OLA

OFFICE OF THE LEGISLATIVE AUDITOR
STATE OF MINNESOTA

Management Letter

Department of Administration

Fiscal Year Ended June 30, 1999

FEBRUARY 24, 2000 **00-03**

Financial Audit Division

The Office of the Legislative Auditor (OLA) is a professional, nonpartisan office in the legislative branch of Minnesota State government. Its principal responsibility is to audit and evaluate the agencies and programs of state government (the State Auditor audits local governments).

OLA's Financial Audit Division annually audits the state's financial statements and, on a rotating schedule, audits agencies in the executive and judicial branches of state government, three metropolitan agencies, and several "semi-state" organizations. The division also investigates allegations that state resources have been used inappropriately.

The division has a staff of approximately fifty auditors, most of whom are CPAs. The division conducts audits in accordance with standards established by the American Institute of Certified Public Accountants and the Comptroller General of the United States.

Consistent with OLA's mission, the Financial Audit Division works to:

- Promote Accountability,
- Strengthen Legislative Oversight, and
- Support Good Financial Management.

Through its Program Evaluation Division, OLA conducts several evaluations each year and one best practices review.

OLA is under the direction of the Legislative Auditor, who is appointed for a six-year term by the Legislative Audit Commission (LAC). The LAC is a bipartisan commission of Representatives and Senators. It annually selects topics for the Program Evaluation Division, but is generally not involved in scheduling financial audits.

All findings, conclusions, and recommendations in reports issued by the Office of the Legislative Auditor are solely the responsibility of the office and may not reflect the views of the LAC, its individual members, or other members of the Minnesota Legislature.

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If you have comments about our work, or you want to suggest an audit, investigation, evaluation, or best practices review, please contact us at 651-296-4708 or by e-mail at auditor@state.mn.us

OLA **OFFICE OF THE LEGISLATIVE AUDITOR**
STATE OF MINNESOTA • James Nobles, Legislative Auditor

Report Summary

Management Letter

Department of Administration
Fiscal Year Ended June 30, 1999

Key Findings and Recommendations:

- Certain divisions did not adequately maintain their accounts receivable balances. Plant Management and the Financial Management and Reporting Division should reconcile the accounts receivable balances recorded on MAPS and on its manual general ledger. Also, PrintComm should pursue its old accounts receivable and write off accounts when it exhausts all collection efforts. (Finding 1, page 2)

- The Building Construction Division did not ensure that the state's accounting system assigned accurate object codes to new building construction expenditures. The department should correctly code building construction expenditures in the state's accounting system and accurately report building construction financial activity to the Department of Finance. (Finding 2, page 3)

- The Risk Management Division did not obtain an actuarial evaluation of its contributions to reserves for the past two years. The Risk Management Division should have an actuary ensure that its annual calculation of reserves is based on sound actuarial principles. Actuarial reviews should occur at least biennially as required by the federal government. (Finding 3, page 3)

- Some scheduled batch jobs run from outside the InterTechnologies Group's secured computer environment. InterTech should secure all scheduled batch jobs to prevent unauthorized modifications. (Finding 4, page 4)

- InterTech does not have formal procedures to control changes to production batch streams. InterTech should document specific agency liaisons that must approve changes to each production batch stream. (Finding 5, page 5)

Management letters address internal control weaknesses and noncompliance issues found during our annual audit of the state's financial statements and federally-funded programs. The scope of work in individual agencies is limited. During the fiscal year 1999 audit, our work at the Department of Administration focused on selected components of the state's Internal Services Fund, selected building construction projects, and certain controls over the scheduled batch processing computer environment. The department's response to our recommendations is included in the report.

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Audit Participation

The following members of the Office of the Legislative Auditor prepared this report:

Claudia Gudvangen, CPA	Deputy Legislative Auditor
Jeanine Leifeld, CPA, CISA	Audit Manager
Chris Buse, CPA, CISA	Audit Manager
Laura Peterson, CPA	Auditor-in-Charge
Carl Otto, CPA, CISA	Auditor-in-Charge
Crystal Eskridge	Auditor
Martha Moore	Intern

Exit Conference

We discussed the findings and recommendations in this report with the following staff of the Department of Administration on February 8, 2000:

David Fisher	Commissioner
Kirsten Cecil	Deputy Commissioner
Kent Allin	Assistant Commissioner
Jack Yarbrough	Assistant Commissioner
Larry Freund	Director of Financial Management
Julie Poser	Accounting Director
Judy Hunt	Internal Auditor

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Representative Dan McElroy, Chair
Legislative Audit Commission

Members of the Legislative Audit Commission

Mr. David Fisher, Commissioner
Department of Administration

We have performed certain audit procedures at the Department of Administration as part of our audit of the financial statements of the State of Minnesota as of and for the year ended June 30, 1999. We have also reviewed certain department procedures related to the state's compliance with the requirements described in the U.S. Office of Management and Budget (OMB) *Circular A-133 Compliance Supplement* that are applicable to the department for the year ended June 30, 1999. We emphasize that this has not been a comprehensive audit of the Department of Administration.

Table 1-1 identifies the financial activities within the Department of Administration that were material to the state's financial statements. We performed certain audit procedures on these activities as part of our objective to obtain reasonable assurance about whether the State of Minnesota's financial statements for the year ended June 30, 1999, were free of material misstatement.

Table 1-1
Activities Material to the State's Financial Statements
Fiscal Year 1999

Revenue Areas	Amount
InterTechnologies Fund sales revenue	$ 74,713,000
Plant Management Fund lease revenue	31,068,000
Travel Management Fund vehicle rental revenue	8,603,000
Central Stores Fund sales revenue	7,979,000
PrintComm Fund sales revenue	6,599,000
Risk Management Fund insurance revenue	6,491,000
Expense/Expenditure Areas	
Building Construction Division expenditures **(1)**	$109,677,000
InterTechnologies Fund:	
Purchased services	44,526,000
Depreciation **(2)**	9,646,000
Plant Management Fund purchased services	8,585,000
Central Stores Fund cost of goods sold	6,315,000
Travel Management Fund vehicle depreciation **(2)**	4,526,000

(1) Selected projects.
(2) Our audit scope also included the InterTechnologies Fund and Travel Management Fund fixed asset balances at June 30, 1999. Those net fixed asset balances were $15,004,000 and $15,667,000, respectively.

Source: State of Minnesota Comprehensive Annual Financial Report for the year ended June 30, 1999.

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Department of Administration

Our financial statement audit work in the Department of Administration also included a review of selected computer-related control activities. The specific controls that we examined help ensure the integrity of data in the state's major financial systems, including the Minnesota Accounting and Procurement System (MAPS). In many cases, the Department of Administration's InterTechnologies Group worked with other state agencies to design these computer-related controls. During this audit, we examined controls over scheduled batch processing. We also reviewed MAPS access controls.

We conducted our audit in accordance with generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Conclusions

Our December 1, 1999, report included an unqualified opinion on the State of Minnesota's general purpose financial statements included in its Comprehensive Annual Financial Report for the year ended June 30, 1999. In accordance with *Government Auditing Standards*, we also issued our report, dated December 1, 1999, on our consideration of the State of Minnesota's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grants. At a later date, we will issue our report on compliance with requirements applicable to each major federal program and internal control over compliance in accordance with OMB Circular A-133.

As a result of our audit procedures, we identified the following weakness in internal control and an instance of noncompliance with federal requirements at the Department of Administration:

1. Certain divisions did not adequately maintain their accounts receivable balances.

As of June 30, 1999, one division had not reconciled its accounts receivable balances. Another division had old outstanding accounts receivable that had not been adequately pursued.

Plant Management did not regularly reconcile its account receivable balance as recorded on the state's accounting system (MAPS) to its general ledger. Plant Management used the MAPS advanced receivable module to invoice customers and record customer receipts. The account receivable balance on MAPS is the sum of all unpaid invoices. The Financial Management and Reporting Division also recorded Plant Management financial activity on a manual general ledger. The account receivable balances on the general ledger should agree with the amounts recorded on MAPS. However, the subsequent reconciliation of these two balances resulted in a $335,000 adjustment to the financial statement accounts receivable amount. The $335,000 difference may be due to the timing of transactions or errors in recording activity. It is important to perform periodic reconciliations to find and correct these differences.

As of June 30, 1999, $107,622 of PrintComm's account receivable balance was over 90 days old. Most of these receivables were due from other state agencies and some dated back to 1994. PrintComm did not have specific collection procedures in its account receivable policy. The subsequent review of outstanding accounts receivable resulted in a $26,000 write-off.

Recommendations

- *Plant Management and the Financial Management and Reporting Division should reconcile the accounts receivable balances recorded on MAPS and on its manual general ledger.*

- *PrintComm should pursue its old accounts receivable and write off accounts when it exhausts all collection efforts.*

2. The Building Construction Division did not ensure that the state's accounting system assigned accurate object codes to new building construction expenditures.

The Building Construction Division allowed MAPS, the state's accounting system, to automatically code new building construction as land improvements. Of the $110 million paid for nine different construction projects we tested, the system recorded nearly $53 million erroneously as land improvements. The errors occurred when the division did not change the default code that MAPS automatically assigned to certain building construction expenditures. Because of the coding errors, the Department of Administration did not accurately report construction in progress amounts to the Department of Finance, risking inaccurate reporting of capital outlay expenditures on the state's financial statements.

Recommendation

- *The department should correctly code building construction expenditures in the state's accounting system and accurately report building construction financial activity to the Department of Finance.*

3. The Risk Management Division did not obtain an actuarial evaluation of its contributions to reserves in the past two years.

The federal government's Office of Management and Budget Circular A-87 sets cost principles for payments from federal awards. The circular requires the following, in order for risk management costs to be allowable:

> Contributions to reserves must be based on sound actuarial principles using historic experience and reasonable assumptions. Reserve levels must be analyzed and updated at least biennially for each major risk being insured and take into account reinsurance, coinsurance, etc.

In the past, the Risk Management Division has periodically had an actuary from the Department of Commerce review the division's calculations for setting billing rates. However, in the past two years, the division did not have an actuary certify that the billing rates were based on sound actuarial principles. State programs that receive federal funding may not be able to participate in the state's self-insurance program without the required actuarial evaluations.

Recommendation

- *The Risk Management Division should have an actuary ensure that its annual calculations of reserves are based on sound actuarial principles. Actuarial reviews should occur at least biennially as required by the federal government.*

4. PRIOR FINDING PARTIALLY RESOLVED: Some scheduled batch jobs run from outside InterTech's secured computer environment.

As of July 1999, 22 percent of the state's scheduled batch jobs were initiated from an unsecured "test" environment. InterTech will not move scheduled batch jobs into its secure production environment until they comply with certain documentation standards. However, agencies can run scheduled batch jobs on a temporary basis from the test environment until they meet the more rigorous production standards. Since our last audit, InterTech implemented additional security features to protect scheduled batch jobs in the test environment. However, we reviewed scheduled batch job documentation and found many jobs that were not protected by these new security features.

A special type of computer program, written in IBM's Job Control Language (JCL), initiates each scheduled batch job. It is extremely important to prevent unauthorized changes to JCL programs because they contain a logonID that gives each job its security clearance. JCL programs also list the specific name and location of all the other computer programs that must execute within each job. Unauthorized changes to any of these JCL program components could result in serious disruptions of critical government services or the widespread destruction of data.

Recommendation

- *InterTech should secure all scheduled batch jobs to prevent unauthorized modifications.*

5. PRIOR FINDING PARTIALLY RESOLVED: InterTech does not have formal procedures to control changes to production batch streams.

InterTech controls the secure production environment that houses agency job streams. As instructed by agencies, InterTech moves scheduled batch jobs into this environment and makes changes to existing jobs. However, InterTech does not maintain a list of agency information systems professionals who have the authority to initiate these production batch stream modifications. Instead, InterTech's information system professionals rely on informal relationships that have been established with state agencies over time.

It is important to document specific agency liaisons for each production batch stream. This documentation will help InterTech ensure that it only makes authorized batch stream changes. Documentation will also help prevent future disruptions in the batch job migration process, should key InterTech employees leave state service.

Recommendation

- *InterTech should document specific agency liaisons that must approve changes to each production batch stream.*

This report is intended for the information of the Legislative Audit Commission and the management of the Department of Administration. This restriction is not intended to limit the distribution of this report, which was released as a public document on February 24, 2000.

/s/ James R. Nobles

James R. Nobles
Legislative Auditor

/s/ Claudia J. Gudvangen

Claudia J. Gudvangen, CPA
Deputy Legislative Auditor

End of Fieldwork: December 1, 1999

Report Signed On: February 18, 2000

Status of Prior Audit Issues As of December 1, 1999

January 4, 1999, Legislative Audit Report 99-1 examined the Department of Administration's activities and programs material to the State of Minnesota's general purpose financial statements for the year ended June 30, 1998**.** The report contained two findings. The Department of Administration resolved both of these findings.

September 15, 1998, Legislative Audit Report 98-52 analyzed scheduled batch processing procedures within the Department of Administration's InterTechnologies Group and within the Department of Finance. Scheduled batch processing is a special type of computing environment that requires little or no user interaction. The report contained two findings addressed to the Department of Administration. We found that the department had not completely resolved these findings. They are repeated as findings 4 and 5 in this report.

State of Minnesota Audit Follow-Up Process

The Department of Finance, on behalf of the Governor, maintains a quarterly process for following up on issues cited in financial audit reports issued by the Legislative Auditor. The process consists of an exchange of written correspondence that documents the status of audit findings. The follow-up process continues until Finance is satisfied that the issues have been resolved. It covers entities headed by gubernatorial appointees, including most state agencies, boards, commissions, and Minnesota state colleges and universities. It is not applied to audits of the University of Minnesota and quasi-state organizations, such as the metropolitan agencies, the State Agricultural Society, the state constitutional officers, or the judicial branch.

Admin MINNESOTA Department of Administration

February 17, 2000

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Dear Mr. Nobles:

Thank you for meeting with us to review the results of the statewide financial audit of selected programs of the Department of Administration for the year ended June 30, 1999. We appreciate your efforts to bring areas needing improvements to our attention. We are committed to implementing the recommendations you suggested in your report.

Thank you also for the opportunity to respond to each finding and recommendation contained in the report. Summarized below are our plans to ensure the integrity of financial data and compliance with pertinent laws.

1. Certain divisions did not adequately maintain their accounts receivable balances.

Resolution

Plant Management and Financial Management and Reporting division personnel will reconcile the accounts receivable balances between MAPS and the general ledger on a quarterly basis, effective September 30, 1999. These reconciliations have become significantly complex with the implementation of MAPS, due to the problems with the MAPS Accounts Receivable System. Users have identified problems requiring modifications to the MAPS Accounts Receivable System. However, based on information received from the Department of Finance, the modifications have been identified as a low priority and may not be implemented.

Person Responsible: Kari Suchy, Plant Management Accounting Supervisor
Tom Nash, Financial Management and Reporting Accountant

PrintComm has made revisions to their current accounts receivable policy that will provide more detail on how receivables will be tracked. This policy will ensure that old accounts receivables are pursued and write-offs will occur after all collections efforts are exhausted. This policy will be revised and implemented by February 29, 2000.

Person Responsible: Mary Mikes, Communications.Media Director

2. The Building Construction Division did not ensure that the state's accounting system assigned accurate object codes to new building construction expenditures.

Resolution

Division of State Building Construction staff are monitoring the MAPS default object code while processing construction projects encumbrances. When necessary, staff will revise the default object code to reflect the correct object code that properly classifies the type of expenditure. The monitoring of object codes has been implemented.

Person Responsible: John Retzer, Division of State Building Construction Business Manager

3. The Risk Management Division did not obtain an actuarial evaluation of its contributions to reserves in the past two years.

Resolution

Risk Management will obtain an actuarial evaluation of its contributions to reserves at least biennially. The next actuarial evaluation will be completed for the Fiscal Year 2001 rate package.

Person Responsible: Fred Johnson, Risk Management Division Director

4. PRIOR FINDING PARTIALLY RESOLVED: Some schedule batch jobs run from outside InterTech's secured environment.

Resolution

As of January 21, 2000, 95 percent of the scheduled batch jobs are secured. The remaining 5 percent are infrequently run jobs, and InterTech expects to have them tracked and secured by May 1, 2000.

Person Responsible: Doug Schneider, InterTech Division Director

5. PRIOR FINDING PARTIALLY RESOLVED: InterTech does not have formal procedures to control changes to production batch streams.

Resolution

A formal procedure to control changes to production batch streams has been developed and is targeted for full implementation on June 1, 2000. This will document specific agency liaisons that must approve changes to each production stream.

Person Responsible: Doug Schneider, InterTech Division Director

Very truly yours,

/s/ Kirsten Cecil, Deputy Commissioner for

David F. Fisher
Commissioner