O L A **OFFICE OF THE LEGISLATIVE AUDITOR**
**STATE OF MINNESOTA**

**FINANCIAL AUDIT DIVISION REPORT**

# Department of Agriculture

## Internal Control and Compliance Audit

## July 1, 2004, through June 30, 2007

**December 18, 2008** **Report 08-35**

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**OFFICE OF THE LEGISLATIVE AUDITOR**

**State of Minnesota • James Nobles, Legislative Auditor**

December 18, 2008

Representative Rick Hansen, Chair
Legislative Audit Commission

Members of the Legislative Audit Commission

Mr. Gene Hugoson, Commissioner
Department of Agriculture

This report presents the results of our internal control and compliance audit of the Department of Agriculture for fiscal years 2005, 2006, and 2007 (July 1, 2004, through June 30, 2007).

Our fieldwork ended in August 2008, and we discussed the results of the audit with department's management on December 4, 2008. The audit was conducted by Brad White, CPA, CISA, CFE (Audit Manager), Ken Vandermeer, CPA, CFE (Auditor-in-Charge), and assisted by auditors Sara Becker and Jerry Foty.

We received the full cooperation of the Department of Agriculture's staff while performing this audit.

*/s/ James R. Nobles*

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For the areas audited, the Department of Agriculture's internal controls were generally adequate to ensure it safeguarded receipts, accurately paid vendors and employees, produced reliable financial records, and complied with most legal requirements. However, the department had some weaknesses in its internal controls for travel, overtime, purchasing cards, cell phones, and limited aspects of its personnel and payroll transactions.

For the items tested, the department generally complied with finance-related legal requirements, except for certain travel, purchasing card, and cell phone requirements. The department resolved a prior finding relating to receipts processing.

## Key Findings

- The department did not adequately control travel expenses and had no separately established criteria for promotion and marketing expenses exempted from state travel rules. The department lacked written policies, had inadequate control over state-paid travel costs when combined with personal travel or when amounts are paid by outside organizations, did not sufficiently document some travel expenditures, and had poor control over mileage claims. (Findings 1 to 5)
- The commissioner and other employees did not document and report accrued travel-related benefits earned on state business trips. (Finding 6)
- Employees submitted untimely travel expense reimbursements causing the state to incur additional employer taxes, and the department failed to properly record some of the commissioner's untimely travel reimbursements as taxable income. (Finding 7)
- Purchasing card controls did not include the monitoring of rejected transactions and card limits, and some employees made restricted purchases. (Finding 8)
- The department did not sufficiently document advance approval to control overtime costs and reasons for payroll expense funding adjustments. (Findings 9 and 10)
- The department did not effectively manage and control its cell phones. (Finding 14)

## Audit Objectives and Scope

Internal controls and compliance for fiscal years 2005, 2006, and 2007 over the following selected areas:

- Receipts
- Employees' Use of Cell Phones and Purchasing Cards
- Payroll Expenditures
- Travel Expenditures

## Background

The Department of Agriculture's mission is to administer programs that ensure the integrity of the food supply and strengthen the state's agricultural economy. In fiscal year 2007, the department received General Fund appropriations of totaling $41 million, collected $43.6 million, and spent $75.5 million.

# Department of Agriculture

## Agency Overview

The Department of Agriculture operates under the authority of *Minnesota Statutes* 2007, Chapter 17. The department has 12 divisions and serves as the state's major agricultural regulatory and promotional agency. Mr. Gene Hugoson has served as the department's commissioner since July 1995.

The department collected various dedicated receipts used to finance licensing, inspection, regulatory, and registration activities. Receipts for a variety of fees, licenses, and loan collections totaled approximately $43 million per year for fiscal years 2005 through 2007. In addition, the department also received General Fund appropriations totaling $40 million per year to fund its operations and grants.[1] Table 1 summarizes the department's total receipts and expenditures for fiscal years 2005 through 2007.

**Table 1**
**Receipts and Expenditures**
**July 1, 2004, through June 30, 2007**

| | FY 2005 | FY 2006 | FY 2007 |
|---|---|---|---|
| Receipts: | | | |
| Fees and Other Receipts | $25,636,252 | $26,407,291 | $25,428,921 |
| Loan Repayments and Interest | 13,663,827 | 11,761,460 | 12,464,800 |
| Federal Grants | 4,029,832 | 5,209,901 | 5,758,789 |
| Total Receipts | $43,329,911 | $43,378,652 | $43,652,510 |
| Expenditures: | | | |
| Payroll | $27,030,637 | $27,591,455 | $27,612,139 |
| Professional/Technical Services | 2,564,816 | 2,110,546 | 1,834,018 |
| Space Rental | 2,461,494 | 3,947,814 | 5,311,120 |
| Supplies and Equipment | 2,134,756 | 1,994,224 | 2,317,589 |
| Travel | 1,473,028 | 1,576,132 | 1,625,198 |
| Communications | 544,367 | 576,825 | 520,396 |
| Other Expenditures[1] | 7,004,123 | 8,220,083 | 7,762,924 |
| Grants and Loans | 45,397,884 | 23,736,157 | 29,077,125 |
| Total Expenditures | $88,066,739 | $69,176,412 | $75,540,113 |

[1]Other expenditures included various services and agency and statewide indirect costs.

Source: Minnesota Accounting and Procurement System.

[1] Grant appropriations for ethanol development were approximately $21 million, $18 million, and $15 million for fiscal years 2005, 2006, and 2007, respectively.

# Objectives, Scope, and Methodology

Our audit of selected financial activities of the Department of Agriculture included receipts, expenditures for personnel, payroll, and travel, and employees' use of cell phones and purchasing cards. This was not a comprehensive audit of all financial operations of the department.

The audit focused on the following objectives for the period July 1, 2004, through June 30, 2007:

- Were the department's internal controls adequate to ensure that it safeguarded receipts and other assets, accurately paid employees and vendors in accordance with management's authorization, produced reliable financial information, and complied with finance-related legal requirements?

- For the items tested, did the department comply with significant finance-related legal requirements over its financial activities, including state and federal laws, regulations, contracts, and applicable policies and procedures?

- Did the department resolve prior audit recommendations pertaining to internal controls over license and fee receipts?[2]

To answer these questions, we interviewed agency staff to gain an understanding of the controls related to the department's financial operations. In determining our audit approach, we considered the risk of errors in the accounting records and potential noncompliance with finance-related legal requirements. We also analyzed accounting data to identify unusual transactions or significant changes in financial operations for further review. In addition, we selected a sample of financial transactions and reviewed supporting documentation to test whether the department's controls were effective and if the transactions complied with laws, regulations, policies, and grant and contract provisions.

We conducted the audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives.

[2] Office of the Legislative Auditor's Financial Audit Division Report 04-24, *Department of Agriculture,* issued June 10, 2004.

We used various criteria to evaluate internal control and compliance. We used as our criteria to evaluate agency controls the guidance contained in the *Internal Control-Integrated Framework*, published by the Committee of Sponsoring Organizations of the Treadway Commission.[3] We used state and federal laws, regulations, and contracts, as well as state policies and procedures and the department's internal policies and procedures as evaluation criteria over compliance.

# Conclusions

For the areas audited, the Department of Agriculture's internal controls were generally adequate to ensure it safeguarded receipts, accurately paid vendors and employees, produced reliable financial records, and complied with most legal requirements.

However, the department had some weaknesses in its internal controls for travel, overtime, purchasing cards, cell phones, and limited aspects of its personnel and payroll transactions.

For the items tested, the department generally complied with finance-related legal requirements, except for certain travel, purchasing card activities, and cell phone requirements.

The department resolved a prior finding related to receipt processing.[4]

The following *Findings and Recommendations* further explain the exceptions noted above.

[3] The Treadway Commission and its Committee of Sponsoring Organizations were established in 1985 by the major national associations of accountants. One of their primary tasks was to identify the components of internal control that organizations should have in place to prevent inappropriate financial activity. The resulting Internal Control-Integrated Framework is the accepted accounting and auditing standard for internal control design and assessment.

[4] Prior findings related to the grain and produce division no longer apply since that division was closed, and the responsibility returned to the federal Department of Agriculture in late 2006.

# Findings and Recommendations

Finding 1

**The department did not establish separate criteria to limit and control certain expenses exempted from state travel requirements.**

The department did not establish alternative criteria to govern travel and related costs incurred for marketing and promotional expenditures[5] that statutes exempt from typical state travel policies.[6]

The commissioner's office and the department's Marketing Services Division regularly traveled to domestic and international locations to develop potential agricultural markets for the state. During fiscal years 2005 though 2007, the commissioner's office and the Marketing Services Division used nearly $800,000 for travel and related expenditures.

In the absence of a department policy, we tested a sample of these exempted travel expenditures to determine whether they were reasonable and necessary for the department to achieve its mission. Testing identified the following costs that were not clearly necessary or reasonable:

- The department's travel expenditures included payment of first class or business class airfare, valet parking or more expensive airport parking, bus tours, and group dinners.

- The department hosted a $3,000 banquet, including alcohol, as part of the 2006 World Bio-fuel Symposium in China. The banquet was part of the department's efforts to market the state's alternative fuels. The department did not document how the banquet was a reasonable and necessary expense, the specific and total costs it would incur to host the event, and who would attend.

A policy allowing or limiting these types of expenditures would help the department to ensure that it uses its resources prudently and to comply with state statutes that require the commissioner to endeavor to prevent the waste and unnecessary spending of public money.[7]

[5] *Minnesota Statutes* 2007, 17.101.
[6] *Minnesota Statutes* 2007, 17.1015.
[7] *Minnesota Statutes* 2007, 17.03, subd. 11.

*Recommendation*

- *The department should develop written policies and procedures to ensure that promotional and marketing costs, including travel and hosting costs, are reasonable and necessary.*

## Finding 2

**The department did not adequately control travel costs paid by other organizations.**

On some travel reimbursement requests tested, the commissioner or other employees had partial or no lodging expenses, meals, airfare, or conference registration fees because another organization paid those costs directly. Since the commissioner and some employees had official relationships with other governmental, non-profit, and for-profit organizations, those organizations sometimes paid some or all of the travel costs related to their activities. The department did not establish controls to sufficiently monitor these payments. Although the department did bill and collect nearly $24,000 from certain organizations during fiscal years 2005 through 2007, other organizations did pay some costs directly to vendors or as reimbursements to the employees.

State policy requires that the state pay for costs related to its employees' travel, and that it bill outside organizations for their share of the costs when appropriate.[8] This allows the department to limit the risk of a conflict of interest and prevents the employee from seeking reimbursement from both the state and the other organization.

*Recommendation*

- *The department should reimburse employees for travel costs funded by sponsoring organizations and bill those organizations for the costs.*

## Finding 3

**The department did not ensure that employees claimed appropriate reimbursement for travel costs when combining personal and business travel or when attending conferences that provided meals.**

The department did not have controls to ensure employees paid for their own costs for personal travel incorporated into state-paid business trips. In addition, the department did not compare employee meal reimbursement claims to conference itineraries to ensure that it did not reimburse employees for meals already paid for through conference fees.

[8] Department of Finance Policy PAY0021.

Sample testing of travel expenditures identified several instances where the department reimbursed travel costs to employees without sufficient evidence that the costs did not include personal travel. Without disclosure of the employees' personal plans, the department could inappropriately incur personal travel costs. State policies require employees to disclose and obtain authorization for any personal travel combined with a state trip.[9] The following bullets provide more detail about these instances:

- Employees departed sooner or stayed later on out-of-state business trips for personal travel reasons but did not always distinguish between personal and business travel costs on the out-of-state travel authorization forms. For example, one employee left early for a conference in Boston without indicating on the out-of-state travel authorization form that personal travel was planned. Although the state did not pay for additional lodging and the employee used vacation hours for the personal days, the department reimbursed the employee for some meals that may not have been necessary had the employee traveled the day before the conference.

- Sometimes employees altered a trip itinerary without documenting the additional cost. For example, the commissioner incorporated a personal stop in Hawaii on his way home from China for a state business trip; he paid his estimated personal share of the additional travel costs but did not document the basis for calculation. On another trip mainly paid for by another organization, the department reimbursed the commissioner for a side trip that incurred $1,251 additional airfare, although the business purpose of the side trip was not documented.

- The department did not document why it paid some questionable lodging costs. For example, the department reimbursed an employee for lodging when the hotel receipt indicated more than single occupancy. Other times, the department reimbursed an employee less than the hotel invoice amount without noting the basis for the reduction. The reduction may have been to reimburse at a single occupancy rate or because another organization paid part of the bill. For example, the department reimbursed one employee $100 less per day than the hotel bill without documenting the reason for the reduction.

In addition, the department did not always ensure that employees submitted a conference itinerary to identify whether meals were provided as part of the conference registration fee. State policy requires that employees must attach the conference itinerary to the out-of-state travel request.[10] The department should refer to the itinerary when evaluating eligibility for meals claimed on the employee's expense reimbursement form. Without identifying conference-

[9] Department of Finance Policy PAY0021.
[10] Department of Finance Policy PAY0021.

provided meals, the department could inappropriately reimburse the employee for meals that were already paid for in the conference fee.

*Recommendations*

- *The department should require employees to disclose personal travel arrangements on the out-of-state travel authorization form and clearly identify the nonreimbursable personal portion of travel costs, including any personal airfare, meals, or lodging costs.*

- *The department should obtaining conference itineraries to identify conference-provided meals and compare to meals claimed by employees for reimbursement.*

## Finding 4

**Department controls did not consistently compare actual trip costs to the authorized estimate and did not ensure that employees submitted sufficient evidence to support travel reimbursement requests.**

The department's Finance and Budget Division staff did not always ensure it compared authorized estimated trip costs to all actual costs incurred. It can be challenging to determine a trip's total actual cost, because the department may separately pay for parts of an authorized trip through various processes. For example, the department may make a direct payment to the vendor for airfare, hotel costs, and conference fees, pay for charges on state purchasing cards, or reimburse the employee for meals and mileage. Out-of-state travel forms tested showed the authorized estimated costs, but often did not identify the actual trip costs. Without this comparison, unauthorized costs or duplicate payments could occur without detection.

In addition, the department reimbursed employees even though their travel reimbursement requests lacked documentation required by state policy.[11] Sample testing identified the following exceptions:

- The department reimbursed two employees for airfare costs (one for $781 and another for $1,251) without receipts to support the expenditure and reimbursed another employee for lodging costs supported by a receipt for a different person's lodging.

- The department reimbursed employees for airfare without evidence that the employee arranged a cost effective travel option. The Finance and Budget Division's staff typically controlled airfare purchases by using the state travel agent, but did not prohibit department employees from making

[11] Department of Finance Policy PAY0021.

their own travel arrangements. However, the department did not require those employees to show that they had obtained a good value for the state.

- The department paid some conference registration costs without showing accurate dates of the conference or amounts paid by other organizations on the out-of-state travel authorization form.

- The department reimbursed employees for foreign expenses without requiring evidence of an appropriate currency exchange rate or translation of foreign invoices. Our verification, using foreign currency monthly average conversion rates, found that employees may have been over reimbursed from $21 to $100. Also, without translation of invoices written in a foreign language, the department could not ensure that only allowable costs were paid.

The Finance and Budget Division's staff generally relied on the supervisors' authorizations to support the validity of transactions and did not follow-up on unusual or questionable items to ensure they were accurate and valid.

*Recommendation*

- *The department should improve control over travel claims by:*
  - *comparing authorized estimated trip costs to actual trip costs;*
  - *documenting the most cost-effective travel options, including use of the state's contract travel agent;*
  - *ensuring that employees submit documentation supporting travel claims;*
  - *supporting the conversion rates used for reimbursing international travel; and*
  - *translating foreign invoices to ensure that reimbursed costs are allowable.*

**Finding 5**

**Department controls did not ensure employee mileage reimbursements complied with state travel policies.**

The department did not adequately control employee mileage claims to ensure compliance with state travel policies.[12] It did not validate employee mileage claims and reimbursed employees for use of their personal vehicle at a higher rate without sufficient documentation. The department reimbursed mileage totaling $133,000, $207,000, and $182,000 for fiscal years 2005, 2006, and 2007, respectively.

[12] Department of Finance Policy PAY0021.

The department's travel form did not comply with the state's policy requiring separate reporting of city-to-city trip miles and local mileage. Separating these mileage readings allows a supervisor to better judge the reasonableness of miles claimed. The policy permits the use of Internet mapping tools to measure point-to-point mileage for reimbursement claims. Following are examples of some mileage claims the department reimbursed to employees even though the claims were not sufficiently supported and seemed excessive:

- One employee claimed 3,300 miles driven over a two-month period while traveling to various locations within the metropolitan area without identifying trip destinations or itemizing mileage between each location. Reimbursement for this claim totaled $1,634. The same employee reported higher than actual mileage for a trip outside the metropolitan area. The employee claimed 566 miles for a round trip from the metropolitan area to Staples; actual round trip is 280 miles. The employee did not explain the additional 286 miles. The department reimbursed the employee $139 for those miles without documenting any validation of the mileage claim. Without itemized trip mileage readings, the supervisor responsible for oversight and approval of the mileage reimbursement had no basis to assess reasonableness of the claim.

- A board member of the Rural Finance Authority (accounted for within the Department of Agriculture's accounting structure) submitted 474 miles for a trip that exceeded actual city-to-city mileage by 118 miles. Neither the board member nor the department documented justification for the additional miles, for which the department reimbursed the board member $48. The department reimbursed the board member for similar mileage to attend four other board meetings.

The department also did not document its basis to authorize reimbursement to an employee at a higher rate when the employee chose to use a personal vehicle rather than an available state vehicle. The department's policy required a $.07 per mile lower mileage reimbursement rate if an employee declined the use of a state vehicle for trips outside the metropolitan area. However, the policy allowed the department to reimburse an employee at the higher rate if authorized.[13] The department authorized the higher rate, which should be based on an estimate of the number of miles driven yearly and an explanation of how it is in the best interest of the state for the employee to use a personal vehicle. However, the department did not document the basis for its authorization for the 12 employees it reimbursed at the higher mileage rate.

Without proper review of mileage and clear authorization for reimbursement rates, the department created an opportunity for error and fraud to occur without detection.

[13] The department documented this authorization by issuing a control number to the employees. The employees used this control number to obtain reimbursement at the higher rate.

*Recommendations*

- *The department should improve controls over employee mileage reimbursements by:*
  - *requiring employees to support mileage claims with point-to-point measurements and to separately report trip and local miles on the employee expense reimbursement forms; and*
  - *documenting the basis for authorization to reimburse an employee at a higher mileage rate when the employee chooses not to use an available state car.*

- *The department should review large employee mileage reimbursements during the past few years and determine the validity of miles claimed. If not adequately justified, the department should recover unreasonable reimbursement amounts.*

**Finding 6**

**Department employees did not document and report accrued travel-related benefits earned on state-paid business trips.**

Eight department employees, including the commissioner and marketing staff, earned airline frequent flyer benefits and hotel reward points while traveling on state business without reporting those benefits to the department's Finance and Budget Division. Some employees used frequent flyer benefits on subsequent state trips, which reduced the department's travel costs, but this practice occurred infrequently and was not monitored by the department.

State statutes require that whenever public funds are used for airline travel by a public employee, any credits or other benefits issued by an airline must accrue to the benefit of the public agency providing the funding.[14] Statutes further require that employees report the airline benefit to the department within 90 days of receipt. Statutes also prohibit employees from receiving any compensation, reward, or future benefit from any source except the state for any activities related to the duties of the employee while on state business.[15]

We reviewed the personal frequent flyer account information for eight employees we identified as earning airline benefits. The accounts showed that, as of July 2008, these employees had frequent flyer balances ranging from 4,000 to over 148,000 miles. Without proper reporting and monitoring of the benefits earned,

[14] *Minnesota Statutes* 2007, 15.435.
[15] *Minnesota Statutes* 2007, 43A.38, subd. 2.

department employees could inappropriately convert those benefits for personal use.

*Recommendations*

- *The department should develop procedures to control the use of benefits earned by its employees while traveling on state business.*

- *The department should identify the benefits earned and used by its employees for previous state business trips. It should work with the employees and the airlines to transfer accumulated balances into a separate department business account.*

## Finding 7

**Employees did not file timely expense reimbursement claims and caused the state to incur an additional $5,170 of employer taxes. Also, the department did not record about $2,500 of the commissioner's late expense reimbursements as taxable income.**

Some department employees caused the department to incur additional employer-paid taxes because they filed late expense reimbursements. In addition, the department did not properly record $2,546 of the commissioner's late expense reimbursements as taxable income.

Several department employees, including the commissioner, submitted expense reimbursements more than 60 days after they incurred the expense. Since July 1, 2005, the Internal Revenue Service and the state[16] has required departments to tax these late expense reimbursements as personal income to the employee, which results in additional employer taxes. (The state's payroll system determines the tax status of the reimbursements based on certain dates the department enters.) During fiscal years 2006 through 2008, the department unnecessarily incurred an additional $5,170 of employer-paid taxes because employees submitted their expense reimbursements late. Of this amount, the department incurred an additional $1,316 because of the commissioner's late claims.

In addition, during fiscal years 2006 through 2007, the department did not correctly identify $2,727 of the commissioner's expense reimbursements as being late and mistakenly identified $181 as being late when they were not.

To comply with federal and state regulations, the department should ensure employees understand the tax consequences of untimely expense reimbursements,

[16] Internal Revenue Service Publication 15, Circular E, effective July 1, 2005, and Department of Finance Policy PAY0021.

and that the Finance and Budget Division's staff understand how to code those taxable reimbursements in the state's payroll system.

*Recommendations*

- *The department should identify and monitor employees who submit late reimbursement claims to ensure they understand the tax consequences and to minimize unnecessary employer taxes.*
- *The department should ensure that it accurately inputs expense reimbursement data so that it properly identifies taxable expense reimbursements.*
- *The department should work with the Department of Finance to determine its ability to correct errors in reporting the taxable status of the commissioner's late expense reimbursements.*

## Finding 8

**The department did not effectively monitor purchasing cards, incurred some restricted purchases, and lacked a key cardholder acknowledgement required by state policy.**

The Department of Agriculture did not use key reports to monitor potential fraudulent activity and purchasing card limits, as required by state policy.[17] In addition, the department allowed employees to purchase certain restricted items with their purchasing card and did not include a required clause in the cardholder agreement form.

State policy requires the department to establish guidelines to monitor and control purchasing card activity. The department developed a written policy similar to the state's policy; however, it did not enforce compliance, as discussed below:

- The department did not adequately monitor cardholder activity by using two key reports that show purchasing card activity and the status of card limits. First, the *Declined Transaction Report* allows the department to detect potential patterns of misuse or abuse. That report showed that department employees attempted to use their credit card, but were denied purchases, totaling $51,000 over the last 12 months. A second report provides key information on the status of account or transaction limits. As of July 2008, this report showed that two department employees had excessive purchasing card authorized levels. The department explained that it did not properly

[17] Department of Administration Policy 99.4.

reduce one employee's card limit after a temporary increase from $10,000 to $20,000 for an international trip to China in September 2007. The department could not explain how or why the second employee's authorized purchasing limit had been increased to $10,000. Monthly reviews of these reports would enable the department to question employees about attempts to use cards inappropriately and to monitor card limits.

- Department employees bought restricted items with a purchasing card. State policy prohibits purchasing certain items with a purchasing card, such as meals, telephone calls, and biddable items. Key controls can be circumvented when these purchases are made using purchasing cards. For example, tested sample items showed that employees charged meals on purchasing cards rather than an employee expense form which circumvents controls over meal eligibility and limits. The department also purchased a $2,200 fixed asset using a purchasing card without assigning an equipment inventory number and updating the equipment records. This update would have routinely occurred if the department had made the purchase through its regular process for biddable items.

- Department staff did not always document the business purpose or unusual situations for card purchases. For example, one employee who usually used a purchasing card to buy small quantities of meat and groceries for lab testing did not explain the business purpose for a $69 purchase of over 15 pounds of one type of meat. The department had no evidence to show that the employee appropriately delivered the meat purchased to the lab for testing. Other tested purchase card transactions included car maintenance costs, tools, hardware, blenders, and a picnic shelter rental without sufficient explanations of the business purposes of these costs.

- The department's cardholder agreements with the employees did not include a key clause requiring the employee to acknowledge certain card use restrictions. According to state policy, employees must sign an agreement acknowledging their understanding of the card use restrictions and repercussions for any purchasing violations. Without this key acknowledgement, department management could encounter problems if it needed to take disciplinary action because of an employee's misuse of a purchase card.

*Recommendation*

- *The department should improve controls over monitoring of card limits and restricted purchases, document the business purpose for unusual card purchases, and amend its cardholder acknowledgement form to comply with state policy.*

## Finding 9

**The department made some payroll funding changes between program accounts without a documented reason and authorization.**

The department did not sufficiently document its reason for 11 of 22 tested corrections it made in the state's payroll system to move payroll expenditures between accounts. In addition, 2 of 22 did not have an authorization for the correction. From fiscal years 2005 through 2007, the department moved approximately $4.6 million between accounts in the state's payroll system.

The department initially charged employee salary and benefit costs to program accounts in the payroll system based on the positions' funding, but could change the funding determination when employees worked on other programs or special projects. For example, the department moved one employee's payroll costs originally charged to the Invasive Species Unit to an account set up for a federal potato pest project. Some of the tested payroll expenditure corrections did not have a supervisory authorization to acknowledge the appropriateness of the transfers.

Without documentation for payroll funding changes, the department cannot ensure that it properly accounted for its payroll costs. The department could charge costs to a program that did not get the benefit of the employee's work or could use funds for other than the appropriated or budgeted purpose.

*Recommendation*

- *The department should document the reasons for and authorizations of payroll funding changes.*

## Finding 10

**Department controls did not always ensure that paid employee overtime had advanced management authorization.**

The department did not consistently document overtime requests and approvals for its employees. State policy requires departments to document advanced approval for all nonemergency overtime to ensure the overtime cost is justified and necessary.[18] For fiscal years 2005 through 2007, the department paid employees nearly $860,000 of overtime, including $90,000 of additional related employer taxes and retirement contributions. Table 3 details these costs by fiscal year.

[18] Department of Finance Operating Policy and Procedure PAY0012.

**Table 3**
**Overtime Costs by Fiscal Year**

| | 2005 | 2006 | 2007 |
|---|---|---|---|
| Overtime Pay | $304,616 | $311,712 | $152,489 |
| Related Taxes and Benefits | 35,573 | 36,142 | 17,829 |
| Total | $340,189 | $347,854 | $170,318 |

Source: Minnesota Accounting and Procurement System.

The department paid overtime to both nonexempt and exempt employees, as defined by the federal Fair Labor Standards Act.[19] The department lacked evidence of the need for the overtime and advanced authorization for some paid overtime.

- For hourly, nonexempt employees, sample testing identified 10 out of 24 employees from various divisions that did not have documentation of advanced authorization of the overtime hours paid. When documented, the divisions used either paper leave slips or email to authorize the overtime.

- For exempt employees, the department did not have any justification or authorization to support overtime paid for two of four employees sampled. For example, one exempt supervisor received over $6,300 for 230 hours of overtime in fiscal year 2006 without evidence of management's approval or a documented reason of the need for overtime paid.

Without documentation to justify the special circumstances for overtime and provide management approval in advance, there is an increased risk that the department could incur unnecessary overtime costs.

*Recommendation*

- *The department should document the reason for overtime and obtain advanced approval of overtime for both exempt and nonexempt employees.*

[19] Nonexempt employees are subject to the protections of the federal Fair Labor Standards Act. Generally, nonexempt employees are hourly employees and are paid time and a half for hours that exceed 40 hours in a work week. Exempt employees are not subject to the federal Fair Labor Standards Act. They are generally salaried employees who are expected to work the hours necessary to fulfill their job requirements. Exempt employees are typically not paid overtime, unless warranted by special circumstances.

**The department did not ensure that it established interagency agreement for one employee providing services to the Animal Health Board.**

**Finding 11**

The department did not enter into an interagency agreement for services an employee provided to another state agency. In fiscal years 2006 and 2007, a Department of Agriculture employee provided services to the Animal Health Board. The Animal Health Board paid $2,478 in fiscal year 2006 and $59,278 in fiscal year 2007 for these services. State policy requires an interagency agreement when departments share employees.[20] An agreement would define and limit the services provided, the period of the agreement, and the financial responsibilities of the departments. Without an authorized written agreement, questions and conflicts could arise.

*Recommendation*

- *The department should formalize its interagency agreement with the Animal Health Board.*

**The department's controls did not detect an inaccurate pay rate increase provided to one employee.**

**Finding 12**

The department inappropriately processed a two-step salary increase to a seasonal worker whose bargaining agreement allowed only an annual one-step increase. The error occurred because the department did not have an independent verification of pay rate changes entered into the personnel system. Once we alerted the department to the pay rate error, it initiated a repayment arrangement with the employee to recover $382 of incorrect wages paid.

*Recommendation*

- *The department should implement controls to independently verify pay rate changes entered into the personnel system to ensure compliance with bargaining unit agreements and management authorization.*

**Finding 13**

**The department did not consistently conduct employee annual performance evaluations.**

The department did not always complete annual employee performance evaluations. The department did not have documented performance evaluations

[20] Minnesota departments of Finance and Administration Operating Policy and Procedure 0705-05 and Department of Administration, Professional/Technical (P/T) Contract Manual, Section 21.

for three of five employees tested; all three employees worked in the commissioner's office. State statutes require annual performance reviews to ensure that departments assess the quality of the state's workforce, provide employees with important feedback, and have a basis for pay increases and disciplinary actions.[21] Department policy further requires the performance evaluations to serve as a basis for achievement awards.[22]

*Recommendation*

- *The department's human resources office should reinforce its existing procedures to ensure that all employees receive an annual performance evaluation.*

## Finding 14

**The department did not effectively manage its personal, electronic communication devices to ensure compliance with state and IRS requirements.**

The department did not periodically review its cell phone service plans and match user needs with the most cost efficient service plan, and it did not have an established process to monitor employee personal use. As of June 2008, the department had about 170 personal electronic communication devices (122 cell phones and 46 other devices) and spent about $76,000 for these devices in fiscal year 2007.[23]

The department had the following weaknesses in its controls over cell phones:

➢ **Approval and Plan Review:** The department did not document supervisory approval of the need for some employees to have state-issued cell phones. In addition, except for one division, the department did not review cell phone service plans annually to match user needs with the most cost efficient service plan. Our review identified four cell phones with minimal use compared to the minutes allowed by the cell phone plan, perhaps indicating that the employee did not need a cell phone or that the plan was not cost effective considering the employee's use. For example, one employee used only 89 minutes in a year on a plan that provided 1,000 minutes each month. State policy requires the department to authorize and review a service plan when it issues a cell phone to an employee to ensure that the service provided matches the business needs of the employee.[24] The policy also requires that the

[21] *Minnesota Statutes* 2007, 43A.20 requires annual performance evaluations for employees of the executive branch.
[22] Department of Agriculture Policy #98-005, Achievement Award Guidelines.
[23] The $76,000 includes about $8,000 of expenditures for electronic communication services the department miscoded, as explained in Finding 15.
[24] Statewide Policy: Appropriate Use of Electronic Communication and Technology.

department annually review the service plan to determine if is cost effective and continues to meet the employee's business needs.

- **Monitoring for Personal Use:** During fiscal year 2007, the department followed an old cell phone policy that the state updated in June 2006. The old policy allowed employees to report their personal use of cell phones, but did not require reimbursement to the state unless the personal use caused them to exceed the monthly service plan minutes. The updated policy prohibits personal use and requires repayment of a prorated share of the cost of the plan if personal use should occur. In addition, the department did not always retain documentation of monthly billing statements reviewed by supervisors and did not have evidence from all employees acknowledging compliance with state policies regarding personal use of cell phones.

- **Reimbursement for Personal Cell Phone:** Rather than providing a state-issued phone, the department reimbursed the commissioner for his personal cell phone's monthly service plan. That plan was not purchased under a state contract, which provides a discounted price. The department reimbursed the commissioner about $1,000 annually during fiscal years 2005 through 2007. State policy limits reimbursement for business use of a personal cell phone to only the cost of calls exceeding the standard monthly service fee. However, since calls appeared to be mainly for business use, the department should consider converting his personal cell phone into a state-issued plan.

Without proper approval of the need for a cell phone, review of annual plans, and reporting of personal usage, the department's control over employee use of cell phones is inadequate and does not comply with federal and state requirements. According to current IRS rules, unless employers enforce a policy that employees track personal cell phone use and require employee reimbursement of the personal calls, including a prorated share of the monthly service fee, employers must report the total cell phone expense as income to the employee.

*Recommendations*

- *The department should improve control over the management of personal electronic communication devices by:*
  - *documenting supervisory approval for the initial request for a device and performing annual reviews of service plans;*
  - *providing a state-issued cell phone to the commissioner or limiting reimbursement to the cost of business calls that exceed the personal plan's standard monthly fee; and*
  - *monitoring monthly supervisory review of employee personal phone usage and recovery for any personal calls made.*

- *The department should amend its cell phone policy to align with the federal and state cell phone guidelines regarding the reporting of personal calls.*

## Finding 15

**The department did not always use proper expenditure codes and liability dates for communication and travel payments in the state's accounting system.**

The department did not properly identify certain expenditure types and obligation dates for transactions in the state's accounting system. Department staff miscoded approximately $8,000 of electronic communication services during fiscal year 2007 as equipment in the accounting system. In addition, the department routinely used the transaction date as the date of liability for cell phone service and incorrectly identified the liability dates for 15 of 19 directly-paid travel costs. State policy[25] requires agencies to properly identify the liability date as the date when it receives goods or services so that the transaction is correctly recorded in the proper accounting period.

*Recommendation*

- *The department should properly code transactions with the correct expenditure types and liability dates in the accounting system.*

[25] Department of Finance Policy 0901-01.

MINNESOTA DEPARTMENT OF
AGRICULTURE
FROM THE FARM TO YOUR FAMILY

December 15, 2008

Mr. James R. Nobles
Legislative Auditor
Office of the Legislative Auditor
Room 140 Centennial Office Building
658 Cedar Street
Saint Paul, Minnesota 55155-1603

Dear Mr. Nobles:

Thank you for the opportunity to review and respond to your office's internal control and compliance audit of the Department of Agriculture. We value the professional review your staff has provided us with this audit and appreciate the recommendations for improvement that have resulted.

The most common finding across the recommendations in this report is that we need to make a greater effort to clearly document and justify expenditures. We agree with this message. We intend to do a better job documenting our efforts.

Specific responses to this audit follow.

**Finding 1: The department did not establish separate criteria to limit and control certain expenses exempted from state travel requirements.**

Audit Recommendation:
*The department should develop written policies and procedures to ensure that promotional and marketing costs, including travel and hosting costs, are reasonable and necessary.*

Department Response:
The department agrees with this recommendation. Minnesota Statute sets promotion of agricultural industries as one of the key duties of the department. Statute also provides exemption from regular state travel policy in order to pursue this duty. Because of this exemption, the department will formalize in written policy how our authority will be prudently exercised.

**Finding 2: The department did not adequately control travel costs paid by other organizations.**

Audit Recommendation:
*The department should reimburse employees for travel costs funded by sponsoring organizations and bill those organizations for the costs.*

Department Response:
The department agrees with this recommendation. The department's travel policy will clearly state that all costs associated with state employee travel will be reported on state forms and that no reimbursements from outside organizations may go directly to employees. Accounting staff will provide better monitoring and guidance of the travel policy.

**Finding 3: The department did not ensure that employees claimed appropriate reimbursement for travel costs when combining personal and business travel or when attending conferences that provided meals.**

Audit Recommendation:
*The department should require employees to disclose personal travel arrangements on the out-of-state travel authorization form and clearly identify the non-reimbursable personal portion of travel costs, including any personal airfare, meals or lodging costs.*

*The department should obtain conference itineraries to identify conference-provided meals, and compare to meals claimed by employees for reimbursement.*

Department Response:
The department agrees with this recommendation. All travel timing and routing needs to be appropriately documented. While the Hawaii stop en route home from China was the only available routing, the alternative timing to allow for a few hours of sleep between flights (all at personal expense) should have been better documented. The side business trip within China to discuss a trade agreement was planned ahead of time, but not well documented. In all cases, department forms should clearly identify the purposes for timing and routing and if any allowable personal travel provisions are included, the costs associated with those provisions should be disclosed and paid for by the employee. The department's travel policy will clearly state this and accounting staff will provide better monitoring and guidance.

**Finding 4: Department controls did not consistently compare actual trip costs to the authorized estimate and did not ensure that employees submitted sufficient evidence to support travel reimbursement requests.**

Audit Recommendation:
*The department should improve control over travel claims by:*
*-comparing authorized estimated trip costs to actual trip costs;*
*-documenting the most cost-effective travel options including use of the state's contract travel agent;*
*-ensuring that employees submit documentation supporting travel claims;*
*-supporting the conversion rates used for reimbursing international travel; and*
*-translating foreign invoices to ensure that reimbursed costs are allowable.*

Department Response:
The department agrees with this recommendation. The department's travel policy will require more documentation of reference costs for travel arrangements not made through the state's contract travel agent and for foreign language receipts and foreign conversion rates. Justification for missing receipts has now been received and actual costs are now being consistently documented on travel forms. Accounting staff will provide better monitoring and guidance.

**Finding 5: Department controls did not ensure employee mileage reimbursements complied with state travel policies.**

Audit Recommendation:
*The department should improve controls over employee mileage reimbursements by:*
*-requiring employees to support mileage claims with point-to-point measurements and to separately report trip and local miles on the employee expense reimbursement forms; and*
*-documenting the basis for authorization to reimburse an employee at a higher mileage rate when the employee chooses not to use an available state car.*

*The department should review large employee mileage reimbursements during the past few years and determine the validity of miles claimed. If not adequately justified, the department should recover unreasonable reimbursement amounts.*

Department Response:
The department agrees with this recommendation. Local mileage needs to be reported separately on reimbursement forms and justified when the purpose is not clear. For example, the RFA Board member's extra local miles were verbally approved and provided good value to the state because the member stayed overnight with a relative rather than incurring lodging costs to the state. Oftentimes, field staff drive to several locations in the country that need to be documented better than just showing the starting point, ending point and odometer readings. The department's travel policy will clearly state this and accounting staff will provide better monitoring and guidance. The department's reimbursement form will be modified to ensure that local miles are documented sufficiently.

**Finding 6: Department employees did not document and report accrued travel-related benefits earned on state-paid business trips.**

Audit Recommendation:
*The department should develop procedures to control the use of benefits earned by its employees while traveling on state business.*

*The department should identify the benefits earned and used by its employees for previous state business trips. It should work with the employees and the airlines to transfer accumulated balances into a separate department business account.*

Department Response:
The department agrees with this recommendation. It is against the law for a state employee to personally benefit from travel-related programs such as frequent flyer programs. The review of travel during this period shows no evidence that this occurred, but does show that better records need to be kept. While no state dollars are at risk, the department believes there is potential value to the state above the costs of tracking these benefits if an employee travels enough to use the benefits of these programs on future state travel. A review has confirmed that there was no personal use of frequent flyer miles earned on state travel. A program for tracking these benefits has been initiated in the department to ensure that this continues to be the case. Reporting requirements and procedures for using these programs will be communicated to department employees. Accounting staff will at least annually review the travel and benefit logs to monitor compliance and assist staff in the appropriate use of these programs.

**Finding 7: Employees did not file timely expense reimbursement claims and caused the state to incur an additional $5,170 of employer taxes. Also, the department did not record about $2,500 of the commissioner's late expense reimbursements as taxable income.**

Audit Recommendation:
*The department should identify and monitor employees who submit late reimbursement claims to ensure they understand the tax consequences and to minimize unnecessary employer taxes.*

*The department should ensure that it accurately inputs expense reimbursement data so that it properly identifies taxable expense reimbursements.*

*The department should work with the Department of Finance to determine its ability to correct errors in reporting the taxable status of commissioner's late expense reimbursements.*

Department Response:
The department agrees with this recommendation. Both IRS Publication 15 and statewide policy state that the general guideline for submitting reimbursement justifications is 60 days. The state's payroll system has incorporated this time frame as the date at which all reimbursed money will be taxed. Some employees, as well as the commissioner, were not aware of the strict interpretation of the guideline and how it would cost them (and the state) additional taxes. In some cases, the intent was to be more efficient by waiting and submitting several smaller expenses together. The commissioner has paid back the amount his reimbursement submissions cost the state in additional taxes. The department has stepped up its efforts to educate staff on the implications of this policy and has added a notification on the expense reimbursement form. Accounting staff will provide better monitoring and guidance.

**Finding 8: The department did not effectively monitor purchasing cards, incurred some restricted purchases, and lacked a key cardholder acknowledgement required by state policy.**

Audit Recommendation:
*The department should improve controls over monitoring of card limits and restricted purchases, document the business purpose for unusual card purchases, and amend its cardholder acknowledgement form to comply with state policy.*

Department Response:
The department agrees with this recommendation. While statewide policy encourages the use of purchasing cards for certain expenses, the electronic credit approval system is not able to disallow all restricted expenses. The most common way restricted purchases get allowed is if meals are included on a lodging bill. The employee is supposed to ask for those charges to be paid separately and submitted for reimbursement on an expense report. The department has identified these violations and required the employees to repay the state for the disallowed expenses and submit them as appropriate on regular expense forms. Accounting staff will provide better monitoring and guidance. In addition, the purchasing card supervisor will increase monitoring of the program through the regular use of the reports mentioned. The clause that was missing from the department's form has been added.

**Finding 9: The department made some payroll funding changes between program accounts without a documented reason and authorization.**

Audit Recommendation:
*The department should document the reasons for and authorizations of payroll funding changes.*

Department Response:
The department agrees with this recommendation. All payroll change forms will state the reasons for the change and have supervisory authorization. Accounting staff will provide explanations on these forms and the Accounting Director will approve all forms.

**Finding 10: Department controls did not always ensure that paid employee overtime had advance management authorization.**

Audit Recommendation:
*The department should document the reason for overtime and obtain advance approval of overtime for both exempt and non-exempt employees.*

Department Response:
The department agrees with this recommendation. The department's human resources director will continue to approve all special project overtime for exempt employees. In order to ensure that the reasons for overtime are documented and prior approval is received, the human resources staff will remind managers and supervisors annually of

their responsibility to document approved overtime. Human resources will also take a sample from each division of overtime documentation in order to ensure that managers and supervisors are following through on their responsibility to document and to receive prior approval of overtime for both exempt and nonexempt employees.

**Finding 11: The department did not ensure that it established an interagency agreement for one employee providing services to the Animal Health Board.**

Audit Recommendation:
*The department should formalize its interagency agreement with the Animal Health Board.*

Response:
The department agrees with this recommendation. When the department enters into interagency agreements, human resources will follow-up with the requesting agency in order to ensure an agreement is completed and a copy is on file for audit purposes.

**Finding 12: The department's controls did not detect an inaccurate pay rate increase provided to one employee.**

Audit Recommendation:
*The department should implement controls to independently verify pay rate changes entered into the personnel system to ensure compliance with bargaining unit agreements and management authorization.*

Response:
The department agrees with this recommendation. The department had depended on the Department of Employee Relations (now the Department of Minnesota Management and Budget, MMB) to review transactions in order to detect errors. Since MMB will not be conducting reviews in the future, Agriculture human resources staff will review transactions monthly in order to detect errors.

**Finding 13: The department did not consistently conduct employee annual performance evaluations.**

Audit Recommendation:
*The department's human resource office should reinforce its existing procedures to ensure that all employees receive an annual performance evaluation.*

Department Response:
The department agrees with this recommendation. The department will reinforce its present performance appraisal notification system. Human resources will track late performance reviews and notify managers and supervisors that they are late. In cases where the performance reviews are more than three months late, human resources will contact the appropriate division director in order to gain compliance.

**Finding 14: The department did not effectively manage its personal electronic communication devices to ensure compliance with state and IRS requirements.**

Audit Recommendation:
*The department should improve control over the management of personal electronic communication devices by:*
*-documenting supervisory approval for the initial request for a device and performing annual reviews of service plans;*
*-providing a state-issued cell phone to the commissioner or limiting reimbursement to the cost of business calls that exceed the personal plan's standard monthly fee; and*
*-monitoring monthly supervisory review of employee personal phone usage and recovery for any personal calls made.*

*The department should amend its cell phone policy to align with the federal and state cell phone guidelines regarding the reporting of personal calls.*

Department Response:
The department agrees with this recommendation. Supervisory approval forms are now being filed centrally in the finance and budget division. Department forms have been changed to provide the appropriate documentation and bills are being monitored on a monthly basis. The department's policy will be changed to provide for annual reviews of device use. The department will work to find an appropriate solution to the commissioner's unique phone needs.

**Finding 15: The department did not always use proper expenditure codes and liability dates for communication and travel payments in the state's accounting system.**

Audit Recommendation:
*The department should properly code transactions with the correct expenditure types and liability dates in the accounting system.*

Department Response:
The department agrees with this recommendation. Training has been implemented for both buyers and accounts payable staff to ensure that proper coding and dates are entered into the state's accounting system.

Sincerely,

Gene Hugoson
Commissioner