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FINANCIAL AND COMPLIANCE AUDIT REPORT

State of Kansas
Fiscal Year 2008

A Report to the Legislative Post Audit Committee
By the Joint Venture of Allen, Gibbs & Houlik and
Berberich Trahan & Co., Under Contract with the
Legislative Division of Post Audit
State of Kansas
February 2009

Legislative Post Audit Committee
Legislative Division of Post Audit

The Legislative Post Audit Committee and its audit agency, the Legislative Division of Post Audit, are the audit arm of Kansas government. The programs and activities of State government now cost about $10 billion a year. As legislators and administrators try increasingly to allocate tax dollars effectively and make government work more efficiently, they need information to evaluate the work of government agencies. The audit work performed by Legislative Post Audit helps provide that information.

We conduct our audit work in accordance with applicable government auditing standards set forth by the U. S. Government Accountability Office. These standards pertain to the auditor's professional qualifications, the quality of the audit work, and the characteristics of professional and meaningful reports. These audit standards have been endorsed by the American Institute of Certified Public Accountants and adopted by the Legislative Post Audit Committee.

The Legislative Post Audit Committee is a bipartisan committee comprising five senators and five representatives. Of the Senate members, three are appointed by the President of the Senate and two are appointed by the Senate Minority Leader. Of the representatives, three are appointed by the Speaker of the House and two are appointed by the House Minority Leader.

As part of its audit responsibilities, the Division is charged with meeting the requirements of the Legislative Post Audit Act which address audits of financial matters. Those requirements call for two major types of audit work.

First, the Act requires an annual audit of the State's financial statements. Those statements, prepared by the Department of Administration's Division of Accounts and Reports, are audited by a certified public accounting firm under contract with the Legislative Division of Post Audit. The firm is selected by the Contract Audit Committee, which comprises three members of the Legislative Post Audit Committee (including the Chairman and Vice-Chairman), the Secretary of Administration, and the Legislative Post Auditor. This audit work also meets the State's audit responsibilities under the federal Single Audit Act.

Second, the Act provides for a regular audit presence in every State agency by requiring that audit work be conducted at each agency at least once every three years. Audit work done in addition to the annual financial statement audit focuses on compliance with legal and procedural requirements and on the adequacy of the audited agency's internal control procedures. These compliance and control audits are conducted by the Division's staff under the direction of the Legislative Post Audit Committee.

LEGISLATIVE POST AUDIT COMMITTEE

Representative Virgil Peck Jr., Chair
Representative Tom Burroughs
Representative John Grange
Representative Peggy Mast
Representative Tom Sawyer

Senator Terry Bruce, Vice-Chair
Senator Anthony Hensley
Senator Derek Schmidt
Senator Chris Steineger
Senator Dwayne Umbarger

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Barbara J. Hinton, Legislative Post Auditor

DO YOU HAVE AN IDEA FOR IMPROVED GOVERNMENT EFFICIENCY OR COST SAVINGS?

The Legislative Post Audit Committee and the Legislative Division of Post Audit have launched an initiative to identify ways to help make State government more efficient. If you have an idea to share with us, send it to ideas@lpa.state.ks.us, or write to us at the address above.

You won't receive an individual response, but all ideas will be reviewed, and Legislative Post Audit will pass along the best ones to the Legislative Post Audit Committee.

The Legislative Division of Post Audit supports full access to the services of State government for all citizens. Upon request, Legislative Post Audit can provide its audit reports in large print, audio, or other appropriate alternative format to accommodate persons with visual impairments. Persons with hearing or speech disabilities may reach us through the Kansas Relay Center at 1-800-766-3777. Our office hours are 8:00 a.m. to 5:00 p.m., Monday through Friday.

LEGISLATURE OF KANSAS

LEGISLATIVE DIVISION OF POST AUDIT

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February 11, 2009

To: Members, Legislative Post Audit Committee

Representative Virgil Peck, Chair
Representative Tom Burroughs
Representative John Grange
Representative Peggy Mast
Representative Tom Sawyer

Senator Terry Bruce, Vice-Chair
Senator Anthony Hensley
Senator Derek Schmidt
Senator Chris Steineger
Senator Duane Umbarger

This report contains significant findings, conclusions, and recommendations from the completed Statewide audit covering fiscal year 2008. This audit was conducted by the joint venture of Allen Gibbs & Houlik and Berberich Trahan & Co., audit firms under contract with the Legislative Division of Post Audit.

The report discusses key aspects regarding the conduct of the audit, but makes no recommendations. We would be happy to discuss any items in the report with any legislative committees, individual legislators, or other State officials.

Barbara J. Hinton
Legislative Post Auditor

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Attention: Legislative Post Audit Committee

We are pleased to present this report related to our audit of the basic financial statements of the State of Kansas (State) for the year ended June 30, 2008. This report summarizes certain matters required by professional standards to be communicated to you in your oversight responsibility for the State of Kansas' financial reporting process. Also included is a summary of recently issued accounting standards that may affect future financial reporting by the State.

Required Communications

Statement on Auditing Standards No. 114 requires the auditor to communicate certain matters to keep those charged with governance adequately informed about matters related to the financial statement audit that are, in our professional judgment, significant and relevant to the responsibilities of those charged with governance in overseeing the financial reporting process. The following summarizes these communications.

Auditor's Responsibility Under Professional Standards

Our responsibility under auditing standards generally accepted in the United States of America *Government Auditing Standards* issued by the Comptroller General of the United States; the provisions of the Single Audit Act; OMB Circular A-133; OMB's *Compliance Supplement* has been described to you in our arrangement letter dated June 26, 2008.

Accounting Policies

Management has the ultimate responsibility for the appropriateness of the accounting policies used by the State. The State's significant accounting policies are discussed in Note 1 to the financial statements.

In the current year, the State adopted the following Governmental Accounting Standards Board (GASB) Statements:

- GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Post-Employment Benefits Other Than Pensions.* This Statement establishes uniform financial accounting and reporting standards for other post-employment benefit plans (OPEB plans) and supersedes existing guidance. See also Note IV to the financial statements.

- GASB Statement No. 48, *Sales and Pledges of Receivables and* Future *Revenues and Intra-Entity Transfers of Assets and Future Revenues.* This Statement establishes accounting and financial reporting standards for transactions in which a government receives, or is entitled to, resources in exchange for future cash flows generated by collecting specific receivables or specific future revenues. It also provides disclosure requirements for a government that pledges or commits future cash flows from a specific revenue source.

Significant or Unusual Transactions

We did not identify any significant or unusual transactions or significant accounting policies in controversial or emerging areas for which there is a lack of authoritative guidance or consensus.

Alternative Treatments Discussed with Management

We did not discuss with management any alternative treatments within generally accepted accounting principles for accounting policies and practices related to material items during the current audit period.

Management's Judgments and Accounting Estimates

Accounting estimates are an integral part of the preparation of financial statements and are based upon management's current judgment. The process used by management encompasses their knowledge and experience about past and current events and certain assumptions about future events. Management may wish to monitor throughout the year the process used to compute and record these accounting estimates. Estimates significant to the financial statements include such items as:

- Taxes receivable
- Incurred but not reported claims
- Arbitrage liabilities
- Depreciation

Audit Adjustments

There were no audit adjustments made to the original trial balance presented to us to begin our audit.

Uncorrected Misstatements

There were no uncorrected misstatements accumulated during the course of the audit.

Management Representations

In connection with our audit procedures, we have obtained a written management representation letter. This representation letter constitutes written acknowledgments by management that it has the primary responsibility for the fair presentation of the financial statements in conformity with generally accepted accounting principles. The representation letter also includes the more significant oral representations made by officers and employees during the course of the audit and includes specific representations, is intended to reduce the possibility of misunderstandings between us and the State and reminds the signing officers to consider seriously whether all material liabilities, commitments and contingencies or other important financial information have been brought to our attention.

Other Disclosures

We encountered no disagreements with management over the application of significant accounting principles, the basis for management's judgments on any significant matters, the scope of the audit or significant disclosures to be included in the financial statements; we are not aware of any consultations management had with other accountants about accounting or auditing matters; no significant issues arising from the audit were discussed or were the subject of correspondence with management; and we did not encounter any difficulties in dealing with management relating to the performance of the audit.

Closing

This report is intended solely for the information and use of the Legislative Post Audit Committee and management and is not intended to be and should not be used by anyone other than these specified parties. It will be our pleasure to respond to any questions you have regarding this report. We appreciate the opportunity to continue to be of service to the State of Kansas.

Allen, Gibbs & Houlik, L.C.
CERTIFIED PUBLIC ACCOUNTANTS

Berberich Trahan, & Co. P.A.
CERTIFIED PUBLIC ACCOUNTANTS

Wichita, KS
January 16, 2009

Recently Issued Accounting Standards

The GASB has issued several statements not yet implemented by the State. The State's management has not yet determined the effect these Statements will have on the State's financial statements. However, the State plans to implement all standards by the required dates. The Statements which might impact the State are as follows:

GASB Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations*

This Statement issued November 2006, will be effective for the State beginning with its fiscal year 2009. This Statement addresses accounting and financial reporting standards for pollution (including contamination) remediation obligations, which are obligations to address the current or potential detrimental effects of existing pollution by participating in pollution remediation activities, such as site assessments and cleanups. This standard requires the government to estimate the components of expected pollution remediation outlays and determine whether the outlays for those components should be accrued as a liability or, if appropriate, capitalized when goods and services are acquired.

GASB Statement No. 51, *Accounting and Financial Reporting for Intangible Assets*

This Statement issued July 2007, will be effective for the State beginning with its fiscal year 2010. This Statement provides guidance regarding how to identify, account for and report intangible assets. The new standard characterizes an intangible asset as an asset that lacks physical substance, is nonfinancial in nature and has an initial useful life extending beyond a single reporting period. The requirements of GASB 51 for the most part require retroactive application.

GASB Statement No. 52, *Land and Other Real Estate Held as Investments by Endowments*

This Statement issued November 2007, will be effective for the State beginning with its fiscal year 2009. This Statement establishes consistent standards for the reporting of land and other real estate held as investments. Endowments were previously required to report their land and other real estate held for investment purposes at historical cost. However, such investments are reported at fair value by similar entities, such as pension plans. The Statement requires endowments to report land and other real estate investments at fair value. The changes in the fair value are to be reported as investment income.

GASB Statement No. 53, *Accounting and Financial Reporting for Derivation Instruments*

The Statement issued June 2008, will be effective for the State beginning with its fiscal year 2010. This Statement requires governments to measure most derivative instruments at fair value in their financial statements. The methods of evaluating the effectiveness of hedging derivative instruments are also addressed.