State of Rhode Island

Findings and Management Comments

Resulting from the Audit of the State of Rhode Island's Fiscal 2024 Financial Statements

David A. Bergantino, CPA, CFE

Auditor General

State of Rhode Island

General Assembly

Office of the Auditor General

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March 21, 2025

Finance Committee of the House of Representatives
Joint Committee on Legislative Services, General Assembly
State of Rhode Island

We have audited the financial statements of the State of Rhode Island (State) for the year ended June 30, 2024 and have issued our report thereon dated March 21, 2025 in the State's Annual Comprehensive Financial Report for fiscal 2024.

As required by *Government Auditing Standards*, we have also prepared a report, dated March 21, 2025, and included herein, on our consideration of the State's internal control over financial reporting, its compliance with certain provisions of laws, regulations and contracts, and other matters required to be reported by those standards. That report includes identification of control deficiencies that are significant deficiencies or material weaknesses in internal control over financial reporting as well as instances of material noncompliance. Our findings related to the financial statements are categorized below:

- 27 findings considered significant deficiencies or material weaknesses in internal control over financial reporting; including findings reported by the auditors of component units (legally separate entities included within the State's financial statements).

- 1 finding concerning compliance or other matters required to be reported by *Government Auditing Standards*.

This communication also includes 11 management comments resulting from our audit of the financial statements which are less significant issues that still warrant the attention of management.

Our *Single Audit Report* for fiscal 2024 is in progress and is scheduled to be completed later this year. That report will include findings related to controls over compliance with federal program requirements and the administration of federal programs.

The State's management has provided their planned corrective actions relative to these findings and management comments, which have been included herein.

Sincerely,

David A. Bergantino, CPA, CFE
Auditor General

FINDINGS AND MANAGEMENT COMMENTS

AUDIT OF THE STATE OF RHODE ISLAND'S FISCAL 2024 FINANCIAL STATEMENTS

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EXECUTIVE SUMMARY

Material weaknesses in internal control continue to cause material misstatements and omissions within the State's financial reporting. Audit procedures have led to the detection and correction of an excessive amount of material errors and omissions indicative of a need to improve internal controls over financial reporting, including the adoption of quality control procedures. The State needs to meet its responsibilities for financial reporting by implementing quality control procedures that significantly improve its accuracy and completeness.

Failure to record State debt and related expenditure activity, accounting errors and omissions which materially misstated General Fund operating results by $83.6 million, and note disclosure omissions for significant commitments and contingencies are examples in support of the need for improved controls over financial reporting.

Management's responsibility for implementing and maintaining a system of internal control is foundational to ensure complete and accurate financial reporting, compliance with federal regulations, and safeguarding assets of the State. This responsibility is defined in State statutes and federal requirements. RI General Law section 35-14-3, *Agency Responsibilities*, under the State's Financial Integrity and Accountability statutes, mandates that "State agency heads are responsible for the establishment and maintenance of a system or systems of internal accounting and administrative control within their agencies. This responsibility includes: (1) documenting the system; (2) communicating the system requirements to employees; and (3) assuring that the system is functioning as prescribed and is modified, as appropriate, for changes in conditions."

Management focus, training, and implementation resources have been insufficient to ensure that departments and agencies are assessing and documenting internal control consistent with management's overall responsibility for the adequacy of its design and operation. Internal controls safeguard public resources and support accurate financial reporting. The State should commit to providing additional training and implementation materials to assist departments and agencies in documenting their internal control. An internal control assessment and documentation effort should be implemented.

The State's current accounting and financial reporting system lacks the integration, functionality, and controls of a comprehensive Enterprise Resource Planning (ERP) system. The lack of integration has led to various manual processes being implemented over time which are prone to error and lack compensating controls to ensure accurate and complete financial reporting.

Weaknesses identified in the State's internal control over financial reporting result from our annual audit of the State's financial statements for the year ended June 30, 2024. The State's management has responsibility for, and maintains internal control over, financial reporting. *Government Auditing Standards* require that we communicate deficiencies in internal control over financial reporting and material noncompliance based on our audit. Twenty-eight (28) findings included herein represent issues required to be reported under those standards. Findings repeated from prior years are identified.

The complexity of Medical Assistance (Medicaid) program operations adds to the challenge of accurately accounting for all Medicaid financial activity within the State's financial statements. This complexity increases each year through new federal regulations, complex managed care contract settlement provisions, new State initiatives, and continued challenges relating to the State's integrated human services eligibility system (RIBridges). Medicaid is the State's single largest activity – approximating $4.0 billion in expenditures or approximately 40% of the State's General Fund expenditures. The State will need to ensure that the design of the next Medicaid Management Information System will provide the functionalities needed to enhance controls over program operations and fiscal oversight.

Controls are lacking to ensure the completeness and accuracy of reported accruals and year-end adjustments relating to the Medicaid program in conjunction with the State's fiscal closing.

The State can improve controls over recording federal revenue to ensure (1) amounts are consistent with the limitations of grant awards from the federal government and (2) federally claimed expenditures are consistent with amounts recorded in the State's accounting system.

The State must continue to improve its consideration of controls over functions performed by external parties through enhanced use and documentation of Service Organization Control (SOC) reports. These improvements are necessary and consistent with management's responsibility for the overall adequacy of the design and operation of internal control.

Controls over the preparation of the Schedule of Expenditures of Federal Awards (SEFA) can be enhanced to ensure all program activity, including amounts passed through to subrecipients, is accurately reported by Assistance Listing Number.

The complexity of Treasury operations has increased substantially over the years without significant modifications to the State's investment in technology and personnel to support those efforts and to ensure internal control best practices are maintained.

There is an excessive volume of journal entries recorded within the accounting system. This volume weakens controls over the appropriate authorization and classification of expenditures and limits transparency regarding the underlying transactions.

Controls over the identification and reporting of leases and subscription-based information technology arrangements (SBITAs) applicable to GASB Statements No. 87 and No. 96 were insufficient to ensure all applicable agreements were properly recorded.

Control deficiencies continue to result in significant misstatements in amounts reported in the Intermodal Surface Transportation Fund financial statements. Internal controls must be improved to ensure consistent and accurate financial reporting.

Controls over the identification of transportation infrastructure assets need further improvement to ensure accuracy and completeness. Controls should be improved to record the disposal of infrastructure assets when retired, replaced, or permanently impaired.

The State continues to assess its current cybersecurity readiness, including identifying risk mitigation priorities. Information systems security resources remain insufficient for the size and complexity of State operations and risk mitigation is not progressing quickly enough.

The State's current practices for periodic logical access and privilege reviews at both the application and network levels need improvement. Practices for database logging and monitoring at the database level also need improvement.

There are multiple products used for security information event monitoring, and not all are properly tracked within ticketing and knowledge-based systems. Consolidation of multiple product views, integration with the ticketing system and maturation of Security Orchestration, Automation, and Response (SOAR) playbooks are desperately needed.

In addition to findings that impact Statewide controls over financial reporting and information systems security, our report includes findings specific to the Rhode Island State Employees' and Electing Teachers OPEB System and Employees' Retirement System of Rhode Island.

Our report includes control deficiencies and material noncompliance reported by the independent auditors of the discretely presented component units included within the State's financial statements. Their accounting and control procedures are generally independent of the State's control procedures.

Our report also includes 11 management comments that highlight opportunities for enhancement of financial-related operational, policy or accounting control matters.

The scholarship disbursement function of the RI Division of Higher Education Assistance does not merit administration as a separate financial reporting entity and these activities should be accounted for within the State's General Fund rather than as a discretely presented component unit.

The legacy systems utilized by the RI Department of Labor and Training (DLT) to process unemployment benefits, temporary disability insurance, and employer taxes have reached end-of-life and pose significant business continuity risks to DLT operations.

The State needs to further enhance its coordination and training to improve its incident response capabilities in the event of a data breach.

The State does not currently account for non-monetary unclaimed property remitted to the General Treasurer in accordance with generally accepted accounting principles. While the Office of the General Treasurer's (Treasury) Unclaimed Property Division maintains an inventory of remitted property, it does not assess and report fair value for the property held and a physical inventory of unclaimed property has not been performed in some time.

Management's response to the findings and comments, including planned corrective actions, are detailed in our report.

INDEPDENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS

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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*

Finance Committee of the House of Representatives and
Joint Committee on Legislative Services, General Assembly,
State of Rhode Island

We have audited, in accordance with the 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 Rhode Island (the State), as of and for the year ended June 30, 2024, and the related notes to the financial statements, which collectively comprise the State's basic financial statements, and have issued our report thereon dated March 21, 2025. Our report includes a reference to other auditors who audited the financial statements of:

- the Tobacco Settlement Financing Corporation, a blended component unit which represents less than 1% of the assets and deferred outflows and the revenues of the governmental activities and less than 1% of the assets and 1% of the revenues of the aggregate remaining fund information;

- the Convention Center Authority, a major fund, which represents 23% of the assets and deferred outflows and less than 2% of the revenues of the business-type activities;

- the Ocean State Investment Pool, an investment trust fund, and the HealthSource RI Trust, Rhode Island Higher Education Savings, and ABLE private-purpose trust funds, which collectively represent 21% of the assets and 22% of the revenues, including additions, of the aggregate remaining fund information; and

- all the component units comprising the aggregate discretely presented component units.

This report includes our consideration of the results of the other auditors' testing of internal control over financial reporting and compliance and other matters that are reported on separately by those other auditors. However, this report, insofar as it relates to the results of the other auditors, is based solely on the reports of the other auditors.

Report on Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the State'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's internal control. Accordingly, we do not express an opinion on the effectiveness of the State'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 and responses, we and the other auditors did identify 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 that a material misstatement of the entity'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 and responses to be material weaknesses: Findings 2024-001, 2024-002, 2024-004, 2024-005, 2024-006, 2024-008, 2024-009, 2024-014, 2024-015, and 2024-017. Other auditors of the discretely presented component units considered the deficiency in the accompanying schedule of findings and responses to be a material weakness: Finding 2024-028.

A *significant deficiency* is a deficiency, or 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 and responses to be significant deficiencies: Findings 2024-003, 2024-007, 2024-010, 2024-011, 2024-012, 2024-013, 2024-016, 2024-018, 2024-019, 2024-020, 2024-021, 2024-022, and 2024-023. Other auditors of the discretely presented component units considered the deficiencies in the accompanying schedule of findings and responses to be significant deficiencies: Findings 2024-025, 2024-026 and 2024-027.

Report on Compliance and Other Matters

As part of obtaining reasonable assurance about whether the State'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 the tests performed by other auditors disclosed an instance of noncompliance that is required to be reported under *Government Auditing Standards* and which is described in the accompanying schedule of findings and responses as Finding 2024-024.

State's Response to Findings

Government Auditing Standards requires the auditor to perform limited procedures on the State's responses to the findings identified in our audit and described in the accompanying schedule of findings and responses. The State'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 entity'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 entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

David A. Bergantino

David A. Bergantino, CPA, CFE
Auditor General
March 21, 2025

SCHEDULE OF FINDINGS AND RESPONSES

INTERNAL CONTROL OVER FINANCIAL REPORTING

STATEWIDE

AUDIT STANDARD:

Management is responsible for a.) the preparation of the financial statements in accordance with generally accepted accounting principles and b.) the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Finding 2024-001 **_(material weakness – repeat finding – 2023-009)_**

INTERNAL CONTROL DEFICIENCIES CAUSING MATERIAL MISSTATEMENTS AND OMISSIONS IN THE STATE'S FINANCIAL REPORTING

Material weaknesses in internal control continue to cause material misstatements and omissions within the State's financial reporting. Audit procedures have led to the detection and correction of an excessive amount of material errors and omissions indicative of a need to improve internal controls over financial reporting, including the adoption of quality control procedures.

Background: Audits in recent years have led to the identification of a significant number of material misstatements and omissions in the State's financial reporting that required correction. During the fiscal 2024 audit, material misstatements within the State's financial reporting continued, resulting in net operating results in the General and Intermodal Surface Transportation (IST) major funds to be materially misstated by $83.6 million and $10.4 million, respectively.

Most of these misstatements and the lack of their detection can be linked to specific control deficiencies which have remained unresolved for too long. In recent years, turnover in several key finance and accounting positions statewide has only reinforced the need for better consideration and documentation of internal control to prevent misstatements in the State's financial reporting.

Criteria: Management is responsible for the preparation and fair presentation of the financial statements in accordance with generally accepted accounting principles. Management is also responsible for the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error. Financial reporting consistency is critical to the comparability of financial results over time.

Condition: The State lacks sufficient oversight, monitoring, and accountability within its current practices to ensure accurate and complete financial reporting. Shared responsibilities exist between individual agencies, who are responsible for preparing adjustments at the fiscal close, and the Office of Accounts and Control (OAC), who is responsible for financial reporting. The shared responsibilities among these entities continue to result in material misstatements in the financial statements and a lack of accountability for financial reporting. Examples of material misstatements and omissions that support the need for improved controls over financial reporting include:

a) *Omission of $93 million in State-appropriation backed revenue bonds* – The State failed to account for this transaction in the draft financial statements because the related cash flows did not follow the State's normal procedures for general obligation debt. This transaction is an example where management most knowledgeable and involved in the transaction resides within the State's Office of Management and Budget (OMB), and processes to ensure that the information necessary for the OAC to account for and disclose the transaction properly are lacking.

b) *Understatement of personal income tax revenue accrual* – The estimation of tax revenue and refund accruals is heavily reliant on data reported by the Division of Taxation (Taxation). Taxation provides reports to the OAC who records the necessary accrual entries. Personal Income Tax revenue was understated by $43.3 million due to miscommunication between the two departments. The lack of quality control procedures, including the review and approval of fiscal closing results by agency management, is leading to significant undetected misstatements in financial reporting.

c) *Significant journal entries made in error during the fiscal close* – Several material journal entries (impacting reported expenditures) were recorded backwards during the fiscal close. Since significant journals are reviewed by senior financial management at the department level and financial reporting staff at the OAC, it raised concerns that designed controls over journal entries were not operating effectively during the fiscal close. Such errors further support the lack of financial oversight where many of the errors could have been identified when year-end results were inconsistent with caseload conference testimony provided in May 2024.

d) *Audit adjustments were required to ensure the consistency of financial reporting between periods* – The State misclassified certain material transactions that required adjustment to ensure consistency with prior period financial statements. Examples included, but were not limited to, 1) interfund transfers reported as current expenditures, 2) current expenditures reported as debt service expenditures, and 3) incorrect recording of revenue sources (general vs. restricted).

e) *Omission of significant matters requiring note disclosure* – The State needs to improve procedures to ensure that significant matters are disclosed. Draft notes for commitments and contingencies are often not updated appropriately and omit newer items of significance to the State's primary government.

f) *Budgetary Comparison Schedules* – Draft schedules for required major funds continue to include errors and omissions needing correction.

Cause: In addition to a variety of internal control deficiencies impacting specific transaction types which are detailed in Finding 2024-004 in this report, the State has several control deficiencies at the financial reporting level that need to be addressed. These deficiencies include the following:

a) *Lack of quality control review for financial reporting* – While the OAC has statutory responsibility for financial reporting (e.g., fiscal closing reports, draft financial statements), those most knowledgeable about key financial transactions and agency finances reside in OMB or within the management of the various agencies and departments of State government. A lack of a comprehensive review of the State's financial reporting by OMB and departmental senior accounting staff currently represents a significant deficiency in the oversight and monitoring required to ensure accurate and complete financial reporting.

b) *Controls over journal entry transactions* – The State relies on designed transaction approval hierarchies to ensure that significant transactions receive reviews by both management at the departmental level and financial reporting staff at the OAC prior to posting. This important control was not found to be effective in ensuring that journal entries recorded were accurate, as a significant number of incorrect journal entries that materially impacted financial reporting went undetected and uncorrected.

Effect: Material misstatements, misclassifications, and omissions in the financial statements going undetected.

RECOMMENDATIONS

2024-001a Enhance the State's quality control process over financial reporting by requiring review of detailed fiscal closing reports by the OMB and senior agency financial managers prior to finalizing the fiscal closing.

2024-001b Reinforce accountability for journal entry approvals with senior agency finance managers. Consider whether significant journal entries should be reviewed by agency budget specialists within OMB prior to posting.

Management's Views and Corrective Actions:
2024-001a: Prior to the release of this report, the Office of Accounts and Control and the Office of Management and Budget begun regular meetings to discuss activities that have a significant impact on financial reporting.

2024-001b: The implementation of the Enterprise Resource Planning software (ERP) improves the daily business processes and improves controls over approvals of financial transactions. The ERP will require agency staff to be the first control point over accuracy of financial transactions with Accounts and Control and Office of Management and Budget being second- and third-line control points respectfully.

Anticipated Completion Dates:
2024-001a: Completed
2024-001b: July 1, 2025

Contact Person: *Dorothy Pascale, State Controller, Department of Administration, Accounts and Control*
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Finding 2024-002	***(material weakness – repeat finding – 2023-001)***

COMPREHENSIVE DOCUMENTATION OF THE STATE'S INTERNAL CONTROL STRUCTURE

Management focus, training and implementation resources have been insufficient to ensure that departments and agencies are assessing and documenting internal control consistent with management's overall responsibility for the adequacy of the design and operation of internal control. Internal controls safeguard public resources and support accurate financial reporting.

Background: The State's management has responsibility for the design and operation of internal control. The Committee of Sponsoring Organizations (COSO) has designed a framework for internal control that consists of three categories of objectives – *operations, reporting, and compliance* – and five components – *control environment, risk assessment, control activities, information and communication, and monitoring*. The Government Accountability Office's "Green Book" – *Standards for Internal Control in the Federal Government* tailors this conceptual framework to the public environment. The Green Book is required for federal agencies and is useful to other governments when applying the principles of an internal control framework.

Criteria: RI General Law section 35-14-3, *Agency responsibilities*, under the State's Financial Integrity and Accountability statutes, mandates that "State agency heads are responsible for the establishment and maintenance of a system or systems of internal accounting and administrative control within their agencies. This responsibility includes: (1) Documenting the system; (2) Communicating the system requirements to employees; and (3) Assuring that the system is functioning as prescribed and is modified, as appropriate, for changes in conditions."

An internal control framework, such as COSO and/or the Green Book, provides an overall structure for management to design, document, and monitor its internal control policies and procedures. Both within and outside government, management has responsibility for the adequacy of the design and operation of an entity's control structure. A complete consideration of internal control, in addition to documenting control policies and procedures, must also include how the policies are communicated, documentation of risks associated with financial reporting and operations, and monitoring of those documented controls to ensure their effectiveness.

Federal regulations, 2 CFR 200.303(a) *Internal controls*, require recipients (i.e., the State) to "establish, document, and maintain effective internal control over the Federal award that provides reasonable assurance that the recipient or subrecipient is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should align with the guidance in "Standards for Internal Control in the Federal Government" issued by the Comptroller General of the United States or the "Internal Control-Integrated Framework" issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO)."

Condition: The majority of agency and Statewide policies and procedures are not documented and administered in the manner that is required by statute, federal regulations, or professional standards (COSO, Green Book). While certain control policies and processes have been documented, there is a lack of formalized documentation and comprehensive internal control structure throughout State government that complies with an accepted framework such as COSO and/or the Green Book. To meet the intended standards, internal control (policies and procedures) must be documented, periodically evaluated, and revised based on updated risk assessments, effectively communicated to employees (through training if necessary), and monitored for effectiveness by the agency. Formalized documentation of internal controls relating to statewide functions (i.e., accounting, procurement, payroll) is a needed first step that will allow agencies to expand on and supplement with their agency-specific policies and procedures relating to critical program functions. Since each State agency has unique programs and procedures that supplement statewide functions, internal control consideration and documentation must also be performed at the agency level, as required by statute.

With the State implementing an integrated ERP system, which will require substantial modification of certain processes and related controls, it is critical that internal controls are evaluated and documented consistent with an acceptable framework. Such an exercise will be vital to ensure that the new ERP and its related configuration and workflow processes provide adequate internal control over the core functions of the new system (e.g., human resources, procurement, accounting and financial reporting, disbursements, etc.). An opportunity exists with the ERP implementation for a coordinated effort to document a comprehensive system of internal control that meets an acceptable framework and to reassess the design of its current control structure (both statewide and at the individual agency level) with emphasis on risk assessment and monitoring - both essential components of internal control.

Cause: Management focus, training and implementation resources have been insufficient to ensure that departments and agencies are adequately documenting their internal control structures based on an accepted framework such as COSO and/or the Green Book. Most agencies would need significant assistance to document and implement a system of internal control that meets the requirements of RI General Law section 35-14-3, *Agency responsibilities*.

Effect: Errors, omissions or noncompliance could go undetected by management due to inadequate design and/or monitoring of internal controls. Continued noncompliance with statutory requirements for agency documentation of internal control.

RECOMMENDATIONS

2024-002a Implement an internal control framework, such as COSO or the Green Book, and commit additional resources, including training and implementation materials, to ensure that departments and agencies are adequately documenting their internal controls accordingly.

2024-002b Ensure that internal controls over financial reporting include documentation of risk assessments, control activities that mitigate identified risks, and monitoring controls to ensure compliance with policies and procedures adopted in conjunction with the new ERP system.

Management's Views and Corrective Actions:
2024-002a: Management has explored the engagement of a consultant to assist in the enterprise-wide documentation of internal controls since agency resources do not possess the knowledge or time to perform this task at a level that would address this audit finding. The estimated cost of this endeavor is between $3 and $5 million. Until the funding for this is provided, controls will be documented as noted in 2024-002 (b) below.

2024-002b: The ERP implementation brings an opportunity to embed internal controls within the software application. The ERP implementation is creating documentation for decisions regarding new business processes and improved internal controls over financial activities. These decision documents include options presented by system implementor, reason the option was selected, a workflow of business process. Agency management will need to ensure their finance teams are well versed in the internal control structure embedded in the system with the assistance of the ERP vendor.

Anticipated Completion Dates:
2024-002a: To be determined; dependent on funding.
2024-002b: Ongoing.

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Finding 2024-003 **_(significant deficiency – repeat finding – 2023-002)_**

EVALUATION OF CONTROLS OVER FUNCTIONS PERFORMED BY EXTERNAL PARTIES

The State must continue to improve its consideration of controls over functions performed by external parties through enhanced use and documentation of Service Organization Control (SOC) reports. These improvements require State agencies (the "user entities") to document and review complementary user entity controls designated in those SOC reports which the service organization assumes are in place and operating effectively for proper and secure use of the contracted entity's services. This consideration is necessary and consistent with management's responsibility for the overall adequacy of the design and operation of internal controls.

Background: SOC reports are provided by service organizations (i.e., vendors, contractors) to assure customers/clients that controls are sufficiently designed and in operation over the contracted services they provide (e.g., data processing, claims payment, fiduciary activities). Management of the user entity should use these reports as part of their overall consideration and documentation of the adequacy of the design and operation of internal control. Management should also ensure that their complementary user entity controls (user entity controls) are documented and reviewed to ensure that they are operating effectively. Ineffective user entity controls limit the usefulness of SOC reports when documenting an entity's financial and operational controls as those reports assume that user entity controls are operating effectively.

To provide an example of the significance of financial operations involving service organizations, benefit disbursements by the State's Medicaid fiscal agent and human services eligibility and benefits system represent approximately 36% of the State's General Fund expenditures. Service organizations are currently involved, to some degree, in most finance-related functions of State government. The use of service organizations has increased over time, and will likely continue to, as more services are being administered through cloud-based applications.

The State has made progress by training employees and implementing a uniform SOC report assessment tool to document the consideration of controls at its service organizations. Centralized monitoring by the Office of Accounts and Control has improved agency compliance with obtaining and providing a standard evaluation of the SOC reports by agency personnel.

Criteria: Management has responsibility for the adequacy of the design and operation of an entity's control structure including functions performed by external parties. This responsibility also includes documenting and reviewing designated user entity controls, which the service organization assumes are in place and operating effectively for the proper and secure use of the contracted entity's services.

Condition: Management's identification of key service organization controls (reported in SOC reports) and their importance to mitigating risks associated with critical programmatic and financial reporting functions are lacking as follows:

- Agencies are not always identifying when SOC reports should be requested from contractors, especially for new services or when contractors change.

- User agency documentation of key SOC controls within that agency's internal control documentation is currently deficient. As indicated in Finding 2024-002, most State agencies lack formalized documentation of internal control, thus management consideration and documentation of how SOC reports are utilized to mitigate operational risks is equally deficient.

- Documentation and testing of user entity controls at the agency level are frequently lacking. These controls are assumed to be operational by the auditor of the service organization when providing an opinion on the effectiveness of the entity's internal controls. Each agency (user entity) must ensure that relevant user entity controls identified by service organizations are also in place and operating effectively. Such control considerations should be included in the documentation and evaluation of internal controls discussed in Finding 2024-002.

When SOC reports identify exceptions, evaluation of such matters must be timely and thorough. Any highlighted deviations in control testing that may result in a qualified opinion regarding the design and effectiveness of certain control procedures at the service organization, as well as user entity control considerations, should be documented, reviewed, and thoroughly vetted. For fiscal 2024, documentation obtained from State agencies utilizing service organizations was incomplete or insufficient regarding the evaluations of the exceptions and the impact on the State's overall operational controls. While SOC reports evaluate whether service organizations are following their described internal controls, agencies are ultimately responsible for evaluating the adequacy of those controls based on the operational risks inherent in the services being provided.

Cause: The lack of comprehensive documentation and consideration of (1) service organization controls and (2) user entity controls by agencies relying on service organizations to perform critical functions for State government represent a weakness in internal control over financial reporting. In addition, insufficient documentation and review of user entity controls limit the related assurance that can be placed on control objectives reported within SOC reports.

Effect: Many functions performed by external parties are material to the State's overall operations. Deficiencies in the design or operation of controls at service organizations could materially impact the State's overall controls over financial reporting and compliance.

RECOMMENDATIONS

2024-003a For user entity (State agency) controls identified within SOC reports, document and evaluate the agency controls to ensure that they are in place and operating effectively.

2024-003b Incorporate agency reliance on control objectives documented and reviewed in SOC reports, in addition to the documentation of related complementary user entity controls, within the agency's formal documentation of internal controls over program operations.

2024-003c Improve documentation of SOC report results, including consideration and mitigation of service organization control deficiencies reported.

Management's Views and Corrective Actions:
The DOA provided training to agency staff, redesigned the review form based on previous year's audit finding. Accounts and Control will monitor agency review of the SOC Type I reports. The SOC Type II reports will be centralized within ETSS who will review on behalf of the agency.

Anticipated Completion Date: December 30, 2025

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Finding 2024-004 ***(material weakness – repeat finding – 2023-003)***

INTERNAL CONTROL DEFICIENCIES INHERENT IN THE STATE'S CURRENT FINANCIAL REPORTING AND ADMINISTRATIVE FUNCTIONS

The State's financial reporting process includes significant manual processes that lack the compensating controls necessary to ensure accurate and complete financial reporting. Most misstatements detected in the State's financial reporting process are the result of manual processes subject to error or the omission of transaction recording.

Background: The State's current systems supporting key financial and administrative functions lack integration and represent risks to the State's business continuity due to their age and dwindling technical support. The lack of integration and functionality has also created several deficiencies in internal control over financial reporting and inefficiencies throughout financial and administrative processes. The State further lacks the types of compensating controls such as monitoring and reconciliation procedures that could detect material misstatements in financial reporting.

The State currently plans utilization of its new ERP system in fiscal 2026 that will include the human capital (human capital management, human resources management, talent management, etc.) and finance (financial management, payroll, analytics and reporting, etc.) modules to significantly improve the integration and functionality of its financial reporting systems.

Criteria: Management needs well-designed financial systems that support comprehensive internal controls over financial reporting, enable organization-wide efficiencies, and promote business continuity. Integrated functionalities support appropriate internal controls, and eliminate inefficiencies resulting from multiple systems, duplicate data entry and ineffective communication between systems.

Condition: Important functionalities are minimally met through legacy systems, the existing statewide accounting system, and multiple departmental processes without intended integration and efficiencies. This results in business continuity risk, decreased efficiency and effectiveness, and control weaknesses. Some of the State's critical systems utilize outdated technology which makes these operations vulnerable from a business continuity and systems security perspective. Certain legacy systems utilize software that is no longer supported and the availability of skilled personnel to work on these systems is limited.

The design and limitations of the State's current financial system have resulted in numerous control deficiencies, collectively representing a material weakness over financial reporting. The following control deficiencies have the most significant impact on the State's controls over financial reporting:

- *General ledger access* – Effective accounting systems restrict general ledger access to those individuals knowledgeable about the State's accounting and financial reporting. The current system allows wide access to the general ledger which results from recording cash receipts through journal entries rather than a cash receipts module. This significantly increases the risk of accounting errors being made and not being detected in a timely manner. This design also creates a large volume of journal entry transactions which is difficult to manage with the State's limited centralized accounting and financial reporting staff.

- *Recording accruals during the fiscal close* – The State currently relies on the manual accumulation of accruals (except for system generated accounts payable) as part of their fiscal closing process. These manual processes are more likely to omit or misstate the recording of accruals as the process lacks effective controls to ensure the completeness and accuracy of recorded amounts. Compensating controls to identify unrecorded accruals have not proven effective in ensuring that all material transactions are recorded.

- *Recording financial activity from subsidiary systems* – Financial activity processed, and in certain situations disbursed, by subsidiary systems often prevents detailed transaction data from being reported in the accounting system. In addition, reconciliations of subsidiary systems to the State accounting system to verify the completeness and accuracy of summarized data reported in the State accounting system are lacking for significant transaction groups.

- *Federal revenue and expenditure reporting* – With the majority of the State's expenditures being funded by federal grants, controls over their reporting are material to the State's financial reporting. The State's accounting system does not meet the State's needs in three important and interrelated areas relating to the reporting of federal revenue and expenditures – time reporting/payroll, grants management, and cost allocation – all functionalities that are integral to the management of federal programs. These functions are currently performed independent of the State accounting system and generally through multiple departmental systems - most of which are duplicative and utilize old and sometimes unsupported technology. Because these systems and processes are decentralized, they do not ensure that federal expenditures are only reported when available grant award authority exists and that federal expenditures are recorded in the proper period due to delays in cost allocation results being reflected in the accounting system.

- *Capital projects reporting* – The State currently tracks capital projects using Excel. Project costs are accumulated in Excel and reported as construction in progress before being reclassified to the proper capital asset category upon completion. This process is inefficient and lacks the controls that a fully integrated capital projects module would provide.

- *Payroll / Personnel Administration* – The State still utilizes carbon-copy paper-based forms to administer payroll for its employees. Forms require manual input into multiple systems which is inefficient and prone to error. During our audit, a high percentage of payroll forms authorizing current employee pay levels could not be located to support the current salary amounts paid during the year. While summary payroll data gets recorded in the accounting system, the lack of an integrated personnel and payroll system requires a high volume of inefficient journal entries to allocate personnel to the appropriate programs and funding sources.

The State has devoted significant financial and personnel resources to the implementation of a new ERP system with the goal of addressing the control deficiencies outlined in this finding. These internal control deficiencies will continue to impact the State's financial reporting until a more integrated and modernized ERP system is implemented.

Cause: The State relies on manual processes for certain critical accounting functions due to a lack of integration, functionality, and controls within the current accounting system. The lack of integration has led to various manual processes being implemented over time which are prone to error and lack compensating controls to ensure accurate and complete financial reporting.

Effect: Business continuity risks, deficiencies in internal control over financial reporting, and the lack of organization-wide efficiencies exist and are exacerbated due to the lack of an integrated ERP system.

RECOMMENDATIONS

2024-004a Manage the business process re-engineering required to align the State's processes to the software-as-a-service functionalities within the ERP system.

2024-004b Ensure that the new ERP system addresses identified internal control deficiencies relating to financial reporting.

Management's Views and Corrective Actions:
Accounts & Control agrees that the current accounting system lends to manual processes and increases the risk of errors. This is one of the main drivers for the implementation of the ERP system which is underway. Refer to 2024-002 above for more detail.

Anticipated Completion Date: Refer to 2024-002 above for detail.

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Finding 2024-005	***(material weakness – repeat finding – 2023-005)***

MEDICAID PROGRAM COMPLEXITY AFFECTS FINANCIAL REPORTING AND OVERALL PROGRAM CONTROLS

The continued and growing complexity of Medicaid program operations, coupled with the insufficient support of the State's antiquated Medicaid Management Information System, adds to the challenge of accurately accounting for all Medicaid program related financial activity within the State's financial statements.

Background: The complexity of the Medicaid program increases each year through new federal regulations, complex managed care contract settlement provisions, new State initiatives, and continued challenges relating to the State's integrated human services eligibility system, RIBridges. Medicaid is the State's single largest program activity – approximating $4.0 billion in expenditures or approximately 40% of the State's General Fund expenditures. Consequently, the financial aspects of this program are material to the State's financial reporting objectives. Expenditures for individuals covered under managed care approximated $2.1 billion, representing the majority of benefit expenditures reported for Medicaid.

Criteria: Management of the Executive Office of Health and Human Services (EOHHS) is responsible for establishing and maintaining internal control over financial reporting to ensure accurate and complete reporting of transactions in accordance with generally accepted accounting principles.

Condition: Ensuring all financial activity is properly and completely recorded in the State's financial statements is an increasingly complex task. Significant Medicaid program activity is currently being accounted for external to the systemic controls and processes designed within the Medicaid Management Information System (MMIS). The MMIS was developed as a claims processing system over 30 years ago and was not designed to meet the current processing and reporting needs of the State's managed care programs. Managed care requires a system that can handle capitation adjustments and a more robust adjudication of encounter data submitted by the State's contracted managed care organizations (MCOs). While the MMIS has been modified over time to handle the disbursement of capitation and the submission of encounter data, it lacks the functionality to completely process and account for managed care activity.

The following were examples of control deficiencies relating to Medicaid financial activity, some of which led to material misstatements requiring audit adjustments to correct financial reporting:

- Manual tracking of amounts due to and from managed care organizations are subject to error or omission. Our audit procedures identified an outstanding receivable of $4.5 million due to the State Medicaid Program from one of the managed care organizations which EOHHS believed had been previously recovered. Audit procedures also identified an unrecorded liability totaling $3.7 million for outstanding managed care premiums due to a managed care organization for enrolled newborns;

- Payments to and recoupments from providers and managed care organizations, each totaling more than $300 million, were disbursed through system and manual transactions processed by the fiscal agent with authorization by the State Medicaid agency. These payments are not subjected to the claims processing controls of the MMIS and often require substantial manual calculations to determine the transaction amounts. These transactions (except for manual payments) are netted within the normal claims processing cycle activity and the MMIS lacks sufficient reporting capability for these transactions. EOHHS currently lacks procedures to ensure that only authorized payments are processed. During fiscal 2024, the volume of payment and recoupment transactions were significant (more than 700 transactions) and individual system payout transactions often exceeded $100,000 (approximately 251 individual payments in 2024); and

- The MMIS's limited ability to process capitation adjustments and to process and report on encounter data makes it very difficult to estimate accruals relating to managed care. The State Medicaid agency currently relies on plan reporting from the MCOs to estimate final contract settlements requiring accrual at year-end. The accuracy of the data provided, the run-out period for providers to continue submitting claims, and the lack of complete encounter data reported in the MMIS remain challenges in accruing accurate managed care settlements at year-end.

While EOHHS's manual procedures are making every attempt to accurately and completely settle and account for its managed care activities, systemic controls do not currently support those efforts, and control deficiencies continue to impact the State's financial reporting. With the State currently exploring procurement for a new MMIS, significant focus should be placed on ensuring that controls over managed care capitation and claiming activity are significantly improved. In the near term, the State should look to utilize federally required audit procedures to improve controls over segments of the managed care settlement process that are currently not being validated.

Cause: The State does not currently have a system that can process retroactive capitation rate changes and/or changes in participant enrollment category. The current MMIS performs limited edits in encounter data submitted by the plans that are no longer adequate for the size and volume of medical claims covered under capitation. Insufficient system reporting for system payouts and recoupments increases the risk that material transactions are not identified that require reporting as prior period activity on federal reports and for financial reporting. The extent to which system payouts are not individually recorded in the State accounting system increases the risk that these transactions are not accounted for properly, as they bypass the State's centralized review procedures designed to ensure that transactions are recorded in the correct accounts and reflected in the correct fiscal period. The State's manual tracking of amounts due to or from managed care organizations is inadequate to ensure the tracking and settlement of these amounts.

Risks relating to inaccurate financial reporting and federal noncompliance have increased due to the length of settlement periods, eligibility discrepancies between the claims payment system and the State's integrated eligibility system, retroactive capitation adjustments, and the volume of transactions being accumulated and evaluated independent of regular program controls.

Effect: Potential effects of this control deficiency include unrecorded or inaccurately recorded financial transactions, incorrect reimbursements to providers or managed care organizations, and noncompliance with federal regulations.

RECOMMENDATIONS

2024-005a Develop specific objectives for managed care data processing (i.e., premium and encounter data processing functionality) that will be required of and included in the specifications for the next MMIS.

2024-005b Minimize instances where material financial activities are reliant on manual processes to ensure proper financial reporting.

2024-005c Develop comprehensive reporting and reconciliation procedures for system payouts, manual disbursements, and system recoupments to improve controls over these transactions which are processed by the Medicaid fiscal agent.

2024-005d Improve controls over non-claims based financial transactions in the next MMIS to provide for individual reporting and proper financial accounting treatment.

Management's Views and Corrective Actions:
2024-005a: EOHHS has, in conjunction with our MES Planning Vendor, documented the existing MMIS processes for premium payments, capitations, and encounters as well as the "To Be" state of these processes in the modernized and modularized MES via assessment of business needs. Additionally, a Gap Analysis was prepared to ensure needs were identified and incorporated accordingly into the procurement(s) for replacement systems that will perform in alignment with Rhode Island-specific needs and have the flexibility to achieve the Programs' objectives in these areas.

Anticipated Completion Date: *Ongoing*

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2024-005b: EOHHS is aware of many of the risks associated with the manual processes as it pertains to its financial activities. Some are these manual processes—such as retroactive active manual payments—are a necessary condition of continued use of the State's legacy MMIS; while other manual payments are a desirable feature of our contractually defined risk share arrangements and revenue maximization strategies. Related to these processes in the system, these requirements are being factored into the development of requirements for the RFP to procure the Core Module, of which Financial Management functions will be a part, for our MES. The steps taken to-date and future strategies to simplify Medicaid-related financial activities, improve financial reporting, and enhance oversight are outlined below:

1. ***Manual Capitation Payments***

   Retroactive adjustments to the rates are a frequent occurrence in Medicaid, but such retroactive adjustments may necessitate a manual payment that creates a risk of error. Such retroactive adjustments may be attributed to enrollment changes impacting individual clients or resulting from rate changes impacting all members enrolled in a product.

   In general, the need to do manual adjustments is caused by the limited ability for EOHHS' legacy MMIS to retroactively reprocess/correct prior months of premium payments. For EOHHS' monthly premium programs (i.e., Rhody Health Partners, Medicaid Expansion, CMS Demonstration, Rite Smiles, PACE, and Non-Emergency Transportation), MMIS can correct payments made within a three-month window – retroactively for the prior month and the current month and prospectively for the future month. And for EOHHS's daily program (i.e., RIte Care), MMIS can only prospectively adjust the rates.

   For individual clients, two exceptions to these limited processing windows were incorporated to allow for the system to retroactively make adjusting payments in two scenarios:

   1. *Payments going back to a newborns'* ***Date of Birth****; and.*
   2. *Recoupments going back to a recipients* ***Date of Death****.*

These two scenarios contribute to the highest number of retroactive adjustments aside from rate changes. Any corrections outside of the systematic adjustment windows or aside from the Newborn and Death causes must still be processed manually.

With respect to rate changes, EOHHS has attempted to limit the need to make retroactive payments. During FY 2020, EOHHS developed an internal MCO contract project charter and workgroup with the goal of ensuring that capitation rates would be completed timely and ensure that amendments are signed and that any new contracted rates are in the system at the start of the year, or soon thereafter to minimize any manual payments.

However, in recent fiscal years—including every SFY between 2022 and 2025—initiatives included in the enacted state budget that impact the rates have not passed until June. Such initiatives must be subsequently incorporated into the actuarially certified rates for either the current (or even prior fiscal years). This process is not immediate. And the timeline for the enacted budget and subsequent rate certification is largely out of EOHHS' control. Resulting delays can lead to large manual payments. While some states may update its rates within MMIS without final state budgets or signed contracts, EOHHS has assessed that this creates its own risk and that the current approach is preferred.

Modern MMIS systems (including those deployed by Gainwell in other states) can reprocess such rate changes through the system, negating the need for a manual payment. Until such system upgrades are implemented, payments associated with a retroactive rate change will remain a manual payment. However, As EOHHS works to modernize and modularize the current MMIS, EOHHS' has incorporated into our planning activities inclusion of requirements to allow for systematic processing of both retroactive enrollment changes impacting individual clients (e.g., for newborns and the deceased) as well as for general rate changes impacting entire populations.

2. ***Risk Share/Gain Share Settlements and Stop Loss Programs***

Across its core contracts, EOHHS has long-maintained risk share arrangements with its MCOs. In FY 2025, EOHHS implemented a temporary separate risk share arrangement specific to the new CCBHC program. EOHHS ended its separate Hepatitis C stop loss program in FY 2022 and its separate Covid-19-related vaccine stop loss program in FY 2024. Any costs associated with Covid-19 vaccinations or Hepatitis C are not incorporated into the general risk share arrangements.

MCO risk share settlements are based on MCO submitted reporting and validated against accepted encounter claims in the MMIS. In FY 2020, the state implemented a requirement that the MCOs report quarterly through a new "Financial Data Cost Report" (FDCR) their membership, benefit expenses, including general ledger adjustments, sub-capitated arrangements, reinsurance arrangements, reserves, benefit expense recoveries and administrative costs for each Premium Rating Group. These expenses are reported at either the rate cell and category of service level, or at the product level (Rite Care/Expansion, etc.). The state uses various financial reporting from the MCOs to validate their risk share reporting, including:

- *Annually, the MCOs must reconcile the information in its FDCR to their NAIC financial statements.*
- *EOHHS utilizes this FDCR data in rate setting as well as to monitor MCO financial performance throughout the year.*
- *EOHHS began utilizing the FDCR reporting for risk share settlement beginning with the final reconciliation for FY 2019.*

EOHHS' risk share arrangements are an important component of its contracts and generally minimize risk to both the MCOs and the State. And so long as they state continues to include such risk-mitigating mechanism in its contracts, any associated settlement will necessarily remain a manual payment.

3. ***State Directed Payments***

Rhode Island incorporates many state directed payments (SDPs) into its managed care contracts. These include legislative mandated rate increases (e.g., for hospitals and nursing facilities) and minimum fee schedules (e.g., annual changes to the FQHC PPS encounter rate, OHIC rate increases). But they also include SDPs with separate payment terms—for example, the AE Incentive Payments, LTSS alternative payment mechanism (APM). These separate payment terms ended in SFY 2024. Most recently—and most significantly—Rhode Island passed an SDP for hospitals in SFY 2024.

These separate payment terms allow the State to be very precise in how much and to whom payments are made. But as a result, these separate payment terms are intentionally paid outside of the capitation *payment system and so necessarily involve a manual calculation and manual payment. However, by FFY 2027 it is expected that such separate payment terms will no longer be allowed, with all such SDP needing to be incorporated into the monthly premium payments.*

Anticipated Completion Date: Ongoing

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2024-005c: In December 2019, EOHHS and the fiscal agent implemented a monthly report recapping all Fiscal Agent Control Notes (FACNs) processed that month. EOHHS Finance also maintains a monthly log of all FACNs it approves. EOHHS is also reviewing the documentation required when FACNs are submitted for payment or recoupments, including how requests document Federal authorities in place. Most recently, Medicaid Finance created a managed care FACN tracker to ensure that staff preparing these FACNs check that all pertinent items, including backup Excel files, fund sources, and provider IDs are included in the FACN. The tracker also mandates a second reader to ensure accuracy.
EOHHS has also implemented "ServiceNow" with their fiscal agent for the purpose of more formally tracking system issues, incidents, password resets. The fiscal agent is in the process of testing functionality for non-financial FACNs, and the financial FACN and system modification request will be implemented at a later date. This tool will eliminate the FACN process as it is defined presently. To the extent that additional codes are needed to clarify the nature of various transactions, EOHHS will work with the fiscal agent to establish and utilize these new codes on a go-forward basis within the new ServiceNow tool. Due to the complexity of having a one stop "ServiceNow" center, this project is still in progress. Remaining ServiceNow functionality should be implemented by June 2024.
Medicaid will develop procedures to ensure proper reconciliation of reconciliation procedures for system payouts, manual disbursements, and system recoupments

Anticipated Completion Date: Ongoing

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2024-005d: EOHHS, in conjunction with our MES Planning Vendor, is evaluating the existing non-claims based MMIS financial transactions and reason codes and has documented the current business processes related to this work as well as the "To Be" state of those processes in the modernized and modularized MES. To ensure these business needs are met, a Gap Analysis has been prepared related to the Financial Management work and that analysis will be incorporated accordingly into the procurement(s) for replacement systems that will perform in alignment with Rhode Island-specific needs and/or have the flexibility to achieve the Programs' objectives in these areas.

Anticipated Completion Date: Ongoing

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Finding 2024-006	*(material weakness – repeat finding – 2023-006)*

CONTROLS OVER ACCRUALS AND YEAR-END ADJUSTMENTS RELATING TO THE MEDICAID PROGRAM

Controls are lacking to ensure the completeness and accuracy of reported accruals and year-end adjustments relating to the Medicaid program in conjunction with the State's fiscal closing.

Background: Receivables and liabilities relating to the Medicaid Program at year-end totaled $150 million and $288 million, respectively.

Criteria: Management is responsible for establishing and maintaining internal control over financial reporting to ensure accurate and complete reporting of transactions in accordance with generally accepted accounting principles. Generally accepted accounting principles require that expenditures are recorded in the correct financial period and, when necessary, estimates can be recorded by management to ensure the completeness of financial reporting.

Condition: The estimation, calculation, and reporting of year-end accruals is an entirely manual process involving no systemic controls to ensure the accuracy and completeness of reported amounts. Accruals for certain benefit expenditures and recoveries associated with the Medicaid program were misstated at June 30, 2024. In addition, certain year-end adjustments recorded at June 30, 2024 were incorrect, significantly misstating reported expenditures. Material audit adjustments were required to:

- Correct a fiscal closing adjustment recorded by the Department of Children, Youth, and Families that understated health and human services expenditures and related federal revenue by $17.7 million;

- Reduce managed care expenditures by $24.7 million for revised estimates of managed care settlements associated with managed care contracts that were initially misstated due to the use of incomplete data available at year-end;

- Reduce drug rebate receivables recorded at June 30, 2024 by $6.7 million for an error in estimation;

- Correct the calculation and recording of prepaid managed care premiums (capitation) at June 30, 2024 which was understated by $11.1 million;

- Reduce expenditures for privately operated providers of services to developmentally disabled individuals by $4 million relating to an overstated accrual estimate;

- Correct the funding sources of health and human services expenditures due to five (5) journal entries omitted or recorded in error at June 30, 2024. The net impact of these audit adjustments shifted $23.0 million in general revenue expenditures to federal or restricted revenue sources; and

- Record or adjust other omitted or misstated liabilities that resulted in a net understatement of expenditures of $3.4 million at June 30, 2024.

Cause: Most year-end closing adjustments and accruals are subject to management review and approval at the agency level and the Office of Accounts and Control prior to being posted in the State accounting system. This dual review and approval process is a critical control over financial reporting and was found to be ineffective in detecting a significant number of material errors in fiscal 2024. In addition, EOHHS's process for identifying and determining outstanding accruals at year-end continues to be prone to error and misstatement.

Effect: Omissions and misstatements in the recording of adjusting journal entries and year-end accruals are resulting in material misstatement of the financial statements.

RECOMMENDATIONS

2024-006a Improve overall review processes for material journal entries to ensure complete and accurate financial reporting.

2024-006b Improve procedures over the identification and determination of prepaid expenditures, receivables, and liabilities relating to the Medicaid program to ensure complete and accurate recording at year-end.

Management's Views and Corrective Actions:

2024-006a: The Auditor General noted the following issues, which EOHHS has bucketed into three categories below:

1. ***Medicaid Finance Errors:***
    - *Correct the funding sources of health and human services expenditures due to five (5) journal entries omitted or recorded in error at June 30, 2024. The net impact of these audit adjustments shifted $23.0 million in general revenue expenditures to federal or restricted revenue sources*
    - *Correct the calculation and recording of prepaid managed care premiums (capitation) at June 30, 2024 which was understated by $11.1 million*
2. ***Sister Agency Misstatements:***
    - *Correct a fiscal closing adjustment recorded by the Department of Children, Youth, and Families that understated health and human services expenditures and related federal revenue by $17.7 million;*
    - *Reduce expenditures for privately operated providers of services to developmentally disabled individuals by $4 million relating to an overstated accrual estimate*
3. ***Impact of Claims Timing:***
    - *Reduce managed care expenditures by $24.7 million for revised estimates of managed care settlements associated with managed care contracts that were initially misstated due to the use of incomplete data available at year-end.*
    - *Reduce drug rebate receivables recorded at June 30, 2024 by $6.7 million for an error in estimation.*
    - *Record or adjust other omitted or misstated liabilities that resulted in a net understatement of expenditures of $3.4 million at June 30, 2024.*

The corrective action plans for items one (1) and two (2) are detailed below in the response to 2024-006(b). Regarding item three (3):

While EOHHS uses the most complete data available at year-end to prepare its accrual entries, certain expenditure categories inherently contain significant uncertainty, due to timing and therefore absence of data and not the estimation methods themselves. It is because of this known limitation with data availability that EOHHS partners with the Office of the Auditor General and Accounts and Control in the months following fiscal close to propose revisions to its accruals that incorporate more recent available data. Two such areas are highlighted in the finding:

- *Pharmacy Rebates: As of 6/30, EOHHS's fiscal intermediary has just issued invoices to drug manufacturers for pharmacy claims with service dates through 3/31. This delay stems from the time required for health plans to adjudicate claims, transmit them to EOHHS via the encounter data submission process, and have them accepted into the State's MMIS. Only after MMIS acceptance can our fiscal intermediary invoice manufacturers for rebates. Consequently, EOHHS must estimate:*
    - *Outstanding collections for invoices issued through 3/31--with almost no collections yet received, as of the close of the fiscal year, for the third quarter.*
    - *Invoiced and collection amounts for the quarter ending 6/30 for pharmacy claims with service dates between 4/1 and 6/30.*
- *Risk Share: Complete expenditure data for risk share arrangements is not available at year-end. As of 6/30, health plans have not paid and are unaware of all claims for dates of service through 6/30. As a result, the accrual for risk share tends to be the most volatile and challenging to predict given the potential changes between what the health plans expect and assume for reserves in their quarterly reporting to EOHHS and what eventually transpires.*

EOHHS will explore ways to reduce this volatility in future accruals, which may include applying discounts to plan-reported incurred but not paid (IBNP) reserves to attempt to control for conservatism in health plan-reporting. Note that risk share/gain share payment/recoupment is necessary because the actuarially certified rates were "incorrect." Understanding the precise magnitude of that error requires continued refinement and completeness of the health plan's claims data, any collection of re-insurance payments or supplemental rebates, among other adjustments to a plan's benefit expenses. EOHHS acknowledges the importance of *issuing financial statements that comply with generally accepted accounting principles and thus welcomes suggestions for improvements to its methodological approaches to reduce the volatility in these areas.*

2024-006b: EOHHS concurs with the findings related accrual errors and misstatements and is committed to rectifying these issues. The Medicaid Director prioritized the creation of standard operating procedures (SOPs) for the fiscal year close by assigning staff in Medicaid's Executive Administrative and Support Services division to work with the Medicaid finance team. They drafted standard operating procedures for end of year accruals and end of year journal entries. These SOPs include a listing of common accruals, staff members assigned to their preparation, and second readers to ensure accuracy of accruals. Second readers will be assigned to review the work of the individual analyst and to second read the file submitted to Accounts and Control, double checking that debits and credits are correctly stated by comparing the file to be sent to original analyst workbooks. The team will also compare the current accrual list to the prior year's list and common accruals in the SOP, including those submitted by BHDDH and DCYF.

<u>Anticipated Completion Date</u>: Ongoing

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Finding 2024-007 ***(significant deficiency – repeat finding – 2023-007)***

<u>CONTROLS OVER PREPARATION OF THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS</u>

Controls over the preparation of the Schedule of Expenditures of Federal Awards (SEFA) can be enhanced to ensure all program activity, including amounts passed through to subrecipients, is accurately reported by Assistance Listing Number.

Criteria: 2 CFR 200.510(b) states "The auditee must also prepare a schedule of expenditures of Federal awards for the period covered by the auditee's financial statements which must include the total Federal awards expended as determined in accordance with §200.502".

The preparation of an accurate SEFA is critical to ensuring the proper recording of federal revenue and expenditures in the financial statements and to ensure that the State can comply with federal Uniform Guidance (2 CFR Part 200) when submitting the State's *Single Audit Report* required by federal regulations.

Condition: While federal expenditures are reported accurately in the State accounting system based on disbursements for most federal programs and the State as a whole, adjustments are still needed, especially for a statewide Single Audit that also includes federal expenditures of component units, to ensure that expenditures are accurately reported on the SEFA. Several adjustments to expenditures, reported in the State accounting system, were necessary to accurately report the federal expenditure activity for fiscal 2024:

- *Disaster Grants – Public Assistance (administered by the Federal Emergency Management Agency) (97.036)* – Under generally accepted accounting principles, disaster grant federal revenue cannot be recognized until the underlying expenditures are approved by FEMA. The FEMA approval is deemed to be the underlying requirement for revenue recognition. Thus, recognition of the federal expenditures can lag the actual fiscal period in which the expenditures are incurred. Expenditures reported had to be increased by $23.8 million for amounts awarded by FEMA in fiscal 2024 that related to expenditures incurred in prior periods.

- *Medical Assistance Program (93.778)* – In accordance with provisions in the State's section 1115 waiver, the State receives federal match for certain Designated State Healthcare Program (DSHP) expenditures when incurred. Those proceeds must be utilized to fund the State match for certain Healthcare Systems

Transformation Programs (HSTP). HSTP expenditures from restricted DSHP funding totaled $8.5 million in fiscal 2024 and required addition to reported federal expenditures on the SEFA.

- *Other Adjustments (Multiple Programs)* – Adjustments totaling $21.7 million were needed to prevent duplication of reported federal expenditures for amounts passed through to component units that are included in the State's financial reporting entity. In addition, we identified and adjusted certain federal accounts with reported expenditures totaling $15.3 million in the State accounting system that were linked to incorrect federal programs.

In addition to adjustments for the primary government's federal expenditures, the State does not adequately review and monitor reported federal expenditures of the discretely presented component units. Such monitoring and oversight are necessary to ensure proper reporting as Rhode Island submits a *Single Audit Report* for the entire financial reporting entity. The State also needs to improve its accumulation of required note disclosures that accompany the SEFA to ensure compliance with federal Uniform Guidance requirements.

Cause: There is a disconnect between the agency personnel responsible for accurate recording of federal expenditures in the SEFA and the Office of Accounts and Control, the agency that prepares the SEFA from the accounting system.

Effect: Without correction, the SEFA would not accurately present federal expenditures with required note disclosures in accordance with the Uniform Guidance requirements.

RECOMMENDATION

2024-007 Ensure policies and procedures for presenting the SEFA and required note disclosures are consistent with Uniform Guidance requirements.

Management's Views and Corrective Actions:
The Department of Administration Office of Grants Management has begun addressing this finding prior to the issuance of this report. A new process to create and report the State Expenditure of Federal Awards (SEFA) is underway. The new business process will use information from the ERP and Grant Management System intended to result in a more accurate and timely reporting.

Anticipated Completion Date: Ongoing

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Finding 2024-008	***(material weakness – repeat finding – 2023-008)***

CONTROLS OVER FEDERAL PROGRAM FINANCIAL ACTIVITY

The State must improve controls over recording federal revenue to ensure (1) amounts are consistent with the limitations of grant awards from the federal government and (2) claimed expenditures on federal reports are consistent with amounts recorded in the State's accounting system.

Background: Federal programs represented 45% of fiscal 2024 General Fund expenditures. Financial reporting risks include categorizing expenditures as federally reimbursable when grant funds have either been exhausted or the expenditures do not meet the specific program requirements. Further, the State can improve its overall centralized monitoring of federal program operations to ensure compliance with federal regulations.

Some federal grants are open-ended entitlement programs where the federal government will reimburse the State for all allowable costs incurred under the program. Other federal grants are limited by a specific award amount and grant period. These grant periods are often for the federal fiscal year and are not aligned with the State's fiscal year.

The State utilizes a cloud-based Grants Management System (eCivis) to manage several federal grant functions. During fiscal 2024, the State began requiring most subrecipient payments to be authorized through eCivis prior to being processed for payment through the State accounting system. This process, while an improvement of controls over disbursements to subrecipients, represents the only integrated use of the eCivis with the State accounting system.

Criteria: Federal revenue and expenditures recorded by the State must be consistent with the limitations of grant awards from the federal government and claimed expenditures on federal reports must be consistent with amounts recorded in the State's accounting system.

Condition: Knowledge of grant requirements, spending authorizations, and limitations on reimbursable expenditures all rest with departmental management who administer the federal grant programs. The Office of Accounts and Control, in preparing the State's financial statements, relies primarily on the coding of expenditures (by funding source – federal) within the RIFANS accounting system. All expenditures recorded in federal accounts are considered reimbursable from the federal government and federal revenue is accrued to match unreimbursed expenditures at year-end. From an overall statewide perspective, controls over financial reporting are ineffective to ensure that all federal expenditures are reimbursable and federal revenue is recognized appropriately. In addition, procedures designed to ensure the consistency of federal expenditures reported in RIFANS (the source of the State's SEFA) with those reported on federal reports were deemed ineffective and discontinued.

With the State's new ERP system expected to become operational in fiscal 2026, focus has been on ensuring a more complete integration of eCivis with the new ERP system. That integration will need to ensure that the following internal control deficiencies relating to federal program financial activity are addressed:

- *Controls are not currently effective to ensure that federal expenditures are only recognized when sufficient federal grant authority exists* – Federal expenditures should only be recognized if eCivis reports sufficient federal grant authority at the time of the transaction. The effectiveness of this interface will require agencies to delineate the applicable grant period when processing transactions in the accounting system to be fully effective.

- *Controls to ensure that federal expenditures are reported consistent with allocation processes approved by the federal government are currently lacking* – Since the new ERP system will not include an integrated cost allocation function, agencies will need to utilize the new ERP system to more accurately allocate costs to federal programs (using time reporting and purchase order allocations functions). If utilized properly, the periodic adjustments required to align reported expenditures to final cost allocation results should be immaterial.

- *Controls to ensure that agencies are drawing federal funds timely and accurately are lacking* – Improve monitoring by creating better management reporting to identify and remedy instances where agencies are not drawing down federal funds in a timely manner or have drawn amounts in excess of reported federal expenditures.

- *Current reconciliation processes to ensure that amounts reported on federal reports are in agreement with the State accounting system are inefficient or lacking completely* – Streamline and improve the reconciliation of federal expenditures reported in the accounting system with amounts reported by agencies on federal reports.

The State will need to consider whether the interface of eCivis with the ERP system, currently in the implementation stages, will ensure sufficient functionality to address the above deficiencies. In certain instances, the State will need to utilize reporting from the new ERP system to implement monitoring controls to accomplish the above objectives.

Cause: Sufficient controls have not been implemented within the current statewide accounting system to ensure amounts are consistent with the limitations of grant awards from the federal government and claimed expenditures on federal reports are consistent with amounts recorded in the State's accounting system.

Effect: Federal revenue could be overstated and not detected for financial reporting purposes. The share of program costs allocable to funding sources (i.e., general revenue vs. federal revenue) could be misstated.

RECOMMENDATIONS

2024-008a Continue to utilize eCivis to improve controls over federal program financial activity.

2024-008b Implement a monitoring process that highlights variances between RIFANS and federal reports to ensure that adjustments are made in a timely manner to correct reporting.

2024-008c Ensure that the interface of eCivis with the new ERP system, currently expected to be implemented in fiscal 2026, will ensure sufficient functionality to address the above control deficiencies.

Management's Views and Corrective Actions:
We agree with the recommendations related to this finding with the caveat below regarding 2024-008(b)

2024-008a: We will continue to utilize eCivis to improve controls over federal program financial activity. Increased adoption of the system allows us greater insight into the federal awards, and system functions to work with state agencies to more effectively monitor fiscal aspects and controls.

2024-008b: As RIFANS is sunsetting as of June 30, 2025, and all fiscal close activities for FY25 will be performed in ERP, this recommendation will not be acted upon.

2024-008c: Our focus is to ensure that eCivis successfully integrates with the new ERP system, currently expected to be implemented in fiscal 2026. Once this is accomplished, sufficient functionality between the two systems will exist to address the control deficiencies noted in this finding.

Anticipated Completion Date: Ongoing

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Finding 2024-009	***(material weakness – repeat finding – 2023-010)***

INVESTMENT NEEDED FOR MODERNIZATION OF THE STATE'S TREASURY FUNCTIONS

The complexity of Treasury operations has increased substantially over the years without significant modifications to the State's investment in technology and personnel to support those efforts and to ensure internal control best practices are maintained.

Background: The Office of the General Treasurer (Treasury) is responsible for the State's cash management functionality which includes oversight of deposit balances with multiple financial institutions, investment of cash balances, maintaining liquidity to meet obligations, and ensuring the safety of deposits and short-term investment balances.

At June 30, 2024, the State's short-term deposit, investment portfolio (exclusive of pension and OPEB related investments), and funds on deposit with fiscal agent (State debt proceeds, which are held in trust by fiduciaries but subject to the State's monitoring of permitted investments and other contract requirements) totaled in excess of $3.5 billion. Organizations of a similar size and complexity would typically have sophisticated and integrated information technology systems to facilitate daily cash management operations and ensure compliance with deposit and investment guidelines.

The Treasury has utilized various applications to facilitate its cash management functionalities, but none have been integrated with the State's accounting system. The State has begun implementation of an ERP system which includes integrated cash management functionalities within the project scope. In addition, the Treasury is working with a consultant to develop a comprehensive plan to modernize information technology in Treasury operations. This would include automation of critical Treasury functions that are currently manually intensive and prone to error. The comprehensive plan would also attempt to maximize integration with the State's new ERP system to the extent possible.

Criteria: Management is responsible for ensuring internal controls over Treasury operations are well designed and effective. Most important within Treasury operations is ensuring segregation of duties. Treasury is also responsible for ensuring the safety and liquidity of the State's deposits and for ensuring compliance with the deposit and short-term investment guidelines of the State Investment Commission.

Condition: Treasury activities are not adequately supported by current technology that accesses and integrates data from multiple sources (e.g., accounting system, banks, custodians, investment counterparties). Data is independently gathered from a variety of sources, which is time consuming and inefficient. Given the current configuration of non-integrated applications, there is an insufficient number of staff assigned to these functions to allow adequate segregation of duties. The following control deficiencies were noted in the systems and processes used to manage the State's cash deposits and short-term investments:

- Difficulties in ensuring segregation of duties relating to the transfer of funds and the recording and reconciling of investment activity.

- The State is currently utilizing Excel to record the purchase and sale of investments. The program is used to journalize summary investment activity into the State's accounting system. While functional, the lack of transaction level detail being recorded in the State's accounting system, coupled with the lack of controls that a more substantial software application would include, increases the risk of error or omission.

- Managing compliance with investment diversification policies (promulgated by the State Investment Commission) and statutory collateralization requirements (mandated for the State's cash deposits) requires continual monitoring to ensure compliance. The Treasury currently lacks a modern cash management system that would facilitate compliance monitoring, requiring those functions to be performed by personnel already depended on for various other Treasury functions. Current monitoring procedures are prone to errors, including the omission of State deposit accounts, when evaluating collateralization requirements.

- The Treasury lacks dedicated internal audit and information security functions, common in most state Treasury operations, to ensure that financial and information security controls are in place and operating effectively.

The Treasury is in the final steps of completing a comprehensive assessment of banking and investment functions and a strategic plan that will provide the necessary recommendations to modernize its operations. This plan, once completed, will require an implementation and funding plan to be developed by the General Treasurer and its State partners in support of critical statewide cash management and investment processes. Integration with the new State ERP system, expected to become operational in fiscal 2026, will be critical to ensure the efficient and effective operation of the State's financial systems.

Cause: The current systems do not contribute to segregation of duties, and staffing is insufficient to adequately segregate the functions with the required redundancy needed in various positions. Current use of Excel lacks required access, data integrity, and other systemic controls to safeguard the recording of the State's short-term investment activity. There is a lack of sufficient technology and personnel resources needed to manage compliance with investment diversification policies and statutory collateralization requirements.

Effect: There is an inability to (1) maintain proper segregation of duties in key Treasury operations, (2) evaluate and monitor financial and operational controls, and (3) effectively monitor compliance with diversification and permitted investment requirements, as well as collateralization policies, for the State's cash and investments.

<u>RECOMMENDATIONS</u>

2024-009a Complete the contracted assessment of Treasury operations to identify potential modern technological and/or contract service solutions needed to manage the size and complexity of the State's current cash management and investment operations.

2024-009b Develop a strategic plan (inclusive of implementation phases and funding plan) needed to modernize the utilization of technology in Treasury operations.

2024-009c Emphasize integration with the State's new ERP system, currently being implemented, to maximize the efficient and effective operation of the State's financial systems.

Management's Views and Corrective Actions:
2024-009a: Treasury staff engaged PFM to provide Banking/Cash Management Consulting services following an RFP process that was initiated in fiscal 2024. After assessing Treasury's cash-related activity, PFM has developed a list of recommended improvements to address process inefficiencies. Treasury has begun implementing some of these recommendations, with the majority to be addressed through an impending banking RFP that will be supported by PFM.

2024-009b: Treasury staff currently utilizes G-Treasury as its workstation for initiating wires and viewing bank balances. PFM's assessment of Treasury's cash activities identified that the State is not fully utilizing G-Treasury's capabilities. Treasury staff and G-Treasury have discussed potential service enhancements that would allow staff to transition from the current Excel-based database to a more secure and modernized cash management system. Leveraging more of G-Treasury's service modules would also improve collateral risk management and investment manager oversight. Treasury will continue to request appropriations to implement and institutionalize the additional and necessary G-Treasury modules.

2024-009c: Treasury staff remains actively engaged in discussions surrounding the State's new ERP system, ensuring seamless banking integrations that enhance the efficiency of financial operations. By participating in ERP implementation meetings, Treasury is positioned to align banking functions with the system's capabilities. Additionally, the augmentation of Treasury's utilization of G-Treasury presents an opportunity to further strengthen integration, optimizing cash management and financial reporting processes. These efforts will help maximize the ERP system's potential, improving automation, transparency, and overall fiscal oversight.

Anticipated Completion Date: Ongoing

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Finding 2024-010 ***(significant deficiency – repeat finding - 2023-011)***

VOLUME OF ACCOUNTING SYSTEM JOURNAL ENTRIES

There is an excessive volume of journal entries recorded within the accounting system. This volume weakens controls over the appropriate authorization and classification of expenditures and limits transparency regarding the underlying transactions.

Background: More than 11,000 journal entries were processed during fiscal 2024 in the accounting system. An additional 37,000 journal entries were used to record receipts/revenues.

Criteria: Initiation and approval of journal entries is typically restricted to a small number of higher-level accounting staff to record specific financial reporting related entries or to make corrections.

Condition: A significant volume of journal entries is required due to the lack of a fully integrated ERP system. For example, journal entries are utilized to:

- Allocate costs to multiple programs and activities. These journals primarily adjust expenditures based on the results of various disparate federal cost allocation systems and agency time reporting systems that are utilized throughout the State;

- Record receipts due to the lack of a revenue and receivable module in the current State accounting system; and

- Reclassify expenditures recorded in governmental funds to facilitate capital asset recording in the government-wide financial statements.

Journal entries typically are considered higher risk from an internal control perspective as approval level controls require appropriate understanding and review of complex transactions to be effective. As the volume increases, the time to adequately review and approve what are often material transactions also increases, threatening the effectiveness of control procedures. Attaching sufficient documentation to journal entries to allow for informed approval by the reviewer also remains a challenge.

Cause: Insufficient cost allocation functionality in the current accounting system necessitates a high volume of journal entries to allocate administrative costs. Since accounting personnel in all departments and agencies need to process receipts through journal entries, the ability to initiate and approve journal entries is more widespread than would typically be seen in most large accounting systems. In addition, while agency finance personnel are knowledgeable about program and agency activities, they are often less familiar with governmental accounting and financial reporting requirements.

Effect: Controls are weakened through the large volume of high-dollar transactions that are recorded through journal entries, increasing the possibility that a material misstatement could occur and remain undetected in the normal course of operations.

RECOMMENDATIONS

2024-010a Ensure the statewide ERP system, expected to be implemented in fiscal 2026, addresses the control deficiencies and inefficient processes that have resulted due to functional limitations of the current accounting system.

2024-010b Enhance review and oversight of material journal entries to ensure appropriate recording of transactions and avoid misstatement of the financial statements.

Management's Views and Corrective Actions:
2024-010a: Refer to 2024-001 and 2024-002 responses.

2024-010b: Management agrees with the recommendations. This is being addressed with the implementation of a new ERP system as stated in prior years. Accounts and Control will consider the review and oversight of material journal entries in the hierarchy decisions for the new system. Refer to 2024-001 and 2024-002 responses.

Anticipated Completion Date: July 1, 2025

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Finding 2024-011 *(significant deficiency – repeat finding - 2023-012)*

PREPARATION OF THE GOVERNMENT-WIDE FINANCIAL STATEMENTS

The State's government-wide financial statements often require audit adjustments to correct misstatements caused by the utilization of significant manual procedures that are prone to error.

Background: The State accounting system maintains distinct accounting records to support the preparation of the government-wide financial statements (accrual basis of accounting) from the governmental fund financial statements (modified accrual basis of accounting). The full accrual set of books is largely populated through the consolidation of the monthly activity from the modified accrual set of books. A capital asset module is utilized to maintain detailed recording for capital asset categories (except for project-based assets such as infrastructure and construction in progress, which are tracked and recorded through more manual processes) throughout the year, and support presentation on the government-wide financial statements. The State's debt obligations are managed through a separate application that is not integrated with the accounting system, requiring manual journal entries to accurately record debt-related activities. Conversion entries are utilized to record noncurrent assets and liabilities and to reclassify fund-level activity as needed. A significant amount of manual processing, mostly in Excel workbooks, is required to compile data needed to prepare these conversion entries.

Criteria: Trial balances from the accounting system should not require significant modification to generate accurate financial statements. Controls should be operational to ensure that all transaction activity is recorded consistently in both sets of books and required updates to account mappings are made when needed. Preparation of the government-wide financial statements should include adequate review to ensure results are consistent with expectations.

Condition: The fiscal 2024 draft government-wide financial statements required several audit adjustments to ensure proper and accurate presentation. OAC staff continue to have difficulty preparing the required reconciliations between the government-wide and governmental fund financial statements. Adjustments in fiscal 2024 were largely attributed to (1) net position reclassifications, (2) revenue categorization differences between operating and capital grants, (3) misstatements in reported capital assets, and (4) reporting long-term liabilities and receivables.

Cause: Most misstatements related to errors in process or classification which occur in conjunction with manual processes inherent in the State's current preparation of the government-wide financial statements.

Effect: Material misstatement of the State's financial statements could occur and not be detected in the normal course of operations.

RECOMMENDATIONS

2024-011a Enhance procedures for preparing the government-wide financial statements to ensure consistent and accurate recording of transaction activity. Minimize manual processes to the extent possible when preparing the financial statements.

2024-011b Implement quality control procedures designed to detect and correct misstatements in the government-wide financial statements.

Management's Views and Corrective Actions:

2024-011a: The process for preparing the government-wide financial statements will change with the ERP implementation. The ERP system automates the production of financial reporting by integrating the ERP with our report generating software.

Anticipated Completion Date: July 1, 2025

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Finding 2024-012	*(significant deficiency – new finding)*

CONTROLS OVER REPORTING OF LEASES AND SUBSCRIPTION-BASED INFORMATION TECHNOLOGY ARRANGEMENTS

Controls over the identification and reporting of leases and subscription-based information technology arrangements (SBITAs) applicable to GASB Statements No. 87 and No. 96 were insufficient to ensure all applicable agreements were properly recorded.

Background: Lease and subscription agreements are executed at the department/agency level and then reported to the Office of Accounts and Control (OAC). The OAC devised a standard template for the departments/agencies to use to report the active agreements, including changes to existing agreements (such as extensions of the term, changes in rent/price that were subject to an index, etc.).

The OAC employs EZLease, a cloud-based software application, to track the leases and SBITAs applicable to GASB Statements No. 87, *Leases*, and No. 96, *Subscription-Based Information Technology Arrangements*. EZLease also calculates and provides the necessary journal entries, based on the data entered for each agreement, to aid the financial reporting process.

Criteria: GASB Statements No. 87 and No. 96 require governments to recognize new leasing and subscription agreements as other financing sources in the fund financial statements and record a long-term liability with a right-of-use asset on the government-wide financial statements.

Both GASB Statements also require governments to remeasure reported assets and liabilities, when applicable, in reporting periods after the initial year of measurement for changes in the agreement terms, contract extensions, and/or changes in underlying estimates used during the initial measurement.

Condition: Amounts reported for other financing sources, capital outlay, assets, and liabilities were materially misstated, requiring adjustment, in the respective financial statements due to the following items noted during our audit:

- Several lease and SBITA agreements that were reported by respective agencies but not accounted for in EZLease;
- A lease agreement not reported by the respective agency that met the State's reporting criteria;
- An extension of a SBITA agreement that was reported by the respective department but was not remeasured to account for the increased long-term liability and right-of-use asset; and
- A lease that was modified and remeasured when there was no change in accordance with GASB Statement No. 87 that would require remeasurement during the fiscal year.

Cause: Review of agency-provided templates was insufficient to accurately identify all applicable agreements that are required to be reported by GASB. Additionally, review of changes to existing agreements was insufficient to ensure proper accounting when changes occurred.

Effect: Material misstatement of the financial statements are not being detected and corrected.

RECOMMENDATION

2024-012 Improve internal controls by implementing supervisory review procedures over the determination, recording, and adjustment of reported assets and liabilities relating to leasing and subscription-based information technology arrangements.

Management's Views and Corrective Actions:

Management agrees with the finding and will enhance review procedures to identify missing information provided by State agencies.

Anticipated Completion Date: Completed

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INTERNAL CONTROL OVER FINANCIAL REPORTING

INTERMODAL SURFACE TRANSPORTATION FUND

Finding 2024-013 **(significant deficiency – repeat finding – 2023-013)**

DIVISION OF MOTOR VEHICLES – CONTROLS OVER REVENUE COLLECTIONS

Controls can be improved over the recording of license, registration, and surcharge fees collected by the Division of Motor Vehicles (DMV) and deposited in the Intermodal Surface Transportation (IST) Fund.

Background: In fiscal 2024, the DMV collected $110 million in revenues (excluding sales taxes) of which $88 million was remitted to the IST Fund's Highway Maintenance Account.

Criteria: DMV must have controls in place to ensure the completeness of revenue reflected within the IST Fund. RI General Law chapter 39-18.1 designates certain fees to be deposited in the IST Fund for transportation purposes.

Condition: DMV lacks procedures to provide reasonable assurance that the appropriate fees earmarked for the IST Fund have been received and recorded as revenue. This should include documentation of the fee structure identified by the RI General Laws, the surcharge amount being applied to each DMV transaction code, and how the DMV computer system, RIMS, is programmed to identify such amounts for the IST Fund. We identified the following control deficiencies:

- There is a partial, but incomplete, crosswalk of the fee structure identified by the RI General Laws for licenses, registrations, surcharges, etc. and how RIMS is programmed to identify such amounts.

- The current reconciliation between the State accounting system (RIFANS) and RIMS does not include all fees collected by the DMV.

- Manual write-offs are not recorded in RIMS; they are maintained outside of the system. Manual write-offs should be recorded within RIMS to maintain a log of the adjustments and to facilitate RIMS/RIFANS reconciliation.

DMV began working through the recommended reconciliation; however, corrective action was not completed in fiscal 2024 and remains in progress. To be an effective control over financial reporting, the reconciliation needs to be completed prior to the fiscal closing by the State.

Cause: Controls to ensure the completeness of the DMV revenues earmarked for transportation purposes within the IST Fund require improvement. DMV should consider ways that the RIMS system can be utilized to enhance monitoring of compliance with statutory revenue requirements and assist the agency in completely reconciling with RIFANS.

Effect: Potential misstatements in the financial statements may not be detected in a timely manner.

RECOMMENDATIONS

2024-013a Ensure the timely completion of monthly and annual reconciliations between RIFANS and RIMS to ensure that recorded revenue is supported by RIMS data.

2024-013b Complete the crosswalk between the fees charged in RIMS and the section of the Rhode Island General Laws authorizing the fee.

Management's Views and Corrective Actions:

2024-013a: The DMV agrees that a reconciliation of the revenues collected is needed and will work to reconcile the revenues collected on an annual basis, there are too many variables outside of the DMV's control which prevent us from reconciling monthly. Additionally, with the implementation of the new ERP system we can not commit to completing the reconciliation prior to the fiscal close. We will work with Accounts & Control to include DMV specific deadlines in future year end close timelines so we can complete before the fiscal close.

2024-013b: The DMV agrees that a crosswalk is a beneficial document to have. The DMV is in the process of completing a crosswalk of fees charged in RIMS and the section of the Rhode Island General Laws.

Anticipated Completion Date: September 30, 2025

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Finding 2024-014	***(material weakness – repeat finding – 2023-014)***

INTERMODAL SURFACE TRANSPORTATION (IST) FUND – FINANCIAL REPORTING

Control deficiencies continue to result in significant misstatements in amounts reported in the IST Fund financial statements. Internal controls must be improved to ensure consistent and accurate financial reporting.

Background: The IST Fund accounts for transportation-related activities of the State, including the federal highway construction program, transportation bond proceeds, and designated revenues collected by the Division of Motor Vehicles. The IST Fund financial statements, although generated by the State accounting system, are the responsibility of the RI Department of Transportation (RIDOT) and are significantly impacted by its internal Financial Management System (FMS).

Criteria: Controls over the preparation of financial statements should ensure consistent and accurate financial reporting. RIDOT management is responsible for ensuring that controls over financial reporting are in place and operating effectively.

Condition: Our audit identified numerous misstatements in the IST Fund financial statements that required adjustment. The misstatements impacted most financial statement categories and materially misstated the financial statements for the major fund. Audit adjustments reduced the operating loss reported on the draft financial statements by $10.4 million. Individual adjustments were necessary to:

- Reclassify certain transactions within account classifications to ensure consistent presentation with GAAP;
- Increase federal revenue and expenditures which were understated by $4.1 million and $2.2 million, respectively; and
- Correct the funding source for project expenditures by $3.3 million programmed to be funded by transportation bond proceeds that were erroneously accrued to federal revenue.

The quantity and magnitude of the misstatements were attributable to several internal control deficiencies relating to financial reporting. Account reconciliations are currently lacking to ensure accurate reporting of federal revenue and expenditures in the IST Fund. Audit adjustments were required and accepted by management to ensure that the financial statements were fairly stated in all material respects.

Our audit also identified a compliance issue impacting financial reporting for the IST fund. RIDOT received bond proceeds, in a prior year relating to the State's transfer of land to the I-195 Redevelopment District Commission (District), a component unit of the State. During fiscal 2024, the State utilized the remaining $4.9 million in proceeds, in addition to State appropriations, to defease the outstanding revenue bonds of the District. Our review of the use of funds identified potential noncompliance with U.S. Code Title 23, Section 156 (c), which restricted the funding for infrastructure projects authorized by the Federal Highway Administration. After discussion with the State, an adjustment was recorded to reclassify the debt service to an allowable revenue source.

Cause: The current review process of the draft financial statements is not adequate to identify significant errors and misclassifications. Identified misstatements resulted from manual procedures designed to compensate for deficiencies in the accounting system. Examples include the allocation of fund balance and allocation of expenditures from the FMS. These manual processes can be prone to error and lack controls to ensure completeness. In addition, most of these accounting processes are performed by the more experienced accounting staff at RIDOT, reducing the likelihood that independent reviews will be performed. Most of the exceptions noted may have been identified if RIDOT had been performing a more detailed review of account balances in conjunction with the fiscal close.

Effect: Account balances within the IST Fund financial statements could be materially misstated and go undetected.

RECOMMENDATIONS

2024-014a Ensure the transactions identified through the reconciliation of each activity and/or funding source within the IST Fund result in the appropriate categorization and reporting of revenue, expenditures, and fund balance components on the financial statements.

2024-014b Implement controls to ensure the accuracy of recorded amounts in the financial statements, including 1) account reconciliations, 2) complete reconciliations between the FMS and State accounting system, and 3) detailed review of financial statement accounts.

2024-014c Implement quality control processes to ensure proper classification and presentation of the financial statements.

Management's Views and Corrective Actions:
2024-014a: RIDOT General Ledger Team continues to implement checks throughout the fiscal year to ensure accuracy and reporting of the IST Fund according to GASB Standards while using proper Generally Accepted Accounting Principles. The reporting in the fund balance has improved as we have continuously worked with Department of Administration's Office of Accounts and Controls Office to ensure all accounts are listed and being reported.

2024-014b: RIDOT has developed a plan of controls to streamline the reconciliation between FMS and RIFANS with new reports and procedures. Ensuring the appropriate reconciliation has provided the RIDOT General Ledger staff the ability to find possible issues quicker and provides RIDOT General Ledger Team the capacity to resolve any issues at the time of reconciliation to prevent any future issues.

2024-014c: RIDOT will continue to improve the control process during fiscal close to provide accurate data and classification of all funds and account to maintain the financial statements of the State.

Anticipated Completion Date: Ongoing

Contact Person: Loren Doyle, Director of Operations, Department of Transportation
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Finding 2024-015	***(material weakness – repeat finding – 2023-015)***

TRANSPORTATION INFRASTRUCTURE REPORTING

Controls over the identification of transportation infrastructure assets need further improvement to ensure accuracy and completeness. Controls should be improved to record the disposal of infrastructure assets when retired, replaced, or permanently impaired.

Background: RIDOT enhanced its process to identify transportation infrastructure assets which use the RIDOT Financial Management System (FMS) to identify each project and ensure that total project costs (e.g., design and construction costs) are included in the capitalized amounts. Since the source of the information used to identify capitalized infrastructure is FMS and the financial statements are based on the State accounting system (as recorded by the Office of Accounts and Control), the data used must be reconciled between the two systems.

Projects are assigned to one of nine infrastructure codes established to identify the type of asset (road, bridge, etc.) and the estimated useful life of the asset which drives depreciation expense.

Criteria: GAAP require recording the State's investment in infrastructure assets to be reflected on the government-wide financial statements. Such amounts should be capitalized and depreciated consistent with the State's adopted accounting policies. Amounts are recorded as construction in progress until placed in service, at which time depreciation commences. Infrastructure disposals should be recorded when assets are replaced or permanently taken out of service.

GAAP also requires that capital assets be evaluated for impairment when events or changes in circumstances suggest that the service utility of a capital asset may have significantly and unexpectedly declined.

Condition: The cost and related accumulated depreciation associated with infrastructure assets that have been replaced or are no longer in service have not been removed from reported infrastructure amounts. The State asserts that these assets are fully depreciated, thus not resulting in a significant misstatement of reported net infrastructure, however, a process for removal to support that assertion by management needs to be implemented. A reasonable process to identify and record infrastructure disposals is also needed to ensure accurate note disclosure of infrastructure assets and related accumulated depreciation.

RIDOT utilizes its FMS to report the amount of infrastructure additions to the Office of Accounts and Control annually. The FMS does not reflect accrued expenditures, while the State accounting system includes accruals for financial reporting purposes. The prior year's accrual reversals in the State accounting system were not properly accounted for when recording infrastructure additions for fiscal 2024 and resulted in construction in progress being overstated by $70 million. Material adjustments were recorded to correct balances at June 30, 2024. RIDOT needs to properly account for accruals when recording infrastructure additions for financial reporting.

In conjunction with its review of asset disposals, RIDOT should consider whether it has transportation infrastructure assets that may be impaired and require proper accounting recognition in accordance with government accounting standards. The State did not properly record the westbound side of the Washington Bridge as impaired, requiring an adjustment of $39.5 million, net of accumulated depreciation.

Cause: Controls over RIDOT's identification and accounting of infrastructure assets are not sufficient to ensure complete and accurate financial reporting for capital assets.

A consistent process to evaluate and remove estimated costs relating to retired, replaced, or impaired infrastructure has not been implemented.

RIDOT does not review infrastructure assets reported in the State's financial statements to ensure that balances are consistent with supporting documentation and the State accounting system.

Effect: Infrastructure assets and related depreciation expense may be materially misstated.

RECOMMENDATIONS

2024-015a Enhance controls over the recording of infrastructure assets by reconciling RIDOT departmental records of construction in progress and infrastructure assets to amounts reported in the State's financial statements.

2024-015b Implement a process to remove estimated infrastructure assets and related accumulated depreciation when assets have been replaced or taken out of service as required by GAAP.

Management's Views and Corrective Actions:

2024-015a: RIDOT will continue to reconcile the infrastructure assets along with construction in progress through RIDOT's Financial Management System (FMS) to match the State's Financials.

2024-015b: In previous years, there were several attempts to develop a method to determine which assets were impaired. RIDOT's Financial Management Team and Bridge Maintenance Teams provided necessary information of which assets were to be impaired, replaced, and/or taken out of service. RIDOT will continue to work with Department of Administration's Office of Accounts and Control to determine the proper life cycle of these assets.

Anticipated Completion Date: Ongoing

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INTERNAL CONTROL OVER FINANCIAL REPORTING

STATEWIDE INFORMATION SYSTEMS SECURITY

AUDIT STANDARD:

Auditing standards define the risk of the use of information technology (IT) as the susceptibility of information processing controls to ineffective design or operation, or risks to the integrity of information in the entity's information system, due to ineffective design or operation in the entity's IT processes.

Finding 2024-016 *(significant deficiency – repeat finding – 2023-016)*

COMPREHENSIVE INFORMATION SYSTEMS SECURITY – ADDITIONAL RESOURCES NEEDED TO ADDRESS CURRENT SECURITY RISKS

Additional resources are needed to mitigate the current risks that have been validated by both internal and contracted cybersecurity assessments. The State's ability to assess, document, and mitigate risks will require substantial maturity of the State's current policies and procedures.

Background: The Division of Enterprise Technology Strategy and Services (ETSS) within the Department of Administration (DOA) has responsibility for the State's varied and complex information systems. This includes ensuring that appropriate security measures are operational over each system and the State's information networks. Information security (IS) is critical to ensure that information technology (IT) dependent operations continue uninterrupted, and that sensitive data accumulated within State operations remains secure with appropriately controlled access.

Periodic comprehensive technology risk assessments are key to uncovering underlying vulnerabilities in the environment as well as providing guidance on where to best spend limited resources to reduce risk. The State's most recent external assessment of its cybersecurity readiness was completed in June 2022. The assessment noted improvements by the State in several areas and identified and prioritized a significant number of critical improvements required to mitigate current security risks. During fiscal 2024, ETSS performed its own self-assessment of cybersecurity and have mapped their risk levels. Critical and high priority improvements will require substantial resources to be devoted by the State to mitigate identified risks. The State also procured a Governance Risk Compliance (GRC) system to be implemented as a tool to manage risks, ensure compliance with relevant regulations, and align operations with adopted IT security policies and procedures.

During our audit we focused on the following mission critical systems due to their impact on the State's financial reporting: RIFANS (Accounting), Payroll, STAARS (Taxation), RIBridges (Health and Human Services), MMIS (Medicaid), RIMS (Motor Vehicles), and DLT benefit and revenue systems (Unemployment, Workers Compensation). We also reviewed the IS over the State's network environment, which is critical to the State's operations and can negatively impact application security if not maintained at an acceptable industry standard level.

During fiscal 2024, ETSS continued to implement a variety of system and network improvements that will enhance managements capabilities (e.g., policy enforcement) and improve overall IS. ETSS continued its ongoing effort to address the human capital resource constraints by adding personnel and contract resources in areas of need during fiscal 2024. In March 2024, a GRC manager was hired with duties that include conducting periodic risk assessments, covering the likelihood and impact from unauthorized access, use, disclosure, disruption, or modification of information systems.

Criteria: IT risk assessment policies and procedures should be documented (National Institute of Standards and Technology (NIST) SP 800-53, RA-1). Risk assessments should be performed on an ongoing basis or whenever there are significant changes (e.g., new system or network implementations) (NIST SP 800-53, RA-3). Risk assessments are vital to managing and mitigating risks, maintaining compliance (e.g., IRS and HIPAA requirements), prioritizing IT spending, and supporting business continuity. The management and oversight of the State's IS relies upon the implementation of a comprehensive plan, which includes detailed policies and procedures that are designed to safeguard all systems and data contained within the State's IT environment. Assessments of compliance to IT policies and procedures for all critical IT systems and data should be performed routinely as part of the comprehensive risk assessment.

Condition: The State's resources are insufficient to mitigate the current risks that have been validated by its own internal cybersecurity assessment. ETSS is challenged with reviewing and updating Statewide policies and procedures in a timely manner. Agency compliance with ETSS policies and procedures and the identification and mitigation of risks remain a challenge. The State has improved technology in recent years to identify and report on certain risks, however, the personnel resources needed to evaluate and mitigate them remain insufficient.

The State needs to formalize its strategic plan to identify the appropriate IS resources needed for the State's size and complexity. An integrated GRC platform, recently procured to aid the State's GRC, needs to be implemented to provide the necessary technical support for the volume of IS risks managed by a large entity.

The State does not adequately oversee, monitor, and review outsourced functions, especially as it relates to software platforms supporting State operations. External resources (contractors) have been employed to expedite implementation, support, and maintenance of critical IS functions, such as firewall and networking services, which are vital IS functions.

ETSS is often unable to provide an adequate transition period to ensure institutional knowledge is transferred from departing staff to replacement staff. Current policies and procedures are also not adequately documented to promote IS knowledge transition to new staff.

Cause: Current resources are insufficient to maintain IS over the State's IT infrastructure, systems, and data for an entity the size of the State. Multiple decentralized IS applications are currently deployed and add to the complexity of operations. The lack of a formalized risk-based approach, which is required to support the number of system implementations, along with concurrent network and security monitoring improvements, are difficult to manage.

Effect: Critical systems and data may be exposed to security vulnerabilities and cyberattacks when comprehensive information security risk assessments are not performed on an ongoing basis and identified risks are not mitigated timely. This could impact the State's ability to ensure continued operation of mission critical systems and the security and integrity of the data within those systems.

<u>RECOMMENDATIONS</u>

2024-016a Using the most recent cybersecurity assessments and existing audit recommendations, formalize a comprehensive plan to address the current IS risks to the State's operations. This plan should be risk-based and include the necessary personnel and systems support required to ensure timely mitigation by the State.

2024-016b Continue to update formal risk assessments periodically (with annual updates to adjust security priorities), with the results documented and communicated to management. Implement the GRC application as the long-term solution supporting IT risk assessment and management.

2024-016c Identify the additional resources needed to address critical IS deficiencies noted in security assessments and audits as part of strategic plan updates.

2024-016d Ensure that policies and procedures throughout ETSS operations are adequately documented to allow for knowledge transfer as personnel changes.

<u>Management's Views and Corrective Actions:</u>

2024-016a / 2024-016b / 2024-016c: ETSS continues to prioritize investment and actions in alignment with risk to the State's operations. In-progress is the implementation of a Governance Risk, and Compliance (GRC) platform for a long-term, scalable, and efficient assessment of our technology partners and agencies with ensuring consistent risk measurement aligned to program frameworks.

2024-016a / 2024-016c: In parallel with technology efforts, ETSS continues work to address personnel capacity risks with a focus on retaining, skilling, and attracting talent. ETSS has launched a training program designed to upskill and provide internal succession planning for current staff with a focus on developing skills required to support the adoption of emerging technologies.

2024-016d: ETSS has recently hired a GRC manager dedicated to management of governance, risk, and compliance which includes the annual review of all policies. A road map has been defined to ensure policies will be updated by end of 2025.

Anticipated Completion Date:
2024-016a / 2024-016b / 2024-016c – Continuous
2024-016d – Q4 CY2025

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Finding 2024-017	***(material weakness – repeat finding – 2023-017)***

PROGRAM CHANGE CONTROLS

The State's enterprise-wide program change control procedures for the various IT applications operating within State government, while improved, have not adequately mitigated the risk that unauthorized program changes could be implemented without detection.

Background: Program change controls are a critical component of any system development lifecycle. These controls ensure that only authorized changes are made to programs (along with user acceptance testing) before being promoted into the production environment. All computer applications require changes and/or updates throughout their production lifecycles. Consequently, these customized applications require a formalized change management system to ensure that only authorized changes are made. While some agencies have formally implemented program change controls, a standardized statewide approach has not been adopted across all agencies.

The State has been developing procedural guidance to detail the correct use of change management software and mandate internal control practices and procedures. ETSS has established the Center of Excellence (COE) and improved the Change Advisory Board's (CAB) processes. This includes a more comprehensive evaluation of proposed changes, assessing risks to agencies, and implementing recommendations that have been carefully reviewed for potential impact. The CAB continues to evolve, aligning more closely with structured NIST Information Technology Infrastructure Library (ITIL) best practices and governance over projects impacting infrastructure. The COE has also made strides in operational maturity by recently establishing an applications CAB. The goal of the applications CAB is to implement the same governance process as the infrastructure CAB, focusing on managing application changes at the agency level. However, the development of uniform guidance procedures for the applications CAB is still ongoing, and full participation across all agencies has not yet been achieved.

Criteria: NIST SP 800-53, §CM-3, 7b states that "configuration change control for organizational systems involves the systematic proposal, justification, implementation, testing, review, and disposition of system changes, including system upgrades and modifications. Configuration change control includes changes to baseline configurations, configuration items of systems, operational procedures, configuration settings for system components, remediate vulnerabilities, and unscheduled or unauthorized changes. Processes for managing configuration changes to systems include Configuration Control Boards or Change Advisory Boards that review and approve proposed changes."

The State's change management process should be standardized so that all code modifications, testing, acceptance, and implementation provide management with a tracking history and record of approvals. This leads to consistent outcomes, efficient use of resources, auditability, and enhanced integrity of the application systems. Automated tools facilitate control over the change management process, reduce human error, and allow for a consistent, predictable, and repeatable process.

Condition: Various agencies throughout the State were not complying with ETSS's program change control policies and procedures, which were still maturing in fiscal 2024. For some of the State's critical systems, automated change control procedures are still lacking to substantiate that only authorized and proper changes were implemented. The creation of the COE and CAB represents a movement towards standardization; however, the risk that unauthorized program changes could be implemented and not be detected remains.

Cause: Various methods are still in place and a structured NIST-approved framework is not fully utilized within all agencies to control program change management. There are still instances where manual and semi-automated procedures that incorporate emails, memoranda, and other paper-based forms to document application changes are being used by various agencies. Uniform adoption of the COE/CAB process Statewide has not taken place. Numerous agencies still lack proper controls to mitigate inappropriate changes.

Effect: Program changes could be put in place without authorization, testing or acceptance by management. Improper program changes can destabilize system operations and negatively impact data integrity and program compliance.

RECOMMENDATIONS

2024-017a Continue to streamline and expand the CAB process and include more detailed documentation. Implement and document procedures detailing specific requirements for program change control and disseminate across ETSS support staff and ensure its proper execution.

2024-017b Determine the appropriate combination of operational, procedural and/or technical adjustments required to use change management monitoring software to ensure that only authorized program changes are deployed.

Management's Views and Corrective Actions:
The ServiceNow ITSM Maturity Project, initiated in November of 2024, focuses on improving several ITIL processes by implementing best practices and utilizing new out-of-the-box functionality within ServiceNow. A major change will be in the ETSS Infrastructure and Operations Change Management process. One key new feature is the ability to create different change models, such as application changes. These changes are expected to be rolled out in Q2 of 2025. After implementation, ETSS will collaborate with relevant teams to implement Change Management and create a Change Advisory Board (CAB) for Enterprise Application changes, which will be later expanded to support other applications.

Anticipated Completion Date: December 19, 2025, ERP Enterprise Application, Ongoing for other agency applications

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Finding 2024-018	***(significant deficiency – repeat finding – 2023-018)***

PERIODIC SYSTEM ACCESS AND PRIVILEGE REVIEWS

The State's current practices for periodic logical access and privilege reviews at both the application and network levels need improvement.

Background: It is critical for an organization to consistently identify and mitigate potential security risks associated with access and permissions by routinely reviewing and recertifying access rights granted to users, vendors, contractors, etc. By confirming user identification, access level assessments, privilege reviews, and activity monitoring, the systems governed or accessed by these users remain secure and protected.

During fiscal 2024, ETSS continued to mature its identity access management by implementing certain automated reviews of system user access to improve timely deactivation of inactive users. These automated reviews function as a compensating control for when access is not reported and terminated through the standard ticketing system process employed by the State.

ETSS began deployment of a privileged access management (PAM) platform solution in fiscal 2024 that will allow for controlling and monitoring privileged access across the State's domain.

Criteria: NIST SP 800-53, §AC-6, 7b states "The need for certain assigned user privileges may change over time to reflect changes in organizational mission and business functions, environments of operation, technologies, or threats. A periodic review of assigned user privileges is necessary to determine if the rationale for assigning such privileges remains valid. If the need cannot be revalidated, organizations take appropriate corrective actions." ITIL Request for Change (RFC) process suggests a formal proposal for a change to an IT service or infrastructure should be submitted as a ticket within a ticketing system.

Condition: Periodic review of granted system access privileges (for standard and nonstandard users) is not consistently performed for several applications utilized throughout State government. Special attention should be paid to review system access for generalized accounts and individuals granted elevated access to ensure that such access remains appropriate and terminated in a timely manner when no longer required. State network access should also be reviewed to ensure timely termination when system users leave employment (State or contractor), transfer to a new position, or no longer require system access.

Agencies are not consistently utilizing the ticketing system to communicate needed changes in user access. Further, when tickets are generated, they sometimes lack the necessary information to provide for a detailed review of the change in access being authorized. ETSS continues to make progress in this area of concern by working with agencies to educate and emphasize the importance of clear and timely communication of logical access and privilege change requests. Agency compliance with adopted uniform standard ITIL RFC processes across their IT environment remains inconsistent.

Cause: Lack of consistent and uniform review of system access (privileges) across many State applications.

Effect: Improper or unauthorized access to State systems or networks which could impact service availability, data integrity, and/or security.

RECOMMENDATIONS

2024-018a Augment the implemented automated access review process to incorporate nonstandard users, as well as for periodic, verifiable privilege reviews for all applications and networks. Prioritize critical financial applications and those that contain sensitive data.

2024-018b Ensure that ticketing requests include critical information to properly track and review system changes for proper authorization. Continue to educate agencies on the importance of utilizing ITIL best practices for program change management.

2024-018c Reinforce policies and procedures for privileged user access reviews to be performed by assigned agency IT staff periodically (no less than annually).

2024-018d Continue deployment of the PAM platform solution to allow for controlling and monitoring privileged access across the State's domain.

Management's Views and Corrective Actions:

2024-018a / 2024-018d: ETSS has aligned security team resources to continue the centralization of management of user identities and align the efforts under the 'Zero Trust Architecture Center of Excellence'. This center of excellence has been charged under the drafted charter to expand privileged access management (PAM) capabilities and enhance access reviews while implementing further automation to mitigate risk.

2024-018b: ETSS is developing and implementing best practices within our ITSM platform, ServiceNow to capture and track critical information for the ERP Enterprise Application project. As part of our ServiceNow ITSM Maturity project, ETSS will configure the ability to build Business Application Services and Service offerings. This will enable the capture of key application service information and the creation of service catalog items with workflows to track requests like granting and removing application access. ETSS will first establish a blueprint for the ERP Enterprise Application and then expand this to include other applications.

2024-018c: The review of policy will fall under the actions of 2024-016d.

Anticipated Completion Date:
2024-018a / 2024-018c – Ongoing
2024-018b – December 1 2025, for ERP Enterprise Application, Ongoing for other applications
2024-018d – Q4 CY2025

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Finding 2024-019	***(significant deficiency – repeat finding – 2023-019)***

DATABASE LOGGING AND ACTIVITY MONITORING

The State's current practices for database logging and activity monitoring at the database level need improvement.

Background: Database logging and activity monitoring is an essential component to maintaining proper security and control over systems. Having an effective mechanism for monitoring and remediating accidental changes or intentional insider threat actions is imperative. ETSS began a phased rollout of a solution used for database activity logging and monitoring that is currently operational within a few key agencies.

Criteria: Proper database logging, monitoring, and alerting is identified as an important step in securing the database by both the Information Systems Audit and Control Association (ISACA) and other IT security professionals as an industry best practice. It is essential to have logging and monitoring at the application level for key financial and sensitive data to guard against unauthorized transactions, errors, and unauthorized changes occurring at the database level outside of the scope of application controls.

Condition: Database logging and monitoring for most State applications is not adequately deployed across the various agencies. More progress needs to be made in advancing the program's usage from informational (majority of current State usage) to true actionable alerts which will aid in mitigation of risk to the programs and services utilizing the technology. While the State improved in this area, consistent application of controls and additional resources are still needed. Interfacing the current solution with the State's Security Information Event Monitoring (SIEM) application requires maturation to allow for proper actionable and centralized monitoring of database activity.

Cause: The State lacks an implemented uniform practice for database logging and activity monitoring. Most agencies have not implemented the solution selected by ETSS due to concerns over system resource utilization. A disconnect between perceived and actual resource consumption exists that needs to be resolved.

Effect: The lack of database logging and monitoring for improper activity makes it more likely that key databases will be vulnerable to malicious attacks without detection. Risk to data integrity may result from unauthorized database changes that go undetected.

RECOMMENDATIONS

2024-019a Complete implementation of a consistent and effective database logging and monitoring process across all State applications. Prioritize applications/databases that contain critical financial and sensitive data.

2024-019b Communicate policies and procedures for database logging and monitoring to assigned agency IT staff. Implement specific training in conjunction with the communication of the policies and procedures to ensure consistent application across the entity.

2024-019c Review resource utilization concerns with agency representatives and create a Plan of Action and Milestones (POAM) to resolve any technical issues preventing implementation.

Management's Views and Corrective Actions:
2024-019a: ETSS continues to mature in the utilization of our constrained resources and we are moving to a more centralized monitoring of our SQL Server databases by the ETSS database administrator (DBA). We have begun deployment of two enterprise monitoring tools; one to monitor activity and performance on our databases using Microsoft Arc, and the second to ingest the database logs using IBM Guardium Data Protection. Both tools provide dashboards that are monitored daily by the ETSS DBA. We also have begun ingesting the logs sent by the Guardium Data Protection service into the state's Security Information Event Monitoring (SIEM) for advanced threat protection.

2024-019b: ETSS is in the process of establishing a Data, Analytics and AI Center of Excellence (DAAI CoE). The DAAI CoE will create policies for the central management of the state's database systems and bring together the staff responsible for database administration from across state government. This will make the deployment of centralized tools for monitoring more efficient since the staff responsible for maintaining databases at each agency will be members of the DAAI CoE. The DAAI CoE will also provide technical training for its members.

2024-019c: A Plan of Action and Milestones (POAM) will be a deliverable of Data, Analytics and AI Center of Excellence (DAAI CoE). The DAAI CoE will analyze our current state of resource utilization and address weaknesses. Collectively the DAAI CoE will be work to address gaps by providing the expertise needed in those areas.

Anticipated Completion Date:
2024-019a: We expect to have all of the SQL Server instances that are hosted in our private cloud connected to Microsoft Arc for activity monitoring by June 2025. We expect to have Guardium Data Protection installed on all of the SQL Server instances that are hosted in our private cloud by the end of the calendar year (12/31/2025). Guardium Data Protection takes longer as it requires downtime on the server, so the installation needs to be scheduled with the agency business owners for each database server.

2024-019b: We expect to have the DAAI CoE established and operational by March 2026.

2024-019c: We expect to have the DAAI CoE produce the POAM by June 2026.

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Finding 2024-020	***(significant deficiency – new finding)***

SECURITY INFORMATION EVENT MONITORING – LACK OF ITIL BEST PRACTICE PROCEDURES

The State needs to effectively integrate IS management applications to allow for improved documentation of risk identification and remediation. Enhancing the Security Orchestration, Automation and Response (SOAR) workflows is also needed for effective risk mitigation.

Background: SIEM and SOAR functionalities are designed to complement each other. SIEM collects and analyzes security data to identify potential threats, while SOAR automatically takes action based on those alerts generated by SIEM. When combined, the functions essentially orchestrate an immediate response to incidents by triggering pre-defined workflows and automating repetitive tasks, allowing for a more timely and effective response.

The State has had various methods and applications in place to address the monitoring of threats, security weaknesses, etc., for some time. Currently, the hardware that maintains one of the principal SIEM products does not communicate with the State's established ticketing system. Thus, daily security threat monitoring and remediation takes place without a centralized ticketing and knowledge-based system in place to properly track events. As a result, threat mitigation documentation is decentralized and not easily referenced, tracked or searchable. ETSS dedicated a staff member that was trained on the SIEM application in fiscal 2024. SIEM for an entity the size of the State is substantial and requires effective technological support and trained personnel to evaluate the reported security information events, assess risk to the State's IT security, and ensure timely remediation.

Criteria: While NIST standards do not specifically mention or require integrating a SIEM product with a ticketing system, it does recommend practices that align closely with the concepts of such an integration in a broader context of Incident Response (IR) and Security Operations. NIST SP 800-63 also provides guidance on establishing an IR methodology that incorporates effective tracking and management of security incidents. NIST SP 800-137 outlines continuous monitoring practices which are applicable to SIEM systems.

Condition: There are multiple products used for security event monitoring and risk mitigation, and not all are properly tracked within ticketing and knowledge-based systems. Consolidation of multiple product views, integration with the ticketing system and maturation of SOAR playbooks are desperately needed. Documentation of incidents is not being cataloged in a centralized knowledge-based library, as recommended by ITIL best practices. While the State's progress in continuing to mature its SIEM functionality is notable, the current volume of SIEM activity requires additional personnel resources to ensure timely evaluation, risk assessment, and remediation. The State's current legacy SIEM product may not effectively meet its needs. More modern cloud-based Extended Security Intelligence and Automation Management solutions may offer greater flexibility in integrating with the various platforms in use throughout the State. Improved SOAR functionality also needs to be developed.

Cause: The State's SIEM function lacks maturity and resources needed for the size of the State's IT operations.

Effect: Information security related events and threats could be reported and not acted upon in a timely manner, undermining the State's overall information security.

<u>RECOMMENDATIONS</u>

2024-020a Review the currently utilized legacy SIEM product and determine if it can effectively meet the State's information security needs. Consider migration to a cloud solution with more modern features and the capability to integrate more easily with other products such as a ticketing system.

2024-020b Consider whether additional resources are needed to research and mitigate reported events timely and to develop and mature policies and procedures for SOAR.

<u>Management's Views and Corrective Actions:</u>
2024-020a: ETSS has migrated to a cloud hosted Security Incident and Event Management (SIEM) solution within a program application environment that has been successful and is currently assessing feasibility to scale across the enterprise. The speed in which the transformation is dependent on funding, resource, and professional services availability.

2024-020b: ETSS aligned security team resources to further bolster the Security Operations Center (SOC) to help implement SOAR/automation capabilities in the recent investments of a next generation managed detection and response (MDR) platform and vulnerability management detection and response (VMDR) platform. Prioritization of further resources will be aligned to ETSS strategic planning noted in 2024-016a / 2024-016c.

<u>Anticipated Completion Date</u>:
2024-020a – Q4 FY2026
2024-020b – Ongoing

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Finding 2024-021	***(significant deficiency – new finding)***

VENDOR AND CONTRACTOR MANAGEMENT – INFORMATION SECURITY OVERSIGHT

Third-party software (inclusive of State systems maintained and operated by contractors) and "Software as a Service" (SaaS) products utilized by agencies may not be receiving regular security reviews. Agencies that administer programs that rely on information systems supported by contractors often lack personnel with the necessary background in information security to fully consider the security risks associated with those systems.

Background: The IT Vendor Management Office (VMO) functions to centralize the process for procurement of all IT hardware, software and services, including security assessments and risk review. Prior cybersecurity risk assessments have noted that third-party software and SaaS products purchased by agencies may not be subject to regular security reviews. Although major software purchases and contract renewals are processed through the VMO, which conducts an initial security review, no subsequent reviews are performed. Additionally, it was noted that the risk levels assigned to vendors during the initial risk assessment are not consistently measured or tracked based on their potential impact to the State. The State does conduct and participate in Quarterly Business Reviews (QBRs) as well as Technical Business Reviews (TBRs) on a routine basis with vendors. These reviews currently focus more on contractor performance and potential vendor/contractor service offerings but could be expanded to include on-going security monitoring.

Several State agencies are responsible for the administration of programs that are supported by contracted information systems. These systems are either State-owned and supported by contractor services or are third-party solutions owned and operated by vendors. The level of security reviews performed on contracted services and/or third-party solutions is inconsistent. Security oversight, for some systems, continued to improve annually with ETSS involvement.

Criteria: NIST SP 800-53 (SR-2) suggests that the supply chain, which includes vendor services (i.e., software/SaaS), represents a growing concern for organizations due to their reliance on external products, services, and systems. These risks can affect individual components, systems, or complete environments. Managing supply chain risks requires coordinated planning within agencies, including risk identification, assessment, response, planning, and ongoing monitoring. This plan should also address risk tolerance, mitigation strategies, evaluation processes, and the development of secure, trustworthy systems.

NIST SP 800-171, §.03.11.01, *Risk Assessment*, includes discussion that "risk assessments also consider risks from external parties (e.g., contractors operating systems on behalf of the organization, service providers, individuals accessing systems, and outsourcing entities)." A standard practice for the review, monitoring, and remediation of risks is through the combination of multiple tools, including but not limited to, vulnerability assessments, penetration testing, and reviewing SOC reports. While SOC reports provide assurance that service organizations are complying with their defined policies and procedures, the State also needs to evaluate whether those policies and procedures are adequate based on the inherent risk of the services being provided. As an example, if the State utilizes a contractor to operate a system that stores significant amounts of personally identifiable information (PII), the State should ensure that the contractor complies with information system security protocols deemed sufficient for the data being stored by the contractor. It is critical that these requirements are detailed in contracts with service organizations to allow for enforceability.

Condition: The State lacks a formal process to evaluate third-party software and SaaS solutions based on their potential security risks. Risk assessments are not being conducted frequently enough, leading to delays in identifying and mitigating risks. Several agencies have expressed concerns about lacking visibility into the status and operations of certain third-party SaaS products that handle sensitive data, such as PII and Payment Card Industry Data Security Standard (PCI DSS) information. Additionally, some State agencies have reported they are not conducting regular SOC 2 compliance reviews with their vendors due to not having the necessary access or expertise to adequately assess the vulnerability of the service providers they rely on.

Due to limitations in ETSS's resources, contract administration responsibilities, including IS, are left to State agencies for some of the State's critical applications. Monitoring IS for these systems is critical to the State's operations. While some agencies may review SOC reports and security scorecard results as one measure of monitoring, personnel responsible for contract oversight of those systems often lack the information systems security background needed to evaluate the adequacy of the contractor's policies and procedures or the significance of the SOC results reported.

Cause: A lack of contractor/vendor oversight exists at agency levels that utilize critical contracted IT services. Regular security reviews of vulnerabilities are not being performed uniformly or in a centralized manner to ensure timely remediation. Several agencies lack the dedicated IS resources capable of performing these critical reviews and ETSS does not have the resources needed to fully coordinate IS reviews of all contracted functions.

Effect: Without a formal process to evaluate contractors and vendors based on the criticality and risks associated with unaddressed vulnerabilities, the likelihood of a security breach increases, potentially resulting in financial losses (such as productivity setbacks or payments made), operational disruptions, loss of data integrity, reputational harm, legal consequences, and the risk of identity theft for individuals whose personal data is exposed.

RECOMMENDATIONS

2024-021a Incorporate security review updates into business reviews conducted with vendors/contractors.

2024-021b Standardize the practice for the review, monitoring, and remediation of IS risks through the combination of multiple tools, including but not limited to, vulnerability assessments, penetration testing, and reviewing SOC reports.

2024-021c Evaluate the IS resources needed to extend ETSS coordination over system security reviews for significant contractor-supported systems and third-party solutions owned and operated by vendors.

Management's Views and Corrective Actions:

2024-021a: All vendors will be required to submit a Security Questionnaire for ETSS' Security review using the Archer risk assessment tool, to gather assessment inputs and develop a risk score.

For vendors that ETSS conducts Quarterly Business Reviews (QBR) and/or Technical Business Reviews (TBR) with, ETSS will share the risk report with the vendor, and ask the vendor to provide a risk mitigation plan, if necessary.

The ETSS Security team created the attached Supply Chain Risk Management Policy, found via this link: https://rigov-policies.s3.amazonaws.com/ETSS_Policy_10-30_Supply_Chain_Risk_Management__SR_.pdf

2024-021b: ETSS has made investment within the last fiscal year to enhance their vulnerability application platform that assesses risk of exploit from code, An enhanced endpoint detection and response platform with subject matter expert services to detect exploit on laptops/desktops/servers, has enterprise scoped external penetration test scheduled to complete Q3 CY2025, self-attestation of enterprise control protections, and has implemented the initial phase of a enterprise risk management platform to centralize and standardize risk assessment for the State. In parallel with these investments the ETSS VMO team has published a new Supply Chain Risk Management Plan (SCRM) that helps set the foundation of risk mitigation with third parties. With these combined efforts the following steps occur specifically to review SOC reports:

1. *A vendor submits its Security Questionnaire that rolls up the objectives of each NIST 800-53 control family which is the State's supported security framework, which will result in the submittal of their artifacts like a SOC report, to the State's Vendor Management Office (VMO) or Agency Information Manager, which is then loaded into the Archer tool by the VMO.*
2. *A request within Archer is submitted to the ETSS Security Team for their review, to assess artifacts and responses that is then calculated by the application to provide a risk rating per engagement.*
3. *Based on the risk rating and data type protections as outline in policy PM-1, a solution is to be defined to mitigate risk or accept it with a suitable justification, which could include, but not be limited to, a request additional information and/or recommended configuration changes then*

returned to the vendor for remediation or implementation, as necessary. This effort is continued before and/or during an annual review process.

2024-021c: As part of an ongoing ETSS Leadership assessment strategic placement of resources is prioritized by critical need to meet the efforts planned with the constraints of workforce headcount allotted to ensure critical services are available to constituents and those services are secure. ETSS leadership is continuously reviewing the ability to move from a vendor led model of support on applications to managed fully within the State's workforce as we can. In the previous CY, RFPs have been posted to modernized legacy solutions aligned with our "cloud first and low code/no code" drive, have worked to set training paths to upskill the workforce to be ready to take over these functions, and have brought on new staff to help further centralize functions like vendor management, identity management, and governance. ETSS leadership have also submitted new job descriptions through the public hearing process to allow for competitive and attractive role descriptions needed to attract the talent and competencies needed. Continuing into the future ETSS Security and Application Leads and AIMs will request additional resources, and in some instances, an independent vendor may be required to perform some tasks due to complexity or niche technical skill sets.

Anticipated Completion Date: Ongoing

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INTERNAL CONTROL OVER FINANCIAL REPORTING

OTHER FUND SPECIFIC FINDINGS

Rhode Island State Employees' and Electing Teachers OPEB System

Employees' Retirement System of Rhode Island

Finding 2024-022	*(significant deficiency – repeat finding – 2023-022)*

RHODE ISLAND STATE EMPLOYEES' AND ELECTING TEACHERS OPEB SYSTEM – ASSESS THE RESOURCES AND SYSTEMS NECESSARY TO EFFECTIVELY ADMINISTER THE OPEB SYSTEM

The State has not implemented administrative processes and computer applications to effectively support the overall administration of the OPEB System. Current functions including 1) accumulating plan census data, 2) managing member eligibility, 3) determining member copays, and 4) plan enrollment functions are supported through decentralized processes that do not adequately support plan administration.

Background: The Rhode Island State Employees' and Electing Teachers OPEB System (the System), acts as a common investment and administrative agent for post-employment health care benefits provided by six plans covering state employees and certain employees of the Board of Education. In fiscal 2024, required employer and employee contributions to OPEB plans approximated $49 million, with $33 million in retiree benefits paid. OPEB assets totaled $676 million at June 30, 2024.

When the State began to advance fund its retiree health benefits, OPEB trusts were established for each of the plans and a formalized governance structure was established by statute; however, no dedicated personnel were specifically tasked with administering the System and no administrative systems were implemented at that time, or subsequently, to capture and control membership data for the various OPEB plans. Instead, membership data, the determination of eligibility for benefits and any required retiree copays are administered through a variety of processes which largely lack the controls needed to administer plans of this size and complexity.

The System's functions are managed across various units within State government. The Department of Administration's Office of Employee Benefits (OEB) currently determines eligibility and manages member benefits for the State Employees, Teachers, Judges, State Police and Legislator plans. The Human Resources Department at the University of Rhode Island separately determines eligibility, calculates benefits, and manages member subsidy receivables for the Board of Education plan. The Office of Accounts and Control handles the accounting and financial reporting aspects of the System and coordinates the actuarial valuations. The Office of the General Treasurer oversees the investment activity of the System.

The State currently manages OPEB enrollment by ensuring that all pre-65 retirees are registered in the State's Workterra software platform, which the State also utilizes to administer active employee benefits. This improvement provides systemic reporting of pre-65 enrollees and assists in ensuring their timely transition to Medicare and post-65 OPEB benefits. State employees, once enrolled in Medicare, are enrolled in Via Benefits which establishes a health savings account (HSA) for the retiree. The State funds a predetermined amount for the retiree who can utilize the funds to pay health claims or purchase Medicare gap insurance coverage. The State, however, lacks a complete system that it considers to be the official record of System enrollment.

Census data for each plan is provided to the System's actuary to prepare required actuarial valuations of the plans. Each plan has unique benefit eligibility and healthcare coverage provisions.

Criteria: As the System grows and matures, the administrative infrastructure supporting the System should be assessed to ensure adequate resources and systems with appropriate controls are in place to manage the System effectively.

Maintaining membership data and determining the eligibility for benefits and required copays should be managed through systems and processes with adequate controls to ensure that membership data is reliable, benefits are accurately and consistently determined in accordance with plan provisions, and census data is maintained to facilitate extraction for actuarial valuations. Duties should be appropriately segregated to ensure that no one individual is responsible for determining eligibility and required copays, enrolling the individual for coverage, collecting and accounting for copay amounts, and maintaining plan census data.

Condition: We identified the following control deficiencies over the various disjointed processes used to administer the OPEB plans:

- Insufficient resources have been allocated and centralized to administer the System effectively. Knowledge of key System benefit provisions, administrative operations and operating procedures are dispersed amongst too many separate units of State government without effective coordination.

- The accumulation of census data provided to the actuary for plan valuation purposes is derived from multiple sources and requires analysis of other external source data to establish the active and retiree plan members for each plan. Controls are inadequate to prevent duplicate or inaccurate census data from being provided to the actuary. The State lacks a documented comprehensive reconciliation of all System members and retirees that ensures completeness and accuracy of reported census data to the State's actuary.

- Inadequate segregation of duties exists between eligibility determinations, benefit calculations, copay receivable billings and collections, healthcare plan enrollment, and maintenance of the plan census information.

- Periodic reconciliations between the plans' records and healthcare providers enrollment data are not documented.

- Procedures for identifying and terminating coverage for deceased members, spouses and dependents are inconsistent and can be improved.

- Documentation and monitoring of user entity controls relating to functions contracted to service organizations (health insurance provider - Blue Cross / CVS Caremark, health benefits administration system - Workterra, health savings account (HSA) administrator - VIA Benefits) are lacking.

- Monitoring and analysis of OPEB liabilities reported for retirees over age 65 requires determining an estimate of the percentage of HSA commitment that is ultimately utilized by retirees over the course of their retirement to prevent overstatement of the liability amount accrued annually.

Cause: The State and System have not implemented administrative processes and computer applications to effectively support the overall administration of the OPEB System, including 1) accumulating plan census data, 2) managing member eligibility, 3) determining member copays, and 4) plan enrollment functions. Existing processes in place to support healthcare plan enrollment for active employees have generally been adopted to support the OPEB System but lack certain functions and controls that are unique to and requisite for the administration of the OPEB System.

Effect: Inadequate controls over key plan administrative functions could impact the reliability of amounts (e.g., member copays and member benefits) reported on the System's financial statements as well as the accuracy of census data used by the actuary to determine each plan's annual contribution amount and the net OPEB liability or asset for each plan.

RECOMMENDATIONS

2024-022a Assess the resources necessary to effectively manage and administer the OPEB System to ensure all System functions are met and adequately controlled.

2024-022b Implement a member benefit computer application to accumulate and manage plan membership data to support the overall administration of the OPEB System with enhanced controls.

2024-022c Evaluate assigned responsibilities for key functions and segregate certain responsibilities for incompatible functions to enhance controls over critical plan administrative functions.

2024-022d Establish consistent procedures to identify deceased plan members and prompt timely termination of coverage.

Management's Views and Corrective Actions:
Management is reviewing the recommendations and is considering administrative review and operational enhancements such as those described in the recommendations. During fiscal year 2023, steps were taken to address the finding, including the posting of a Request for Information (RFI) to solicit OPEB system assessment and software solution. Unfortunately, the responses received were inadequate. Continued efforts will be made to address the OPEB issue set forth in this report, however all resources are currently prioritized to the ERP implementation.

Anticipated Completion Date: Ongoing

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Finding 2024-023	***(significant deficiency – repeat finding – 2023-023)***

EMPLOYEES' RETIREMENT SYSTEM OF RHODE ISLAND (ERSRI) – OVERSIGHT OF THE DEFINED CONTRIBUTION PLAN

Background: The Employees' Retirement System of the State of Rhode Island (System) oversees a defined contribution (DC) plan for members which is part of the overall "hybrid" pension benefits, in conjunction with defined benefit plan benefits, for most covered employees. The DC plan is administered totally by the Teachers Insurance and Annuity Association of America (TIAA) and the System is reliant on information provided by TIAA for financial reporting purposes. No independent records are maintained by the System for the DC plan activities.

As expected, total assets of the DC plan have grown considerably since plan inception and members are beginning to withdraw funds to meet their retirement objectives. Total assets in the DC plan at June 30, 2024 totaled $2.1 billion.

Criteria: The System should have sufficient information to support effective compliance monitoring and financial reporting for the DC plan. Management is responsible for the accuracy of the System's financial reporting.

Condition: The System does not receive information on the employer remittances of employer and employee contributions to the DC plan and therefore has limited information to ensure employer compliance with the DC plan provisions. Contribution compliance monitoring should be included within the risk-assessment process to determine effective controls are in place.

Our testing in fiscal 2024 noted two instances where employer remittances to the plan administrator incorrectly coded employer and employee contribution amounts in reverse. These two employers were also noted to have employer and employee remittances coded in reverse during fiscal 2023. Since the System utilizes reporting by the plan administrator for financial reporting, incorrect employer coding results in misstatements in the financial statements. The exceptions noted continue to support a deficiency in internal control over financial reporting for the DC plan.

As the plan matures and investment assets continue to grow, the System should assess and strengthen their oversight of the DC plan to ensure 1) compliance by the plan administrator with contracted plan provisions, 2) employer compliance with plan provisions, and 3) the accuracy of reported DC plan activity in the financial statements. This should include consideration of relevant risks and the development and formalization of an oversight/monitoring plan to meet this objective. The monitoring plan should include how the plan administrator's annual Service Organization Control (SOC) Report is utilized by the System as oversight of critical defined contribution plan activities. Ensuring documentation of critical user entity controls (i.e., reviewing plan reports and ensuring reconciliation to internal records and/or plan documents) and how those controls are performed should also be documented within the plan.

Additionally, consideration should be given to modifying the existing contribution and benefit system for the defined benefit plans to also include the employer data for the DC plan before transmission to TIAA. This would facilitate monitoring of contribution data and provide independent corroboration of amounts reported by TIAA as employer and employee contributions to the plan. In the short-term, requiring employers to provide more data elements (i.e., employee wages subject to contribution) in their submissions to the plan administrator coupled with additional reporting by the plan administrator would allow the System to enhance its monitoring of employer compliance with DC plan provisions. The System indicated that it began reviewing employer contributions to the DC plan during fiscal 2024, however, those procedures were not formally documented to provide for review during our audit. The System should specifically detail the documentation requirements for monitoring procedures being implemented in response to this finding to allow for those procedures to be evaluated as controls over financial reporting.

Other plan administration areas that should be addressed in the plan to strengthen internal controls include periodic (at least monthly) analytical reviews of investment growth and performance, contributions to and distributions from the plan and fees paid. The analytical reviews should include documentation of follow-up and resolution when actual results differ from expectations.

Cause: At the inception of the DC plan, the plan design, enacted by legislation, provided for employer and employee contribution data to flow directly from the employer to TIAA without any data capture by ERSRI. The System lacks sufficient accounting and contribution data to monitor compliance (through effective control processes) with contribution requirements and to ensure the accuracy of TIAA reporting utilized to prepare the DC plan financial statements.

Effect: Material misstatements could exist in the financial statements of the DC plan and not be identified in a timely manner.

RECOMMENDATIONS

2024-023a Perform a risk assessment for the DC plan and identify areas where internal controls and oversight can be strengthened.

2024-023b Consider modifying the existing contribution and benefit system for the defined benefit plans to capture employer (employee and employer contributions) data for the DC plan or implement other procedures to enhance monitoring of employer compliance with the plan provisions.

2024-023c Formalize a DC monitoring plan to protect member plan balances, ensure compliance by the plan administrator, and enhance controls over financial reporting of the plan within the System's overall financial reporting.

Management's Views and Corrective Action Plan:
A public RFP was issued in 2023 for the State of Rhode Island Defined Contribution Retirement Plan. The Defined Contribution Plan maintained its existing relationship with TIAA and recently signed a revised contract that included requirements to provide tools to ERSRI with the ability to monitor contribution processing and add internal controls. ERSRI is working with TIAA to implement an industry standard SPARK file layout to provide internal controls for ERSRI by using reports generated by TIAA. A formalized DC monitoring plan will be documented upon completion of rollout and testing of the process.

With regard to investment activity, the State Investment Commission (SIC) contracts with a vendor that serves to monitor the investment activities of the DC plan. This vendor communicates with the Investments team regularly and reports to the SIC on a quarterly basis. ERSRI and Treasury feel confident the oversight functions performed with the vendor, the Investments team and the SIC serve as a strong monitoring process related to the investment activities of the DC plan.

While ERSRI has a robust wage and contribution processing system for the defined benefit (DB) plan, configuration to accommodate the defined contribution (DC) plan processing would require significant technical and personnel resources that cannot be funded through the DB administrative allocation consistent with R.I. Gen. Laws § 36-8-10.1. Administrative funding for the DC plan is insufficient to cover such a change.

Anticipated Completion Date: Ongoing

Contact Person: Stacey Whitton, Chief Financial Officer, ERSRI
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DISCRETELY PRESENTED COMPONENT UNITS

Finding 2024-024	***(material noncompliance – repeat finding – 2023-024)***

RHODE ISLAND CONVENTION CENTER AUTHORITY – RESTRICTIVE COVENANTS

Criteria: Bond indentures require that the Rhode Island Convention Authority (Authority) fund the Operating Reserve requirement of the restrictive covenants for the Rhode Island Convention Center (RICC) and the Amica Mutual Pavilion (AMP).

Condition: During the year ended June 30, 2024, the Authority was unable to fund the Operating Reserve requirement of the restrictive covenants for the RICC and the AMP pursuant to the indentures. The Authority is currently in violation of certain debt indentures with respect to the Operating Reserve requirement.

Cause: The Authority does not have sufficient cash flow to fund the Operating Reserve.

Effect: As a result of this fund not being funded, the Authority is in noncompliance with certain bond indentures.

RECOMMENDATION

2024-024 The auditors recommended that the Authority fund the Operating Reserve.

Management's Views and Corrective Actions:
The Authority will fund the Operating Reserve provided there is sufficient cash flow or if an alternative means of security, such as a letter of credit, is available.
Given that the Authority continues to make timely and complete debt service payments, it would make little sense for the trustee to declare a default for reserve fund noncompliance. In fact, this has been the practical practice over several years as the Authority has failed to maintain adequate reserves due to insufficient State appropriations. If a default was declared, the Authority would have 90 days to cure and would seek a legislative appropriation to remedy the default. Of course, annual appropriations in excess of debt service requirements would assist in building reserves and reaching the requirements. The Authority and its advisors are actively in search of a viable resolution to this matter.

Anticipated Completion Date: Undetermined

Contact Person: Daniel McConaughy, Executive Director, Rhode Island Convention Center Authority
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Finding 2024-025	***(significant deficiency – repeat finding – 2023-026)***

RHODE ISLAND PUBLIC TRANSIT AUTHORITY – FARE REVENUES

Criteria: The Rhode Island Public Transit Authority should reconcile the daily farebox report and GFI Software daily summary report, as well as deposits to the related documentation.

Condition: During our current year testing of fare revenue policies and procedures, we noted all the days selected had variances (some immaterial and some more than 1% of revenue) between the daily farebox report and GFI daily summary report. We also noted immaterial variances between deposits and the related documentation and discrepancies in the coin deposits to the bank.

Cause: The Authority's internal control did not have adequate policies or procedures in place to ensure the reconciliation of records timely and reviewing reporting from GFI system in comparison to deposits to correct these variances going forward.

Effect: Daily reconciliations with the farebox reports and the GFI daily summary are consistently showing variances which, if not corrected going forward, could result in material variances.

RECOMMENDATION

2024-025 The auditors recommended that the Authority enhance internal control policies and procedures to correct this process going forward.

Management's Views and Corrective Actions:
The variance is related to challenges with the existing technology used for cash collection. This system has exceeded its useful life and the Authority is actively exploring alternate options for cash collection and vaulting. More accurate information is one of the key objectives of this effort.

Anticipated Completion Date: Ongoing

Contact Person: Christopher Durand, Executive Director, Rhode Island Public Transit Authority
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Finding 2024-026 ***(significant deficiency – repeat finding – 2023-028)***

RHODE ISLAND COLLEGE – INTERNAL CONTROL OVER FINANCIAL REPORTING

Criteria: Rhode Island College (College) is responsible for financial reporting in the form of financial statements that present fairly, in all material respects, the respective financial position, changes in financial position, and statement of cash flows.

Condition: The College did not properly account for construction in progress invoices that were in accounts payable as of June 30, 2024. Per capital asset audit testing, it was identified that invoices are only included in additions when they are paid and not when they are accrued.

Cause: The College received invoices related to construction in progress after the fiscal year-end, requiring personnel to manually accrue the expenses. During this accrual process, a miscommunication regarding categorization of the accrual resulted in an understatement of construction in progress and an overstatement of operating expenses.

Effect: The College had an overstatement of expenses of $3,815,080 and an understatement of construction in progress by the same amount.

RECOMMENDATION

2024-026 The College should improve internal controls for purchasing / year-end accruals by implementing procedures to properly differentiate payables at year-end. This includes identifying accrued invoices during year-end close that relate to construction in progress in order to mitigate similar issues in the future.

Management's Views and Corrective Actions:
Management agrees with the finding and recommendation.

Anticipated Completion Date: June 30, 2025

Contact Person: Sara Enright, Interim Vice President for Administration and Finance, Rhode Island College
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Finding 2024-027	***(significant deficiency – new finding)***

COMMUNITY COLLEGE OF RHODE ISLAND – INTERNAL CONTROL OVER FINANCIAL REPORTING

Criteria: The Community College of Rhode Island (College) is responsible for financial reporting in the form of financial statements that present fairly, in all material respects, the respective financial position, changes in financial position, and statement of cash flows.

Condition: The College did not properly account for subscription-based information technology arrangements ("with terms beginning prior to July 1, 2023) under GASB Statement No. 96, *Subscription-Based Information Technology Arrangements (SBITA)*. Per SBITA audit testing, it was identified that contracts were included in additions to right-of-use assets and liabilities during fiscal year 2024 that should have been record as additions during fiscal year 2023.

Cause: The College's process for capitalization of SBITA right-of-use assets and liabilities only occurs at year-end and arrangements that qualify as a SBITA under GASB Statement No. 96 may be missed as a result.

Effect: The College had an understatement of assets of $677,435 and an overstatement of liabilities for the same amount.

RECOMMENDATION

2024-027 The College should improve internal controls for reviewing new software purchases and amendments or modifications to existing software agreements on a monthly basis to mitigate similar issues in the future. This includes identifying all software purchases that contain potential SBITAs and performing an evaluation to determine whether software in question qualify.

Management's Views and Corrective Actions:
Management agrees with the finding and recommendation and plans to hire an additional employee in the finance department to assist in this role.

Anticipated Completion Date: Ongoing

Contact Person: David Rawlinson, Controller, Community College of Rhode Island
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Finding 2024-028	***(material weakness – new finding)***

QUONSET DEVELOPMENT CORPORATION – TIMELINESS AND ACCURACY OF FINANCIAL REPORTING

Criteria: The Quonset Development Corporation should be completing monthly reconciliations on any significant transaction areas relating to the business, which should include but not be limited to, pension reporting, GASB 87 reporting and reporting of the schedule of federal expenditures.

Condition: During our current year audit, final reconciliations, in regards to the final accounting for the Corporation's new pension fund, the reporting on the schedule of federal expenditures and GASB 87 schedules with leases were delayed when the audit commenced. Based on discussions with management, the internal team was reviewing the inputs on all the Corporation leases to ensure accuracy and they also scrubbed the schedule of federal expenses to determine if expenditures were reported in the proper period.

Cause: The Corporation finance team had significant turnover in fiscal 2024, which lead to a lot of these delays in reconciliations and reporting being done timely.

Effect: The results of this process identified that a fiduciary fund for the rollout of the old pension plan into a new pension fund was not properly recorded in the financials for fiscal year 2024, which resulted in material activity being recorded to show the transfers into the plan and the payments out of the plan.

In addition, the management team reconciled the schedule of expenditures for the year noting that the prior year schedule excluded approximately $1.3m in federal expenses as well as the accrued revenue relating to this funding.

The other reconciliation item that resulted from the overall clean up on the GASB 87 lease input included variances from prior year of an understatement of assets of approximately $400k, an understatement of liabilities of approximately $530k, understatement of revenue of approximately $90k and an understatement of expense of approximately $235k.

RECOMMENDATION

2024-028 The auditors recommended that the Corporation enhance internal control policies and procedures to correct this process going forward.

Management's Views and Corrective Actions:

Since its inception in 2005 the Corporation has a strong track record of timely and accurate financial reporting. The findings outlined in this report for the current year are symptomatic of the poorly timed and unplanned exit of the Finance Director on March 5, 2024. The search for a replacement lasted until May 6, 2024. This vacancy combined with having a small accounting staff led to the challenges identified.

The efforts of the team to regroup and be diligent in its effort to provide accurate information revealed the prior year variances in both the schedule of federal expenditures and the GASB 87 schedules. While this work affected the timeliness of the audit it was important to reconcile the record to move forward.

The work completed with this GASB 87 reconciliation has resulted in the creation of detailed workbooks that will provide a sound foundation moving forward. Those workbooks are locked only to those who have intimate knowledge of how the transactions work and their financial statement impact. Three staff members are well trained and knowledgeable in this area, ensuring contingency for the future recordings necessary.

During the reporting period, the Corporation undertook an effort to terminate its defined benefit pension and payout the pensioners with their full benefit. To effectuate this, work a new pension fund was established in March 2024 to accept funds from the RI Commerce Corporation. The funds were received, and all pensioners were paid either a lump sum or provided with a lifetime annuity on or before June 30, 2024. This activity occurred during the staff vacancy and was overlooked in the year end reporting provided to the audit team. The weakness related to this pension fund has been addressed in that all transactions will be reflected on the general ledger going forward.

Notwithstanding this oversight, we are proud of the outcome. All pensioners have been paid what was due to them and the Corporation has reduced its potential future liability with the full transition of all staff to the defined contribution plan.

To avoid future challenges the Corporation is adjusting the accounting staff. In addition to engaging a new Chief Financial Officer, the Corporation has created a position for a Corporate Controller to add depth to the team should a future key personnel vacancy occur. The Corporation remains dedicated to providing timely accurate financial reporting to support its mission of operating and developing the full potential of the Business Park.

Anticipated Completion Date: Ongoing

Contact Person: Patricia Testa, Chief Financial Officer, Quonset Development Corporation
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MANAGEMENT COMMENTS

Management Comment 2024-01 ***(repeat comment – 2023-01)***

RHODE ISLAND DIVISION OF HIGHER EDUCATION ASSISTANCE (RIDHEA)

The remaining activities of the RI Division of Higher Education Assistance (RIDHEA) should be accounted for within the State's General Fund rather than as a discretely presented component unit.

In prior years, the predecessor Rhode Island Higher Education Assistance Authority performed multiple activities including acting as the guaranty agency for federally insured student loans. With federal changes to those programs some years ago, RIDHEA was created within the Office of the Postsecondary Commissioner (OPC). While the operational and financial aspects of the guaranty agency wound down, the Division continued to be reported as a discretely presented component unit with separately issued and audited financial statements. What now remains is essentially the disbursement of scholarship funds which originate from the State. RIDHEA reported net position of $49,515 at June 30, 2024, almost fully exhausting amounts reserved for future scholarships. Moving forward, RIDHEA's lone financial activity will be disbursing annual scholarships funded by the annual revenue stream from the State's 529 College Savings Plan. Revenue from the 529 College Savings Plan has been steadily declining in recent years. Reported revenues appropriated for scholarships totaled $3.9 million, $4.1 million, and $4.9 million for the fiscal years ending June 30, 2024, June 30, 2023, and June 30, 2022, respectively.

This activity could easily, and more appropriately, be reported within the State's General Fund rather than as a separate financial reporting entity. This would eliminate the additional accounting and financial reporting requirements currently maintained for RIDHEA's operations and allow OPC to administer the scholarship program through a restricted receipt account in the General Fund. In addition, accounting for the scholarship and grant program within the State's General Fund would bring those operations under the State's centralized control processes (i.e., disbursements, bank reconciliations), significantly improving the segregation of duties over program operations that are currently limited.

RECOMMENDATION

MC 2024-01 Account for the scholarship and grant activities of the Division of Higher Education Assistance – Office of Postsecondary Commissioner within the State's General Fund and eliminate the Division of Higher Education Assistance within the Office of the Postsecondary Commissioner.

Management's Views and Corrective Actions:

The Office of the Postsecondary Commissioner concurs with the Auditor General and that organizational changes of the Division merit a review of the current operations and financial reporting requirements. A structural change of this nature will need to be reviewed by legal counsel and its auditors to determine if any of the Council on Postsecondary Education's liabilities, obligations, and all other responsibilities related to the operations of the Division will need to be amended. Any findings from this review will need to be presented to the Council on Postsecondary Education for approval. In addition, the Office would request that the Auditor General provide guidance from legislative council to assist in determining the legislative changes, if any, that may require approval from the General Assembly.

Anticipated Completion Date: Ongoing

Contact Person: Zachary J. Saul, Chief Financial Officer, Office of the Postsecondary Commissioner
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Management Comment 2024-02 ***(prior finding – 2023-020)***

DISASTER RECOVERY TESTING

Further progress is needed to transition remaining systems to the disaster recovery (DR) platform and test all critical functionality of major systems, standardize application testing, and incorporate business continuity planning within the State's overall DR policy and testing.

Periodic testing of the DR plan is a vital component of an overall business continuity plan to increase the likelihood that critical systems can be restored should a disaster disable or suspend operations at the State's data center. ETSS has a designated DR facility appropriately distanced from the State's primary operational area. During fiscal 2024, the State continued the process of modernizing its hardware and procedures with the completion of its Hyperconverged Infrastructure (HCI) platform. In the new HCI platform, the State's critical data and applications are backed up to more modern datacenter server hardware located at the State's disaster recovery site as opposed to requiring local replication utilizing old legacy infrastructure (e.g., tape backups). The State now has an operational Tier 1 (restoration requires manual activities to be performed) DR/backup platform at its disaster recovery location, representing significant progress in the State's DR processes. Most mission critical systems operating within the State's data center have transitioned to this platform as of June 30, 2024.

The State needs to continue its progress to fully comply with NIST SP 800-53, which recommends performing a full DR test at least once a year. For high impact systems, testing should be done more frequently and/or whenever any significant changes are made. The State should perform readiness assessments more regularly in addition to its yearly full DR test. Further, ETSS needs to continue its implementation of this solution with the addition of agencies not yet converted to the new HCI platform. As of June 30, 2024, approximately one half of State agencies were deemed to be at stage of recoverability, which would allow for true business continuity in the event of a disaster. A list of remaining systems has been developed, and the restoration priority has been established. Most systems still pending transition continue to utilize older legacy backup procedures.

RECOMMENDATIONS

MC 2024-02a Continue to convert remaining State systems, based on priority, to the HCI DR platform.

MC 2024-02b Continue to perform complete DR testing, at a minimum annually, and more frequently for high priority systems.

MC 2024-02c Ensure that agencies have adopted formal business continuity policies and procedures that adequately address risks associated with information system service disruption or potential data breach.

Management's Views and Corrective Actions:
MC 2024-02a: We are 80% done converting ETSS state supported systems onto our HCI DR virtual platforms. The remaining systems that are not fully virtual are leveraging legacy physical technologies that are in the planning stages for decommissioning in the coming year.

MC 2024-02b: We plan to continue our DR testing schedule with our essential tier 1 platforms which does occur annual. Currently, we are working towards a disaster recovery Request for Information that will provide us modern options to increase our testing capacity and frequency.

MC 2024-02c: Our agency application team has worked with each ETSS supported agency groups to confirm they have in place a current business continuity plan. Our disaster recovery group in I&O has worked with all agency partners to ensure their latest information is correct & up to date in our scoping worksheet.

Anticipated Completion Date:
MC 2024-02a: December 31, 2025
MC 2024-02b / MC 2024-02c: Ongoing

Contact Person: *Osiris R. Gonzalez, Deputy Chief of Infrastructure, Enterprise Technology Strategy and Services, Department of Administration*
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Management Comment 2024-03	***(repeat comment – 2023-03)***

UNRESOLVED BALANCE IN THE PUBLIC SERVICE CORPORATION TAX ESCROW ACCOUNT

Efforts should continue to resolve the unidentified remaining balance in the public service corporation tax escrow account.

Telecommunication companies annually declare the net book value of their tangible assets located in Rhode Island to the Division of Municipal Finance in accordance with Rhode Island General Law § 44-13-13. The Division of Municipal Finance calculates and collects the tax due and distributes the proceeds (net of a 0.75% administrative fee) to the municipalities based on percentage of population.

The collection and disbursement of the tax proceeds are accounted for in an escrow liability account that continued to show an unresolved variance of $4.9 million at June 30, 2024. This variance has existed and remained unresolved for an extended period.

Previous efforts to determine the underlying cause of the balance have been unsuccessful and the issue remains without resolution. A portion of the balance can be attributed to the 0.75% administrative fee which has not been transferred from the account for multiple years.

RECOMMENDATION

MC 2024-03 Determine the cause of the unresolved account balance in the Public Service Corporation Tax escrow account and make any required adjustments or distributions.

Management's Views and Corrective Actions:
DOR has worked on reconstruction of this account and tracking the year-to-year balance. Continuing to review the process and will work closely with Accounts and Control to document balances.

Anticipated Completion Date: Ongoing

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Management Comment 2024-04	***(repeat comment – 2023-04)***

STANDARDIZED AGENCY CAPITAL ASSET INVENTORY POLICIES

The State should formalize annual capital asset inventory procedures for all agencies.

The Office of Accounts and Control requires departments to perform agency-specific inventory verification for capital assets on a three-year cycle. Inventory results are reported to the Office of Accounts and Control which prompts any required accounting adjustments. While this process has improved controls over financial reporting of capital assets, it has continued to highlight capital assets that could not be located or accounted for by State agencies. Improved inventory control is important for both accountability of State assets and to ensure timely reporting and removal of capital assets for financial reporting.

Such findings support ineffective tracking of capital assets by State agencies. The State should mandate requirements for the annual performance and documentation of capital asset inventories. This has become especially important with the increase in laptop and tablet use in recent years to support hybrid work schedules. The mobility of these items necessitates more frequent and thorough accountability of capital assets at the agency level.

RECOMMENDATION

MC 2024-04 Formalize and implement policies and procedures for annual capital asset inventories by State agencies.

Management's Views and Corrective Actions:
Accounts & Control through its office of Insurance Risk Management has resolicited for assistance to perform a physical inventory of all assets to ensure one complete list for capitalization and insurance purposes.

Anticipated Completion Date: December 2025

Contact Person: Jonathan Rodriguez, Insurance Risk Manager, Department of Administration, Insurance Risk
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Management Comment 2024-05 ***(repeat comment – 2023-05)***

DEPARTMENT OF LABOR AND TRAINING LEGACY SYSTEMS – BUSINESS CONTINUITY RISKS

The legacy systems utilized by the RI Department of Labor and Training (DLT) to process unemployment benefits, temporary disability insurance, and employer taxes have reached end-of-life and pose significant business continuity risks to DLT operations.

The State's administration of the unemployment insurance (UI) program is a critical function of State government. The State disbursed over $200 million in unemployment benefits in fiscal 2024 during a period of low unemployment. UI benefits during periods of high unemployment can range in the billions. This critical State system currently utilizes a front-end cloud-based application to handle benefit application functions and applicant verification processes (anti-fraud controls). The front-end application process, however, still transmits data to an antiquated legacy system that has limited system support options. The legacy system handles benefit determinations and a variety of functions (e.g., wage history, job search requirements) required to comply with federal requirements of the Unemployment Insurance Program.

The State's temporary disability insurance (TDI) program provides weekly payments to Rhode Island workers who miss work due to a non-work-related illness or injury. The State disbursed over $200 million in disability insurance payments in fiscal 2024. DLT uses a separate imaging system to store applications and medical records which does not interface with the TDI legacy system. The system determines benefit payments and is the official record for TDI claimant files and payments.

The Employer Tax Unit processes all Quarterly Tax and Wage Reports and accompanying tax payments, submitted by Rhode Island employers. The employer's "experience" with the unemployment of former employees is the dominant factor in the DLT computation of the employer's annual State UI tax rate. The computation of the employer's annual tax rate is based on State UI law and federal regulations. These payments include all required Employment Security, Job Development Fund, and Temporary Disability Insurance taxes. In fiscal 2024, the Employer Tax Unit collected over $550 million dollars in taxes paid by employers.

During fiscal 2024, the State (DLT and ETSS) worked with a consultant to complete a strategic plan to modernize the State's DLT legacy systems. The strategic plan provides a roadmap for the modernization of unemployment activities through the implementation of modules for income support and case management and customer relationship management, while interfacing with the State's new ERP system for financial management functions. The State must now adopt and approve a funding plan for implementation of the Modernization Strategic Plan, including approval from the federal government and the expected costs that could be reimbursed by federal grants.

RECOMMENDATION

MC 2024-05 Develop a complete implementation and funding plan for the DLT Systems Modernization Strategic Plan.

Management's Views and Corrective Actions:
The Department of Labor and Training is currently developing a request for proposal for this initiative which will be complete by June 30, 2024. The Department is working on securing funding.

Anticipated Completion Date: June 30, 2024 for RFP development then dependent on funding.

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Management Comment 2024-06	***(prior finding – 2023-021)***

INCIDENT RESPONSE TRAINING

The State needs to further enhance its coordination and training to improve its incident response (IR) capabilities in the event of a data breach.

A strong and well-designed IR program is required for the State to effectively respond to incidents such as a data breach initiated from outside the State network, or an insider attack on agency infrastructure and systems. Per NIST SP 800-61, a key step in establishing an incident response capability includes "staffing and training the incident response team." This includes designated agency staff as well as ETSS personnel.

At the State operations level, ETSS has an IR Plan and has trained their staff on their various responsibilities and, when appropriate, requires the agencies to be involved depending on the nature of the incident. This coordination is required under the shared services IT security model (between ETSS and individual agencies) employed by the State which requires both parties to be prepared. Depending on the nature of the incident, the agency response may need to include business continuity plan activation.

ETSS also has had an Application Review Board in place for some time and has since rebranded the entity into the Center of Excellence. The COE is where the Change Advisory Board meetings are held regarding continuous improvement processes towards IR plans for each agency. In fiscal 2024, meetings and discussions took place to improve current documentation of IR plans for each agency, which are also referred to as Continuity of Operations by some agencies. ETSS holds a high-level master document of IR plans for each agency.

Agency-level incident response training still varies widely from implemented and verifiable, to not occurring at all. Formal incident response training is essential so that all staff are clear on their roles and responsibilities in the event of an IT security incident (e.g., data breach). Progress towards maturation of a seamless IR process needs to continue. Many agencies continue to deprioritize IR training in their yearly planning. Additional focus is still needed to ensure that all designated agency personnel are properly trained and prepared to respond in the event of an incident affecting agency systems.

RECOMMENDATION

MC 2024-06 Expand incident response training to include all necessary ETSS and agency personnel to ensure proper preparation and coordination in the event of an incident impacting the State's IT operations.

Management's Views and Corrective Actions:

ETSS has updated the annual training for all users to include further information on how to respond or report an incident commensurate with their level of responsibility in an IR event. ETSS leadership also exercised the major incident response plan in September of 2023 in a critical scenario led by the Critical Infrastructure Security Agency (CISA) subject matter experts. The scenario covered an incident that started with a state service managed by a third-party compromise that expanded to the State network and further out to need municipality and public safety response with increasing simulations. This created an environment to test the capabilities of ETSS teams, Agency personnel, Governor's policy group, National Guard, public safety personnel, Federal support, and municipality stakeholders.

Anticipated Completion Date: Ongoing

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Management Comment 2024-07	***(new comment)***

INFORMATION TECHNOLOGY HARDWARE LIFECYCLE MANAGEMENT PROGRAM

The State needs to incorporate a centralized Hardware Lifecycle Management (HLM) program to improve planning, acquisition, implementation, maintenance, upgrade, and disposal of IT hardware. An HLM program, in addition to improved asset management, supports IT security and business continuity through the timely replacement of end-of-life equipment.

The State's IT environment utilizes various hardware components critical to its operation and security. These hardware components include routers, switches, servers, hubs, firewalls, intrusion detection devices, etc. The quantity of hardware components within the State's IT domain requiring management is substantial. The State needs to fully develop and incorporate a centralized HLM program to better manage its inventory of IT hardware components and ensure proper planning for replacement of end-of-life equipment that is no longer supported.

In recent years, ETSS has dedicated significant resources to replacing end-of-life equipment throughout the IT domain. This highlights the need for an HLM program that assists the State moving forward and prevents those issues from recurring in the future. Equipment budgeting and procurement, security compliance monitoring, maintenance scheduling, and inventory management would also be enhanced through an effective HLM program.

RECOMMENDATION

MC 2024-07 Implement an HLM program to effectively manage IT equipment budgeting and procurement, security compliance monitoring, maintenance scheduling, and inventory management.

Management's Views and Corrective Actions:

ETSS has an active project to improve hardware lifecycle management as part of the ITSM overhaul efforts that includes the hardware listed as well as endpoint devices. Specifically, for those listed examples there is a separate scoping effort on-going to replace the aging hardware and modernize the technology. This effort is the next phase of a longer-term replacement effort that has been replacing all network assets over the last 2 FYs.

Anticipated Completion Date: Ongoing

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Management Comment 2024-08 ***(new comment)***

TECHNOLOGY APPLICATION REVIEW NEEDED TO MINIMIZE THE NUMBER OF IT SECURITY APPLICATIONS WITH OVERLAPPING SERVICE OFFERINGS

Over time, the State has implemented various applications designed to improve IT security monitoring and remediation, however, many of these applications have similar, if not identical, functionalities. The State needs to review the various applications currently in use and develop a plan that allows for efficient utilization of less applications for IT security monitoring and remediation across its domain.

The State utilizes multiple software technologies for solutions to carry out various security monitoring and remediation services. These solutions often have overlapping service functionality and are also a factor in resource allocation and risk management/mitigation. With competing products to address the same need (monitoring, incident and vulnerability mitigation, etc.), overlapping and disparate remediation processes are inefficient. Furthermore, not having a centralized view for monitoring and mitigation puts strain on current and future human capital resources. Currently, staff are being alerted to issues in several systems, and in many cases must navigate to other systems to remediate them, which is inefficient.

The current situation with overlapping technology products has resulted from the State's previous operational model where agency support was disparate and not centrally managed. This allowed agency staff to utilize a variety of application solutions resulting in numerous competing products that perform the same function. Now that ETSS operates through a centralized support model, it needs to conduct an application review that focuses on minimizing the number of disparate applications being deployed and allows for the development of a plan that promotes a more centralized and efficient security monitoring and remediation process.

RECOMMENDATION

MC 2024-08 Review the various applications currently in use and develop a plan to streamline the number of applications being utilized, allowing for more effective and efficient IT security monitoring and remediation across the State's IT domain.

Management's Views and Corrective Actions:
ETSS has updated legacy security applications with new and enhanced platforms with the directive to resolve an gaps or findings and rationalizing the portfolio to ensure we are efficient in our monitoring. ETSS continues to unify their security portfolio as funding and resources are available with strategic expansion and funding. Also, with the implementation of revised project intake governance in 2024 all the agencies are required to go through a centralized approval process for extension, upgrade and implementation of any security tools and technologies which is governed by ETSS and DOA centrally. ETSS ensure reusability of existing tools/product and a robust Architecture principles are implemented through CISO Zero trust CoE. ETSS continues to balance this progress to ensure the tools can help efficiency, resources are adequately trained to operate the toolset, and we can scale into other features within the platform and move off legacy when ready. While the solutions reviewed in scope of the OAG team audit may have similar features as noted in the applications broad marketing or an available function listed on vendor website this does not mean these features are licensed use, the features function as needed to resolve a gap nor it is the best solution for that need, trained resources are available to leverage nor are all system compatible to that use at the current point in time, or cost prohibition exists that requires planning to evolve into those platforms overtime from incumbent solutions.

Anticipated Completion Date: Ongoing

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Management Comment 2024-09	***(new comment)***

FINANCIAL REPORTING OF UNCLAIMED PROPERTY

The State does not currently account for non-monetary unclaimed property remitted to the Office of the General Treasurer in accordance with generally accepted accounting principles (GAAP).

GAAP requires that unclaimed property held by the State be recorded within a custodial fund and that amounts be reported at fair value. While the State currently records monetary assets remitted to the State, it does not report non-monetary assets held as unclaimed property. These unclaimed assets include various types of property including jewelry, stock certificates, and coin collections, as examples.

While the Office of the General Treasurer's (Treasury) Unclaimed Property Division maintains an inventory of remitted property, it does not determine the fair value of the property held and a physical inventory of unclaimed property has not been performed in some time. In order to comply with GAAP, the Treasury will need to consider the following procedures:

- Reconcile the physical inventory of assets with the inventory listing on a regular basis;
- Determine the fair value for non-monetary assets in the Treasurer's custody;
- Determine if auctioning assets considered abandoned (not claimed within the period defined by law) is needed to prevent the volume of non-monetary assets from becoming unmanageable; and
- Include the fair value of non-monetary assets in unclaimed property reported to the Office of Accounts and Control to ensure complete and accurate reporting in the State's financial statements.

Treasury should adopt the above procedures within their official policies and procedures to ensure proper accounting controls are in place for all unclaimed property held by the State.

RECOMMENDATION

MC 2024-09 Modify existing policies and procedures relating to unclaimed property to ensure that assets remitted to the State are accounted for in accordance with GAAP.

Management's Views and Corrective Actions:
Prior to receiving this comment, Treasury planned an auction for Unclaimed Property tangible items for 2025. To that end, we issued two Requests for Proposals (RFPs), both of which are set to close in mid-March. The RFP for appraisal services will help determine the dollar value of each item currently held in our custody. Once the appraisals are completed, most, if not all, of the items will be publicly auctioned later this year. The proceeds from these sales will be assigned as cash to the rightful owner. For any items that are not sold, they will be retained in our custody until the rightful owner comes forward to claim them.

Treasury will work to incorporate these recommendations, in part or in sum, into existing policies and procedures while balancing the consideration of their budgetary and operational impact.

Anticipated Completion Date: Ongoing

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Management Comment 2024-10 **_(new comment)_**

MANAGEMENT'S RESPONSIBILITY FOR IDENTIFYING MATERIAL LAWS AND REGULATIONS

Management's identification of laws and regulations that could have a direct and material impact on the State's financial statements needs to be more comprehensive.

Generally accepted auditing standards require that auditors perform tests of the audited entity's compliance with certain provisions of laws, regulations, contracts, and grant agreements that could have a direct and material effect on the financial statements. It is the responsibility of management, with the oversight of those charged with governance, to ensure that the entity's operations are conducted in accordance with the provisions of laws and regulations, including those that specifically relate to material amounts and disclosures reported in an entity's financial statements.

For an entity the size of the State, identifying laws, regulations, contracts, and grant agreements (legal, regulatory, and contractual requirements) that could have a direct and material effect on the financial statements is challenging. To meet this responsibility in conjunction with the annual audit of the State's financial statements, we request management to provide their identification of legal, regulatory, and contractual requirements, that in their opinion, have a direct and material effect on the financial statements. The State's response to our request in recent years has been incomplete, supporting the need for more comprehensive consideration and documentation of legal, regulatory, and contractual requirements to demonstrate management's responsibilities in this area.

The State needs to conduct a comprehensive review of legal, regulatory, and contractual requirements and adequately document those that could have a direct and material effect on the financial statements. The State should also document any related procedures that ensure the State's compliance with these requirements in conjunction with the State's documentation of internal control. Once completed, this documentation will require annual update for newly adopted requirements or changes to existing laws, regulations, or contracts.

RECOMMENDATION

MC 2024-10 Conduct a comprehensive review of legal, regulatory, and contractual requirements and adequately document those that could have a direct and material effect on the financial statements.

Management's Views and Corrective Actions:
The Department of Administration will begin a regularly scheduled meeting that involves the Office of Accounts and Control, Office of Management and Budget, and Division of Legal Services to improve controls and identification of those items noted in the comment above which could have a significant impact on the financial statements.

Anticipated Completion Date: July 1, 2026

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Management Comment 2024-11 **_(new comment)_**

POLLUTION REMEDIATION OBLIGATIONS

The State's identification and recording of pollution remediation obligations, which relies on data and information from multiple agencies, does not adequately document all considerations required by accounting standards.

The State reports pollution remediation obligations in the financial statements annually. Documentation submitted to the Office of Accounts and Control by agencies responsible for monitoring and performing pollution remediation is incomplete and lacks the formalization needed to support the considerations required by accounting standards. The following are areas where the State needs to improve its documentation:

- All potential pollution sites monitored by the Department of Environmental Management should be evaluated, documenting whether an "obligating event" exists in relation to those sites, and whether the State is responsible for monitoring and/or remediation activities. Obligating events can occur due to public health and welfare regardless of whether the polluted site is State-owned. The State's specific responsibilities for monitoring and/or remediation should be documented for each site.

- Recognition benchmarks, including annual revisions, that support the range of liability related to each site that the State is obligated for should be identified and documented.

- The estimation method used and the support of the estimated future costs, based on the appropriate recognition benchmark reached in the remediation process, should be included in the documentation.

Documentation needs to be improved to support the completeness and accuracy of pollution remediation liabilities reported in the financial statements.

RECOMMENDATION

MC 2024-11 Improve documentation supporting the completeness and accuracy of pollution remediation obligations reported in the financial statements.

Management's Views and Corrective Actions:
We agree with the auditors' comments, and the following actions have already begun or will be taken to improve the situation:

Estimates and other information on existing projects are not all streamlined as every project is treated differently. RIDOT will investigate providing a standardized format to make the necessary information as transparent as possible. Internally, RIDOT, will complete annual reviews of projects that include pollution remediation. The Finance Dept will coordinate with the various Project Managers assigned and update information as necessary. RIDOT will strive to include RIDEM more frequently throughout the fiscal year with updates and revisions to existing projects.

As an initial step, the Rhode Island Department of Environmental Management's Office of Land Revitalization and Sustainable Materials Management (LRSMM) and staff persons from the Rhode Island Department of Transportation (RIDOT) recently met and reviewed all LRSMM site numbers and cross-referenced them with RIDOT project number records to ensure that the listing maintained by both agencies was comprehensive. By ensuring that both agencies have records pertaining to the same sites, greatly reduces the discrepancies found in reported estimated costs. LRSMM and RIDOT are currently performing additional internal review and intend to meet again to further evaluate the cost estimate data for all sites. Once LRSMM and RIDOT agree as it relates to the estimated cost for each site's remediation and current level of completion both agencies will be able to provide more well-informed estimates annually. LRSMM hopes to maintain clear lines of communication and transparency with RIDOT by having periodic update meetings on all remediation sites going forward.

Anticipated Completion Date: June 30, 2025

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