

State of Arizona

CONCLUSION: The State of Arizona is responsible for preparing its annual financial report and a federal expenditure schedule, maintaining effective internal controls, and being accountable for its use of public monies. Our Office is responsible for auditing the State's financial statements, schedule, and major federal programs annually. A summary of the State's financial statements and federal expenditure schedule is presented below.

Based on our audits, we issued opinions on the State's financial statements and federal expenditure schedule and issued reports on internal control and on compliance over financial reporting and major federal programs. The information in the State's fiscal year 2016 financial statements and schedule is reliable. Our Office identified internal control weaknesses over financial reporting and internal control weaknesses and instances of noncompliance over major federal programs. The most significant findings are summarized on the next page.

Condensed financial information

Statement of net position—This statement reports all of the State's assets, deferred outflows of resources, liabilities, deferred inflows of resources, and net position. Net position is reported in three major categories:

- **Net investment in capital assets**—shows the equity in land, buildings, equipment, and infrastructure.
- **Restricted**—shows the resources that must be used for restricted purposes as specified by donors and other external entities, such as the federal government.
- **Unrestricted**—shows the remaining net position balance after allocating the net investment in capital assets and restricted balances.

Statement of activities—This statement reports all revenues, expenses, and other changes in net position. Revenues include program revenues—those generated by or dedicated to a specific program—and general revenues, such as taxes raised for general purposes. It also reports revenues and expenses as either governmental activities—primarily supported by taxes and grant monies—or business-type activities—primarily supported by user fees and charges. Net position increased by \$1.6 billion, or 6.8 percent, in fiscal year 2016.

Federal expenditure schedule—During fiscal year 2016, the State expended approximately \$16 billion in federal awards. The State's federal award expenditures increased by \$777 million, or 5.1 percent, compared to fiscal year 2015.

Statement of net position As of June 30, 2016 (In millions)

Assets and deferred outflows	
Current and other assets	\$ 17,133
Capital assets, net of depreciation	28,047
Deferred outflows of resources	1,002
Total assets and deferred outflows	46,182
Liabilities and deferred inflows	
Current liabilities	5,811
Noncurrent liabilities:	
Net pension liability	5,234
Other	9,973
Deferred inflows of resources	563
Total liabilities and deferred inflows	21,581
Net position	
Net investment in capital assets	21,484
Restricted	8,048
Unrestricted (deficit)	(4,931)
Total net position	\$24,601

Statement of activities Year ended June 30, 2016 (In millions)

Program revenues	
Governmental activities	\$15,594
Business-type activities	5,452
General revenues	
Governmental activities	13,809
Business-type activities	676
Total revenues	35,531
Expenses	
Governmental activities	28,305
Business-type activities	5,653
Total expenses	33,958
Change in net position	1,573
Net position—beginning, as restated	23,028
Net position—ending	\$24,601

Federal expenditure schedule Year ended June 30, 2016 (In millions)

Federal grantor agency	
Department of Health and Human Services	\$ 9,882
Department of Agriculture	2,137
Department of Education	2,064
Department of Transportation	811
Department of Labor	404
Other	658
Total federal expenditures	\$15,956

Understanding the State's financial report

Understanding how to extract information from the State's financial report is important when reviewing financial performance and evaluating future financial decisions. As described below, our Office's financial report user guide and internal control and compliance reports user guide, available at azauditor.gov under reports and publications, help users identify and understand important and useful information in the State's financial report and our reports on internal control and on compliance over financial reporting and federal programs. Specifically:

- **Financial report user guide**—describes key financial information contained in the state financial reports and indicates where to find this information. Key components in a financial report include the independent auditors' report, management's discussion and analysis, government-wide financial statements, fund financial statements, notes to financial statements, and other required supplementary information.
- **Internal control and compliance reports user guide**—describes our internal control and compliance reports over financial reporting and federal programs. Those reports, which are included in our single audit report, provide information about whether the State has effective internal control procedures and whether it has complied with certain financial- and federal-related laws and regulations.

Summary of audit findings and recommendations

For the financial statement audit, we found internal control weaknesses over the State's financial reporting related to its financial statement preparation and information technology (IT) resources. For the federal compliance audit, we tested 22 federal programs under the major program guidelines established by the Single Audit Act and found that the State did not always have adequate internal controls and did not always comply with federal program requirements for some of its federal programs. Our single audit report includes a schedule of findings and questioned costs that contains further details to help the State correct these internal control weaknesses and instances of noncompliance. Our findings and recommendations over IT resources are summarized below.

The State had inadequate policies and procedures over IT resources—The State's IT resources, which include its systems, network, infrastructure, and data, are vital to its daily operations. We reviewed the IT controls at the Departments of Administration, Economic Security, Child Safety, and Revenue (agencies) and found that these agencies did not have adequate policies and procedures to effectively identify, analyze, and respond to risks that may impact their IT resources; to sufficiently manage access, including preventing, detecting, and responding to unauthorized access; and to track, document, and test IT resource changes. These agencies also lacked comprehensive up-to-date contingency plans to provide for the continuity of operations in the event of a disaster, system or equipment failure, or other interruption.

Recommendations

To help ensure these agencies have adequate internal controls over their IT resources to identify, analyze, and respond to risks; prevent and detect unauthorized access; prevent and detect unauthorized, inappropriate, or unintended changes; and ensure their operations can continue in the event of a disaster, system or equipment failure, or other interruption, these agencies need to update their policies and procedures over their IT resources to ensure they address the following:

- **Risk-assessment process**—The risk-assessment process should include the identification of risk scenarios, including the scenarios' likelihood and magnitude.
- **Sensitive information**—Security measures should be developed to identify, classify, and inventory sensitive information and protect it.
- **Logging and log monitoring**—Key user activity should be logged and monitored, particularly for users with administrative access privileges and remote access.
- **User access**—A periodic, comprehensive review should be performed of all existing employee accounts to help ensure that network access granted is needed and compatible with job responsibilities.
- **Configuration management**—Changes made to IT resources should be logged and documented, and a record should be retained of all change details.
- **Contingency planning**—The contingency plan should be updated at least annually for all critical information or when changes are made to IT resources, and updates to the plan should be communicated to key personnel.
- **IT standards and best practices**—IT policies and procedures should be reviewed against current IT standards and best practices, updated where needed, and implemented entity-wide, as appropriate.