and eligibility related to the Education Savings Account (ESA) program, inaccurate financial information for the GAAP package related to Unemployment Insurance and material amounts of inventory, capital assets, accounts receivable, subscription-based information technology arrangements, unearned revenues, accounts payable, and various related footnote disclosures for financial reporting. Sand provided the State with recommendations to address each of these findings.

Five of the findings discussed above are repeated from the prior year. Each Department head has a fiduciary responsibility to provide oversight of their Department's operations and financial transactions. Oversight is typically defined as the "watchful and responsible" care one exercises in their fiduciary capacity.

A copy of the audit report is available for review on the Auditor of State's website at Audit Reports – Auditor of State.

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STATE OF IOWA

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

JUNE 30, 2024

State of Iowa

State of Iowa

Officials

Name	Title
	Executive Branch
Honorable Kim Reynolds	Governor
Kraig Paulsen	Director, Department of Management
	Legislative Branch
Amy Sinclair	President of the Senate
Pat Grassley	Speaker of the House of Representatives
Timothy McDermott	Director, Legislative Services Agency
	Judicial Branch
Susan Christensen	Chief Justice of the Supreme Court

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Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with Government Auditing Standards

To the Governor and Members of the General Assembly:

We have audited in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States, the financial statements of the governmental activities, the business type activities, the aggregate discretely presented component units, each major fund and the aggregate remaining fund information of the State of Iowa as of and for the year ended June 30, 2024, and the related Notes to Financial Statements, which collectively comprise the State of Iowa's basic financial statements, and have issued our report thereon dated December 20, 2024. Our report includes a reference to other auditors who audited the financial statements of the Tobacco Settlement Authority, the Iowa PBS Foundation, the Iowa Finance Authority, the University of Iowa Center for Advancement and Affiliate, the Iowa State University Foundation, the University of Northern Iowa Foundation and the University of Iowa Health System, as described in our report on the State of Iowa's financial statements. This report does not include the results of the other auditors' testing of internal control over financial reporting or compliance and other matters that are reported on separately by those auditors. The financial statements of the Iowa PBS Foundation, the University of Iowa Center for Advancement and Affiliate, the Iowa State University Foundation and the University of Northern Iowa Foundation were not audited in accordance with Government Auditing Standards.

Report on Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the State of Iowa's internal control over financial reporting (internal control) as a basis for designing 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 of Iowa's internal control. Accordingly, we do not express an opinion on the effectiveness of the State of Iowa's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and, therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as described in the accompanying Schedule of Findings, we identified certain deficiencies in internal control that we consider to be material weaknesses and significant deficiencies.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility a material misstatement of the State of Iowa's financial statements will not be prevented or detected and corrected, on a timely basis. We consider the deficiencies described in the accompanying Schedule of Findings as items (A)(1), (A)(2), (A)(3), (B)(1), (B)(2) and (C) to be material weaknesses.

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. We consider the deficiencies described in the accompanying Schedule of Findings as items (D)(1) through (D)(8) to be significant deficiencies.

Report on Compliance and Other Matters

As part of obtaining reasonable assurance about whether the State of Iowa's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the financial statements. 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 which are required to be reported under Government Auditing Standards.

However, we noted certain immaterial instances of noncompliance or other matters which will be reported to management in separate reports.

The State of Iowa's Responses to Findings

Government Auditing Standards requires the auditor to perform limited procedures on the State of Iowa's responses to the findings identified in our audit and described in the accompanying Schedule of Findings. The State of Iowa's responses were not subjected to the other auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on the responses.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the State of Iowa's internal control or on compliance. This report is an integral part of an audit performed in accordance with Government Auditing Standards in considering the State's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Brian R. Brustkern, CPA
Deputy Auditor of State

December 20, 2024

Findings Related to the Financial Statements:

INTERNAL CONTROL DEFICIENCIES:

(A) Education Savings Accounts (ESAs)

Iowa Department of Education

(1) Controls over Contracts

Criteria – The Students First Act was introduced by Governor Reynolds and signed into law on January 24, 2023. The bill established a framework and funding for Education Savings Accounts (ESAs), which may be used by eligible families to cover tuition, fees and other “qualified education expenses” at accredited nonpublic schools in Iowa. As defined in the legislation, “qualified education expenses” includes tuition and fees at a nonpublic school, textbooks, fees or payments for educational therapies, including tutoring or cognitive skills training, curriculum fees, software and materials for a course of study for a specific subject matter or grade level, tuition or fees for nonpublic online education programs, tuition for vocational and life skills education approved by the Iowa Department of Education, education materials and services for pupils with disabilities from an accredited provider, including the cost of paraprofessionals and assistants who are trained in accordance with state law, standardized test fees and advanced placement examinations or examinations related to postsecondary education admission or credentialing. The law requires all funds be first put towards tuition. Only after tuition is covered may they be used for other “qualified educational expenses”. The only limit on how tuition is used by private schools is they cannot provide a rebate to participants.

Chapter 257.11B.5 of the Code of Iowa also provides the Director of the Iowa Department of Education may enter into contracts with a third-party entity necessary for the administration of the program. Primary Class, Inc. dba Odyssey (Odyssey), signed a contract with the Iowa Department of Education on April 6, 2023 to administer the Educational Savings Accounts for the time period April 6, 2023 through April 5, 2026.

In addition, the agreement with Odyssey requires the Iowa Department of Education to maintain documentation for the following:

- Payment Card Industry (PCI) Data Security Standard (DSS) attestation documentation.
- Ongoing monitoring of Odyssey’s compliance with the contract.
- Semi Annual Review Meetings to review the performance of services, discuss fee and expense issues and other such issues to ensure ongoing monitoring of Odyssey.
- Alert reports of changes or problems which would negatively impact completion or performance of the work.
- Reports on unscheduled downtime on the website to monitor service level credits that shall require the Contractor to pay the State of Iowa in the event of service level failures.

U.S. Auditing Standards – AICPA (Clarified) AU-C 315 requires the auditor to perform risk assessment procedures to obtain an understanding of the components of the Department's system of internal control. The components are the control environment, the entity's risk assessment process, the entity's process for monitoring the system of internal control, the information system and communication and the control activities. Based on this understanding, the auditor is required to evaluate whether a control is designed effectively to address the risk of material misstatement at the assertion level or effectively designed to support the operation of other controls and determine whether the control has been implemented by performing procedures in addition to inquiry of the Department's personnel. These risk assessment procedures include inquiries of management and of other appropriate individuals within the Department and observation and inspection of necessary documents to support, corroborate or contradict the inquiries made of management or others. Observation and inspection may also provide information about the entity and its environment. AU-C 330 and AU-C 500 further provides obtaining evidence through inquiry should be combined with observation, inspection or other audit procedures. Inquiry alone is not sufficient audit evidence.

<u>Condition</u> – While a letter to the Office of the Auditor of State from the Director of the Department of Management provided answers to various questions asked of the Iowa Department of Education, the Iowa Department of Education did not provide the Office with documentation of the controls over the Education Savings Account (ESA) program in order for us to determine whether controls were effectively designed and implemented to determine whether only eligible students received the funding, the amount paid was proper and whether adequate meetings, discussions, reports and ongoing monitoring was performed by the Iowa Department of Education. The Iowa Department of Education also refused to provide us with various documents requested for us to document our understanding of the system of internal control and document our observation and inspection of the documents in order to test controls as deemed necessary.

Therefore, we were unable to determine whether any controls regarding the ESA program were effectively designed to support the program and whether controls had been implemented.

<u>Cause</u> – Management for the Iowa Department of Education and the State of Iowa refused to provide information and documentation as requested by the Auditor of State's Office.

In a letter from the Director of the Iowa Department of Management to the Office of Auditor of State, "As to the very last statement in the list, which speaks to the need to "make observations to verify the controls," this is unheard of in relation to an ACFR report."

<u>Effect</u> – Inadequate controls could affect the Department's ability to prevent or detect and correct misstatements, errors or misappropriation in the ESA program on a timely basis by employees in the normal course of performing their assigned functions. Inadequate controls could also affect the Department's ability to prevent or detect and correct noncompliance with the agreement with Odyssey on a timely basis by employees in the normal course of performing their assigned functions.

Recommendation – As included in AU-C 330, other audit procedures in combination with inquiry to obtain audit evidence, such as observation, is necessary to be in compliance with auditing standards. The Department should document their procedures, processes and controls over the various aspects of the ESA program and provide this documentation to the Auditor of State's Office. In addition, the Department should provide the Office of Auditor of State with information as requested for purpose of the audit.

Response – The Department disagrees with the Office of the Auditor of State ("AOS") in its determination of criteria, condition, cause, effect, and recommendation. The documentation sought in this matter related to the Education Savings Accounts ("ESA") program is beyond the scope of the engagement letter for the Annual Comprehensive Financial Report ("ACFR"). The Department, including the Department of Management and other state agencies, have repeatedly advised the AOS that unrelated program information sought under the guise of the ACFR requires a separate engagement letter pursuant to Iowa law.

AOS attempted to use the ACFR to request information outside of the ACFR on the ESA program. The information sought by AOS is, however, obtainable simply by sending an engagement letter to the Department for the ESA program. Iowa Code section 11.3 provides that an "examination commences when the period of professional engagement begins pursuant to the government auditing standards prescribed by the comptroller general of the United States and published by the United States government accountability office or as specified in Code of Federal Regulations, Title 2, Part 200."

The comptroller general of the United States has consistently recognized the importance of engagement letters. They are a written agreement that document the objectives and scope, roles and responsibilities of both management and the auditor, and detail other matters of the engagement. Rathan than submitting an engagement letter, the AOS decided to issue a finding on the Department's ACFR for the lack of production of documents related to the ESA program, and erroneously imply that there could be a lack of internal controls. To be clear, the ESA program does not lack internal controls. This approach by the AOS is disingenuous and improper.

A more concerning issue, however, is the glaring conflict of interest and extreme bias that Auditor Sand has regarding the ESA program. The Generally Accepted Government Audit Standards ("GAGAS") 3.30 instructs auditors to evaluate their own independence for bias threats and self-interest threats. A bias threat is when an auditor will, as a result of political, ideological, social, or other convictions, take a position that is not objective. A self-interest threat is when an auditor has a financial or other interest that will inappropriately influence the auditor's judgment or behavior. Examples of circumstances that create bias threats for an auditor include when there are preconceptions about the objectives of a program under the audit that are strong enough to affect the auditor's objectivity. See, e.g., GAGAS 3.40.

Auditors should be, but are not always, apolitical. Auditor Sand not only has a preconception about the ESA program, but he has spoken at length about the program, campaigned against the program, and even encouraged others to challenge the program.

There have been dozens of posts by Auditor Sand on social media attacking ESAs. For example, Auditor Sand has said:

- "The vouchers plan would give YOUR money to the wealthy" (1/15/2023)
- "vouchers as a path to ending public education" (12/28/2022)
- "Vouchers supporters want to skip checks and balances and avoid an actual cost assessment of vouchers. Tell them how bad it is" (1/12/2023)
- "Giving Iowa's private schools roughly $1,000,000,000.00 over the next few years is not the right priority" (2/10/2023)
- "the vouchers bill had 0 rules for how private schools spend your $" (4/13/2024)
- "Iowa taxpayers gave $84 million from public schools to people who could already afford private school" (1/27/2024)
- "Call them vouchers, call them ESA, whatever - just don't expect them to be successful" (8/20/2023)

It is unfortunate that Auditor Sand does not want the ESA program to be successful. These hyperbolic and overly politicized comments from Auditor Sand evidence a lack of impartiality and objectivity regarding the ESA program.

GAGAS discusses independence in paragraph 3.19. That provision states, "Auditors and audit organizations should avoid situations that could lead reasonable and informed third parties to conclude that auditors and audit organization are not independent and thus not capable of exercising objective and impartial judgment on all issues associated with conducting the engagement and reporting on the work."

The Department is aware of the rights, duties, and responsibilities of Auditor Sand as prescribed by Iowa Code Chapter 11. The Department reaffirms its opposition to Auditor Sand's determination of criteria, condition, cause, effect, and recommendation in the ACFR. The ESA program does not lack internal controls. The detailed information sought regarding the ESA program is outside the scope of the ACFR and requires a separate engagement letter to audit (by an unbiased auditor).

Conclusion – Response acknowledged. The ESA program spent approximately $104,000,000 during the year ended June 30, 2024. Under auditing standards generally accepted in the United States of America (GAAS) planning materiality is required on all engagements. The ESA program is considered a material class of transactions for the State's Annual Comprehensive Financial Report (ACFR). Under GAAS the auditor is obligated to audit the program included in the ACFR which also includes documenting proper internal controls over taxpayer funding. U.S. Auditing Standards – AICPA (Clarified) AU-C 300.07 states "The auditor should establish an overall audit strategy that sets the scope, timing, and direction of the audit and that guides the development of the audit plan." This means that the scope of the engagement is determined by the auditor, not the auditee. Therefore, the engagement letter signed for the ACFR by the Iowa Department of Administrative Services and the Iowa Department of Management encompasses this program.

The Administration's insistence on an engagement letter, and insistence that it can negotiate the scope of the audit within the letter, is a baseless attempt to deny the Auditor access to the information it needs to do its work. The auditing standards referenced in the Code of Iowa do not require an engagement letter; they contemplate several different ways an audit can begin. Notably, the Auditor's office is charged by Code of Iowa §11.2 with the duty to "annually, and more often if deemed necessary, audit the state and all state officers and departments receiving or expending state funds." Under accounting standards, this legislative directive is a "recurring engagement." The Iowa Supreme Court has explicitly held that the Auditor is not required to provide an engagement letter to initiate an audit. *Kirkwood Inst. Inc. v. Sand,* 6 N.W.3d 1, 11 (Iowa 2024), *Sand v Doe,* 959 NW 2d 99,109 (Iowa 2021).

As previously stated, AU-C 315 requires the auditor to perform risk assessment procedures to obtain an understanding of the components of the Department's system of internal control. While we were able to substantiate the dollar amount of expenditures of the ESA program, the Department withheld documentation related to internal controls over the ESA program. Under professional standards, observation or inspection are required in addition to inquiry to determine whether controls over a material class of transactions have been properly designed and implemented. Inquiry alone is not considered sufficient.

Collectively, the team members involved in this engagement and this finding have in excess of 100 years of experience, specifically dedicated to audits of governmental entities and, are independent in fact and appearance. Both this inquiry and finding were based on their professional judgment and their understanding of and compliance with GAAS. With the ESA program expected to grow to over $340,000,000 in the future, it is essential to determine if controls have been properly designed and implemented.

(2) Service Organizations

Criteria – U.S. Auditing Standards – AICPA (Clarified) AU-C 402 defines a service organization as an organization or segment of an organization that provides services to user entities that are relevant to those user entities internal control over financial reporting. Based on the contract with Primary Class, Inc. dba Odyssey (Odyssey), Odyssey is a service organization for the Iowa Department of Education for the Education Savings Accounts (ESA) program. As such, the objective of the Office of Auditor of State is to obtain an understanding of the nature and significance of the services provided by the service organization and their effect on the Iowa Department of Education's internal control relevant to the audit, sufficient to identify and assess the risks of material misstatement and design and perform audit procedures responsive to those risks.

In addition, the agreement with Odyssey requires Odyssey annually submit a copy of their Systems and Organization Controls 2 (SOC 2), type 2 report. The SOC 2 report is related to controls at a service organization which are relevant to security, availability, processing integrity, confidentially or privacy. The type 2 report is a report on management's description of a service organization's system and the suitability of the design and operating effectiveness of controls.

Condition – The Iowa Department of Education did not provide the Auditor of State's Office with this report or provide an explanation about whether the report was not obtained from Odyssey.

Cause – Management for the Iowa Department of Education did not respond to our request for a copy of the required SOC 2, type 2 report.

Effect – Inadequate controls could affect the Department's ability to prevent or detect and correct misstatements, errors or misappropriation in the ESA program on a timely basis by employees in the normal course of performing their assigned functions. Without obtaining the SOC 2, type 2 report, Odyssey has not complied with the agreement with the Iowa Department of Education, and they have not provided the required report to document there were controls in place relevant to security, availability, processing integrity, confidentially or privacy and whether those controls are operating effectively.

Recommendation – The Department should ensure Odyssey obtains the required report, in compliance with the agreement, and Odyssey provides it to the Department. This report should then be provided to the Auditor of State's Office.

Response – The Department disagrees with the Office of the Auditor of State ("AOS") in its determination of criteria, condition, cause, effect, and recommendation. The documentation sought in this matter related to the Education Savings Accounts ("ESA") program is beyond the scope of the engagement letter for the Annual Comprehensive Financial Report ("ACFR"). The Department, including the Department of Management and other state agencies, have repeatedly advised the AOS that unrelated program information sought under the guise of the ACFR requires a separate engagement letter pursuant to Iowa law.

AOS attempted to use the ACFR to request information outside of the ACFR on the ESA program. The information sought by AOS is, however, obtainable simply by sending an engagement letter to the Department for the ESA program. Iowa Code section 11.3 provides that an "examination commences when the period of professional engagement begins pursuant to the government auditing standards prescribed by the comptroller general of the United States and published by the United States government accountability office or as specified in Code of Federal Regulations, Title 2, Part 200."

The comptroller general of the United States has consistently recognized the importance of engagement letters. They are a written agreement that document the objectives and scope, roles and responsibilities of both management and the auditor, and detail other matters of the engagement. Rathan than submitting an engagement letter, the AOS decided to issue a finding on the Department's ACFR for the lack of production of the SOC 2 report related to the ESA program, and erroneously suggests that Odyssey has not complied with the agreement and has not provided the SOC 2 report. To be clear, a SOC 2 report has been provided to the Department and is in the possession of the Department. Odyssey has complied with the agreement and the request by the AOS for the SOC 2 report is beyond the scope of the ACFR.

A more concerning issue, however, is the glaring conflict of interest and extreme bias that Auditor Sand has regarding the ESA program. The Generally Accepted Government Audit Standards ("GAGAS") 3.30 instructs auditors to evaluate their own independence for bias threats and self-interest threats. A bias threat is when an auditor will, as a result of political, ideological, social, or other convictions, take a position that is not objective. A self-interest threat is when an auditor has a financial or other interest that will inappropriately influence the auditor's judgment or behavior. Examples of circumstances that create bias threats for an auditor include when there are preconceptions about the objectives of a program under the audit that are strong enough to affect the auditor's objectivity. See, e.g., GAGAS 3.40.

Auditors should be, but are not always, apolitical. Auditor Sand not only has a preconception about the ESA program, but he has spoken at length about the program, campaigned against the program, and even encouraged others to challenge the program.

There have been dozens of posts by Auditor Sand on social media attacking ESAs. For example, Auditor Sand has said:

- "The vouchers plan would give YOUR money to the wealthy" (1/15/2023)
- "vouchers as a path to ending public education" (12/28/2022)
- "Vouchers supporters want to skip checks and balances and avoid an actual cost assessment of vouchers. Tell them how bad it is" (1/12/2023)
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- "Iowa taxpayers gave $84 million from public schools to people who could already afford private school" (1/27/2024)
- "Call them vouchers, call them ESA, whatever - just don't expect them to be successful" (8/20/2023)

It is unfortunate that Auditor Sand does not want the ESA program to be successful. These hyperbolic and overly politicized comments from Auditor Sand evidence a lack of impartiality and objectivity regarding the ESA program.

GAGAS discusses independence in paragraph 3.19. That provision states, "Auditors and audit organizations should avoid situations that could lead reasonable and informed third parties to conclude that auditors and audit organization are not independent and thus not capable of exercising objective and impartial judgment on all issues associated with conducting the engagement and reporting on the work."

The Department is aware of the rights, duties, and responsibilities of Auditor Sand as prescribed by Iowa Code Chapter 11. The Department reaffirms its opposition to Auditor Sand's determination of criteria, condition, cause, effect, and recommendation in the ACFR. Odyssey has complied with its agreement. The Department is in possession of the SOC 2 report, which is outside the scope of the ACFR and requires a separate engagement letter to audit (by an unbiased auditor).

Conclusion – Response acknowledged. The ESA program spent approximately $104,000,000 during the year ended June 30, 2024. Under auditing standards generally accepted in the United States of America (GAAS) planning materiality is required on all engagements. The ESA program is considered a material class of transactions for the State's Annual Comprehensive Financial Report (ACFR). Under GAAS the auditor is obligated to audit the program included in the ACFR which also includes documenting proper internal controls over taxpayer funding. U. S. Auditing Standards – AICPA (Clarified) AU-C 300.07 states "The auditor should establish an overall audit strategy that sets the scope, timing, and direction of the audit and that guides the development of the audit plan." This means that the scope of the engagement is determined by the auditor, not the auditee. Therefore, the engagement letter signed for the ACFR by the Iowa Department of Administrative Services and the Iowa Department of Management encompasses this program. A SOC 2 report on Odyssey, the service organization, is within the scope of the ACFR as it relates to the controls relevant to security, availability, processing integrity, confidentiality or privacy. The Department's response states they are in possession of the SOC 2 report, which should be provided to the auditor.

Iowa Department of Revenue

(3) Controls over Eligibility

Criteria – Chapter 257.11B.2(a) provides for the school budget year beginning July 1, 2023, pupils who attend a nonpublic school for that school budget year shall be eligible to receive an education savings account if they are eligible to enroll in grades one through twelve and were enrolled in a nonpublic school year immediately preceding the school year for which the education savings account payment is requested if the pupil's household has an annual income less than or equal to three hundred percent of the most recently revised poverty income guidelines published by the United States Department of Health and Human Services.

The contract with Odyssey states "Contractor shall coordinate with the Iowa Department of Revenue for joint application development and/or integrations as appropriate for the purposes of income verification and program eligibility."

Condition – The Iowa Department of Revenue did not provide documentation on how they coordinated with Odyssey for income verification and program eligibility. Therefore, we were unable to determine whether there was a system of controls over income verification and program eligibility.

Cause – The Iowa Department of Revenue initially responded to inquiries stating that on face value it wasn't relevant to the ACFR. Further inquiries with the Department did not receive a response.

Effect – Inadequate controls could affect the Department's ability to prevent or detect and correct misstatements, errors or misappropriation in the ESA program on a timely basis by employees in the normal course of performing their assigned functions. Pupils whose households did not meet the income guidelines could have received education savings accounts.

Recommendation – The Department should provide documentation to the Office of Auditor of State on how income verification and program eligibility was determined and documented and how they coordinated with Odyssey in compliance with the Contractor agreement.

Response – The Department disagrees with the Office of the Auditor of State ("AOS") in its determination of criteria, condition, cause, effect, and recommendation. The documentation sought in this matter related to the Education Savings Accounts ("ESA") program is beyond the scope of the engagement letter for the Annual Comprehensive Financial Report ("ACFR"). The Department, including the Department of Management and other state agencies, have repeatedly advised the AOS that unrelated program information sought under the guise of the ACFR requires a separate engagement letter pursuant to Iowa law.

AOS attempted to use the ACFR to request information outside of the ACFR on the ESA program (i.e., documentation on how the Department coordinated with Odyssey for income verification and program eligibility). The information sought by AOS is, however, obtainable simply by sending an engagement letter to the Department for the ESA program. Iowa Code section 11.3 provides that an "examination commences when the period of professional engagement begins pursuant to the government auditing standards prescribed by the comptroller general of the United States and published by the United States government accountability office or as specified in Code of Federal Regulations, Title 2, Part 200."

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A more concerning issue, however, is the glaring conflict of interest and extreme bias that Auditor Sand has regarding the ESA program. The Generally Accepted Government Audit Standards ("GAGAS") 3.30 instructs auditors to evaluate their own independence for bias threats and self-interest threats. A bias threat is when an auditor will, as a result of political, ideological, social, or other convictions, take a position that is not objective. A self-interest threat is when an auditor has a financial or other interest that will inappropriately influence the auditor's judgment or behavior. Examples of circumstances that create bias threats for an auditor include when there are preconceptions about the objectives of a program under the audit that are strong enough to affect the auditor's objectivity. See, e.g., GAGAS 3.40.

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The Department is aware of the rights, duties, and responsibilities of Auditor Sand as prescribed by Iowa Code Chapter 11. The Department reaffirms its opposition to Auditor Sand’s determination of criteria, condition, cause, effect, and recommendation in the ACFR. The ESA program has adequate controls. The detailed information sought regarding the ESA program is outside the scope of the ACFR and requires a separate engagement letter to audit (by an unbiased auditor).

Conclusion – The ESA program spent approximately $104,000,000 during the year ended June 30, 2024. Under auditing standards generally accepted in the United States of America (GAAS) planning materiality is required on all engagements. The ESA program is considered a material class of transactions for the State's Annual Comprehensive Financial Report (ACFR). Under GAAS the auditor is obligated to audit the program included in the ACFR which also includes documenting proper internal controls over taxpayer funding. U.S. Auditing Standards – AICPA (Clarified) AU-C 300.07 states "The auditor should establish an overall audit strategy that sets the scope, timing, and direction of the audit and that guides the development of the audit plan." This means that the scope of the engagement is determined by the auditor, not the auditee. Therefore, the engagement letter signed for the ACFR by the Iowa Department of Administrative Services and the Iowa Department of Management encompasses this program. As previously stated, AU-C 315 requires the auditor to perform risk assessment procedures to obtain an understanding of the components of the Department's system of internal control. Income verification and program eligibility for the year ended June 30, 2024 was required by Chapter 257.11B.2(a) of the Code of Iowa, therefore documentation of controls over income verification and program eligibility are within the scope of the ACFR and should have been provided.

(B) Unemployment Benefits

Iowa Department of Workforce Development

Criteria – A deficiency in internal control over financial reporting exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements of the financial statements on a timely basis. Properly designed policies and procedures and implementation of the policies and procedures are an integral part of ensuring the reliability and accuracy of the financial statements.

(1) Unemployment Benefits Fund Employer Accounts

Condition – To comply with governmental accounting and financial reporting standards for the Unemployment Benefits Fund, the Iowa Department of Workforce Development (IWD) has developed the MYIOWAUI system to track employer unemployment insurance contributions based on quarterly employer payroll reports. The system generates information regarding the balance of employer contributions receivable and delinquent accounts, including penalty and interest calculations, for financial reporting purposes. This activity is reported to the Iowa Department of Administrative Services – State Accounting Enterprise (DAS-SAE) in a GAAP package.

According to IWD, an account goes to non-collectible status when the most recent debt creation date on the account is older than 720 days and the last payment was not received within 90 days. These accounts should be written off for reporting purposes and should not be included in the balance reported in the GAAP package. For the year ended June 30, 2024, $159,897 of $20,488,723 of contributions, $173,238 of $9,465,240 of interest and $16,889 of $3,351,561 of penalties older than 720 days were included in the accounts receivable balance reported in the GAAP package.

Cause – Although policies and procedures have been established to require independent review of year-end cut-off transactions to ensure financial statements are accurate and reliable, the independent review did not identify material errors in the GAAP package.

Effect – IWD employees did not detect the errors in the normal course of performing their assigned functions. As a result, material adjustments to the financial statements were necessary.

Recommendation – IWD should ensure financial information generated for the GAAP package is properly reviewed for accuracy. IWD should continue to modify the MYIOWAUI system to ensure the data is accurate, timely and conforms to established policy.

Response – We have identified an issue with our reporting where some accounts are not pulling in the data needed to determine if the uncollected debt is older than 720 days. This report is being corrected in conjunction with the UI Modernization project that is currently occurring and will begin correctly pulling data beginning in July 2025. Until the report is corrected, we have identified additional reports for the IWD Financial Management Team to use by having them pull the Contributary Report and the Non-Collectible Debt report and find the common account numbers. As this is a manual process, it will decrease the material misstatement risk that comes with the current reporting process. The Contributary Report with the Non-Collectible Debt report account numbers removed will provide the IWD Financial Management Team with the information they are looking for and provide a materially acceptable reportable value.

Conclusion – Response accepted.

(2) Unemployment Benefits Fund Reconciliation

Condition – IWD utilizes an external accounting system for processing Unemployment Insurance (UI) benefit payments to claimants, and billings and collections to and from other states for UI claimants. In addition, IWD utilizes a system to track employer unemployment insurance contributions, and each state maintains its own UI trust fund reserve built from state taxes, primarily from employers, and used only to pay for UI benefits. IWD has developed a process to reconcile the systems daily to ensure payments agree by program type and in total for financial reporting purposes. IWD has also developed procedures to maintain accurate account balances using a manual general ledger to produce a monthly trial balance for external accounting systems which is reconciled to State accounting records.

The following were noted for the year ended June 30, 2024:

(a) The manual general ledger was not maintained during the fiscal year. After year end, manual ledgers were adjusted for reporting purposes.

(b) Monthly financial statements were not prepared during the fiscal year. After year end, financial statements of the external accounts were updated for reporting purposes.

(c) Reconciliations of the manual general ledger and monthly financial statements to the State accounting records were not performed during the fiscal year. After year end, reconciliations were performed. There was no evidence of independent review or approval of the reconciliations.

Cause – Although policies and procedures are established to maintain the manual general ledger, prepare monthly financial statements and perform a reconciliation to the State accounting system, IWD did not perform these tasks during fiscal year 2024 until it was brought to their attention during the audit. As a result, IWD did not correct these errors for several months.

Effect – The lack of maintaining manual general ledgers, monthly financial activity reports and reconciliations to the State accounting system can result in unrecorded transactions, undetected errors and the opportunity for misappropriation.

Recommendation – IWD should follow policies and procedures already established to ensure the manual general ledger and monthly financial activity is maintained. In addition, monthly reconciliations should be performed and variances between the systems should be investigated and resolved timely.

Response – The Department acknowledges these critical ledgers, reports, and reconciliations were not maintained throughout state fiscal year 2024. IWD did not have a Chief Financial Officer to provide oversight to the unit for a majority of the fiscal year in order for this to occur. During the GAAP reporting and audit process, IWD worked with both the GAAP Team and the Auditor's Office to ensure that it has the detail it needs in order to maintain and reconcile these ledgers for subsequent fiscal years.

Conclusion – Response accepted.

(C) Reconciliation of Unemployment Insurance Billings, Collections and Delinquent Accounts

Iowa Department of Workforce Development

Criteria – An effective internal control system provides for internal controls related to maintaining delinquent account listings, reconciling Unemployment Insurance (UI) overpayment billings, collections and delinquent accounts and comparing UI overpayment collections to deposits to ensure proper recording of UI overpayment receipts, the propriety of adjustments and write-offs and the propriety of delinquent account balances.

Condition – UI overpayment billings, collections and delinquent accounts were reconciled monthly throughout the year and a delinquent accounts listing was prepared. However, the reconciliation performed showed unexplained variances between the ending of one month and the beginning of the next month. Reconciliations were subsequently corrected, and the activity was reported to DAS-SAE in a GAAP package. Although policies and procedures have been established to require independent review of the reconciliation, no evidence exists that the review was performed.

Cause – Policies have not been established and procedures have not been implemented to investigate variances in the monthly reconciliations of the UI overpayment billings, collections and delinquent accounts and UI overpayment collections to deposits.

Effect – This condition could result in unrecorded or misstated UI overpayment receipts, improper or unauthorized adjustments and write-offs and/or misstated delinquent account balances.

Recommendation – A listing of delinquent accounts should be prepared on a monthly basis. Procedures should be established to investigate variances in the reconciliation of UI overpayment billings, collections and delinquent accounts for each billing period and collections to deposits. The Department designated independent person should review the reconciliation and monitor delinquents. The review of the reconciliation should be documented by the signature or initials of the reviewer and the date of the review.

Response – Each month when there is a variance between the ending of one month and the beginning of the next month, when IWD Financial Management is reconciling the UI overpayments billings, collection and delinquent accounts, the team member from Financial Management will work with the Benefits Collection Manager to determine what is causing the variances. This will be initiated by an email from the team member in IWD Financial Management and we can provide copies of the emails that took place during the last year.

Conclusion – Response accepted.

(D) Financial Reporting

Criteria – A deficiency in internal control over financial reporting exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements of the financial statements on a timely basis. Properly designed policies and procedures and implementation of the policies and procedures are an integral part of ensuring the reliability and accuracy of the State's financial statements.

Departments record receipts and disbursements in the Iowa Advantage system throughout the year, including the accrual period. Activity not recorded in the Iowa Advantage system is reported to the Iowa Department of Administrative Services – State Accounting Enterprise (DAS–SAE) in a GAAP package. Departments submit their GAAP packages to DAS–SAE by the first week of September each year.

(1) Iowa Department of Administrative Services

Condition – The Department overstated depreciation related to buildings and improvements by $283,187,840. This amount was properly adjusted for reporting purposes.

Cause – Although policies and procedures are in place to review GAAP package information, the review did not identify the misstatement.

Effect – The amount reported as buildings and improvements depreciation was misstated.

Recommendation – The Department should implement additional procedures to ensure information reported in the Department's GAAP package is accurate.

Response – The Department of Administrative Services has a process in place to review reconciliations. In this instance it was an administrative oversight and the Department will conduct additional training to ensure all steps are followed.

Conclusion – Response accepted.

(2) Iowa Economic Development Authority

Condition – The Authority overstated contractual commitments by $488,001.

Cause – Although policies and procedures are in place to review GAAP package information, the review did not identify the misstatements.

Effect – The amount reported for contractual commitments was misstated.

Recommendation – The Authority should implement additional policies and procedures to ensure information reported on the GAAP package is accurate.

Response – This error occurred on a specific program fund and was due to the primary reviewer including an award twice. It was picked up on the obligation control log and then again on an email detailing out several recaptures of awards on this program. While it was a mistake on the primary review, the information on recaptures was not provided to the secondary reviewer. The Authority will ensure all documentation for its' contractual commitments are provided to all necessary fiscal staff to provide for a more thorough review.

Conclusion – Response accepted.

(3) Iowa Department of Revenue

Condition – The Department understated amounts reported on the GAAP package for Subscription-Based Information Technology Arrangements (SBITA). The SBITA assets were understated by $36,117,998 and current year amortization was overstated by $1,001,557. These amounts were properly adjusted for reporting purposes.

Cause – A portion of one of the contracts qualifying as SBITA was excluded from the GAAP package. Although policies and procedures are in place to review GAAP package information, the review did not identify the misstatements.

Effect – The amounts reported for SBITA were misstated.

Recommendation – The Department should implement effective policies and procedures to ensure information reported on the GAAP package is accurate.

Response – The expense was classified as an intangible asset in previous fiscal years. The Department agrees with the GAAP Team that it should be classified as a SBITA asset, and will do so for future reports.

Conclusion – Response accepted.

(4) Iowa Department of Workforce Development

Condition – The following conditions were noted for the Unemployment Insurance Trust Fund:

(a) The Department understated the allowance for taxes receivable by $3,507,334, resulting in the net receivable being overstated by the same amount. This was properly adjusted for reporting purposes.

(b) The Department overstated interest and penalty on accounts receivable and the related allowance by $7,443,825 and $1,910,075, respectively. This was properly adjusted for reporting purposes.

(c) The Department understated wage claims benefits receivables by $1,210,925. This was properly adjusted for reporting purposes.

Cause – Although policies and procedures are in place to review GAAP package information, the review did not identify the misstatements.

Effect – The amounts reported for accounts receivable were misstated requiring adjustments to the financial statements.

Recommendation – The Department should implement effective policies and procedures to ensure information reported to DAS-SAE on the GAAP package is accurate.

Response – The Department went through an unprecedented turnover rate of its' financial management staff, including its Chief Financial Officer during state fiscal year 2024. This resulted in many new and current staff who were completing the GAAP package for the first time – as the majority had not been exposed to this in prior years. The IWD Finance Team worked with both the GAAP Team and the Auditor's Office to identify instances where inefficiencies and inaccuracies exist in the GAAP reporting process. The IWD Financial Management Team made sure to flag these inefficiencies and inaccuracies to ensure that repeat errors do not occur in future reporting periods.

Conclusion – Response accepted.

(5) Iowa Department of Justice (Attorney General)

Condition – The Department understated accounts receivable related opioid settlement agreements by $107,535,531. This amount was properly adjusted for reporting purposes. In addition, $1,041,431 of anti-trust settlement funds were incorrectly coded as opioid settlement funds.

Cause – Although policies and procedures are in place to review GAAP package information and deposit classifications, these reviews did not identify the misstatements.

Effect – The amounts reported for accounts receivable for the opioid settlement agreements were misstated and funds deposited for an anti-trust settlement were miscoded as opioid settlement funds.

Recommendation – The Department should implement effective policies and procedures to ensure information reported on the GAAP package is accurate. The Department should also implement procedures to ensure all deposits are classified correctly.

Response – Staffing changes occurred at a critical time during the end of the fiscal year close-out. The Department of Justice will ensure all accounts receivables are reported on our GAAP package going forward. The Department will also ensure anti-trust settlement funds are properly coded in the future.

Conclusion – Response accepted.

(6) Iowa Department of Public Defense

Condition – The following conditions were noted:

(a) The Department overstated the amount of capital assets reclassified from construction in progress to buildings and improvements by $8,499,347. This was properly adjusted for reporting purposes.

(b) The Department understated buildings and improvements accumulated depreciation by $1,330,376. This was properly adjusted for reporting purposes.

(c) The Department understated construction in progress additions by $9,755,525. This was properly adjusted for reporting purposes.

(d) The Department understated capital asset additions by $273,494, understated capital asset deletions by $33,367 and overstated the gain on sale of capital assets by $11,717. These were not adjusted for reporting purposes.

Cause – Although policies and procedures are in place to review GAAP package information, the review did not identify the misstatements.

Effect – The amounts reported for capital assets were misstated requiring adjustments to the financial statements.

Recommendation – The Department should implement effective policies and procedures to ensure information reported to DAS-SAE on the GAAP package is accurate.

Response – The Department of Public Defense Accounting Manager accepted a position outside the Department of Public Defense in May 2024, and the GAAP package for state fiscal year 2024 was completed by a new state employee. These errors are due to a new team member and a need for additional training. As issues have been identified, a review of the GAAP package has been ongoing, errors corrected, and training coordinated with the DAS team for future submissions.

Conclusion – Response accepted.

(7) Iowa Department of Transportation

Condition – The following conditions were noted:

(a) The Department understated unearned revenues by $4,681,082. This was properly adjusted for reporting purposes.

(b) The Department understated sales revenue from the disposal of capital assets by $1,646,100. This was properly adjusted for reporting purposes.

(c) The Department overstated accounts receivable by $1,076,211 due to an error when transferring accounting data to a new system. This was not adjusted for reporting purposes.

(d) The Department understated accounts payable by $41,456,078 and understated the related accounts receivable by $20,138,534. During testing, the auditor discovered one transaction totaling $962,295 that was recorded to the incorrect fiscal year. After Department staff were notified of the error, they were able to determine that there were multiple transactions incorrectly coded, and the total misstatement was identified. These were properly adjusted for reporting purposes.

(e) The Department overstated construction commitments by $2,218,999 and overstated other contractual commitments by $8,496,728. These were properly adjusted for reporting purposes.

(f) The Department misstated amounts reported for Subscription-Based Information Technology Arrangements (SBITA). General Fund SBITA assets and accumulated amortization were overstated by $1,677,659 and $1,879,820, respectively. In addition, amortization expense was overstated by $324,892, principal expense was understated by $41,790, interest expense was overstated by $38,525 and the SBITA liability was overstated by $1,734,350. Internal Service Fund SBITA accumulated amortization was understated by $16,227. These were not adjusted for reporting purposes.

Cause – Although policies and procedures are in place to review GAAP package information and system activity, the review did not identify the misstatements.

Effect – The amounts reported were misstated and required adjustments to the financial statements.

Recommendation – The Department should implement effective policies and procedures to ensure that all financial reporting is accurate.

Response – The Department believes it has the appropriate policies and procedures in place to ensure sound internal controls for this purpose. The issues noted above resulted from human errors related to new GASB standards, grant processes the Department had no experience with, and the implementation of accounting systems that altered internal procedures.

The Department acknowledges that these items were inaccurate, as noted by the auditor, but emphasizes that all discrepancies were corrected prior to the publication of the state financial statements. To address these findings, the Department has taken steps to provide additional training to staff involved with the new systems, processes, and standards. This training aims to enhance their ability to accurately identify and resolve issues during review processes, ensuring these matters have been effectively addressed moving forward.

Conclusion – Response accepted.

(8) Iowa Department of Transportation

Condition – The Department is required to submit financial information related to inventory on hand as of June 30, 2024. The Department is not reporting fuel and salt as inventory.

Cause – Policies and procedures adopted by the Department do not include fuel and salt as items reported as inventory.

Effect – The amount reported for inventory is not accurate.

Recommendation – The Department should implement procedures to ensure inventory amounts are being accurately reported.

Response – In fiscal year 2022, the Department revised accounting policies to only include materials stored in the Department central warehouse as a part of the Department inventory and eliminated material stored at field locations.

Fuel – The Department removed fuel from inventory in accordance with the fiscal year 2022 inventory policy change. Salt – The Department stores salt in field locations, as a result salt was not reported as inventory in alignment with the accounting policy change in fiscal year 2022.

Additionally, since the Department's fuel storage tanks lack automated reporting for on-hand quantities, expensing fuel upon delivery ensures consistent and accurate reporting for the fiscal year based on delivered and invoiced amounts without relying on manual measurements of tank level to produce estimates of on-hand quantities.

Conclusion – Response acknowledged. The Department should implement procedures to ensure inventory amounts at all locations are being accurately reported.

INSTANCES OF NONCOMPLIANCE:

No matters were noted.