OLA

OFFICE OF THE LEGISLATIVE AUDITOR
STATE OF MINNESOTA

Management Letter

Department of Children, Families & Learning
Fiscal Year Ended June 30, 1999

MARCH 10, 2000 **00-05**

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

Summary

Management Letter

Department of Children, Families & Learning
Fiscal Year Ended June 30, 1999

Key Findings and Recommendations:

- The Department of Children, Families & Learning (CFL) did not properly record the date of liability for construction grant expenditures on the state's accounting system. We made an audit adjustment of $1.4 million on the state's financial statements to record the correct liability. CFL should ensure that the record date on the accounting system is the date the subrecipient incurs the liability for construction costs. (Finding 1, page 2)

- CFL did not disburse grant funds to subrecipients based on current needs for the Low Income Home Energy Assistance Program (CFDA # 93.568). The Cash Management Improvement Act requires recipients to minimize the time elapsing between drawing federal funds and the actual disbursement of these monies. (Finding 2, page 3)

- CFL did not draw federal funds in accordance with the approved method outlined in the Department of Finance's agreement with the U. S. Treasury. The agreement specifies that the state shall schedule receipt of federal funds in accordance with the approved clearance pattern. (Finding 3, page 4)

- Finally, CFL did not comply with certain federal and state indirect cost requirements. CFL should ensure that it uses the correct expenditure totals when calculating indirect cost charges to federal programs. CFL should also make statewide indirect cost payments quarterly. (Finding 4, page 4)

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 Children, Families & Learning focused on selected state educational aids and seven federal programs. The department's response to our recommendations is included in the report.

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Department of Children, Families & Learning

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Audit Participation

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

Claudia Gudvangen, CPA	Deputy Legislative Auditor
Renee Redmer, LPA	Audit Manager
Joan Haskin, CPA, CISA	Audit Director
Susan Kachelmeyer, CPA	Senior Auditor
Anna Lamin	Senior Auditor
Valerie Wozniak	Intern

Exit Conference

The findings and recommendations in this report were discussed with the following staff of the Department of Children, Families & Learning at an exit conference held on February 25, 2000:

Christine Jax	Commissioner
Cindy Lavorato	Assistant Commissioner
Mark Kaszynski	Energy Programs Director
Tom Melcher	Program Finance Manager
Katie Shea	Agency Finance Manager
Bonnie Carlson	Monitoring and Compliance Supervisor
Staci Hanson	Energy Programs
Sue Nicol	Accounting Officer Senior

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OFFICE OF THE LEGISLATIVE AUDITOR

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

Representative Dan McElroy, Chair
Legislative Audit Commission

Members of the Legislative Audit Commission

Dr. Christine Jax, Commissioner
Department of Children, Families & Learning

We have performed certain audit procedures at the Department of Children, Families & Learning (CFL) 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 also have audited certain federal financial assistance programs administered by the department as part of our audit of the state's compliance with the requirements described in the U.S. Office of Management and Budget (OMB) *Circular A-133 Compliance Supplement*. We emphasize that this has not been a comprehensive audit of the Department of Children, Families & Learning.

Table 1 identifies the financial activities within CFL that were material to the state's financial statements. We performed certain audit procedures on these programs 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
Programs Material to the State's Financial Statements
Fiscal Year 1999
(in thousands)

Expenditures	Amount
General Fund - School Aids **(1)**	$3,847,150
Expendable Trust Fund – Endowment School Fund Apportionment	19,513
Capital Projects Fund – Construction Grants	14,352
Federal Fund:	
Title I Grants to Local Educational Agencies	96,938
Child and Adult Care Food Program	51,327
Special Education Grants to States	52,296
Child Care and Development Program	48,231
Low Income Home Energy Assistance Program	38,920
National School Lunch Program	68,093
Loans Receivable	
Maximum Effort School Loan Fund	14,221

(1) State education aids paid through the department's centralized payment system.

Source: Minnesota Accounting and Procurement System (MAPS) for fiscal year 1999.

Table 2 identifies the State of Minnesota's major federal programs administered by CFL. We performed certain audit procedures on these programs as part of our objective to obtain reasonable assurance about whether the State of Minnesota complied with the

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types of compliance requirements that are applicable to each of its major federal programs.

Table 2
Major Federal Programs
Fiscal Year 1999
(in thousands)

CDFA No.	Program Name	Total Expenditures
10.550	Food Distribution **(1)**	$14,432
10.558	Child and Adult Care Food	51,327
84.027	Special Education State Grants	71,719
84.048	Vocational Education-Basic State Grants	6,802
84.173	Special Education – Preschool Grants	9,501
93.568	Low Income Home Energy Assistance Program	38,920
93.596	Child Care and Development Program	54,395

(1) Value of food commodities distributed during fiscal year 1999.

Source: Minnesota Accounting and Procurement System (MAPS) for fiscal year 1999.

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 have 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 weaknesses in internal control and noncompliance with program requirements at CFL.

1. CFL did not properly record the date of liability for construction grant expenditures on the state's accounting system.

CFL did not properly record the date the state incurred a liability for construction grants in the Minnesota Accounting and Procurement System (MAPS). CFL reimburses eligible subrecipients for construction costs incurred and reported to the department. Fiscal year 1999 construction grant expenditures reported in the Building Fund, as adjusted by the

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auditor, totaled $14.4 million. Reimbursement forms submitted to fiscal services staff for payment did not include the date the liability was incurred by the subrecipient. The date that facilities management staff approved the reimbursement form was the record date entered into MAPS. The department should record the date that the subrecipient incurs the expenditure to properly show the date the state incurs a liability. Because the correct date of liability recognition was not recorded on the accounting system, expenditures reported on the state's draft financial statements were understated by $1.4 million.

Recommendation

- *CFL should ensure that the record date on MAPS is the date the subrecipient incurs the liability for construction costs.*

2. PRIOR FINDING NOT RESOLVED: CFL did not comply with the Cash Management Improvement Act for the Low Income Home Energy Assistance Program (LIHEAP).

CFL did not disburse grant funds to subrecipients based on current needs for the Low Income Home Energy Assistance Program (CFDA 93.568). CFL allows its subrecipients to hold up to 30 days' cash on hand irrespective of its disbursement cycle. Subrecipients request cash once a month and receive federal funds in the form of 30-day cash advances. This advance payment method caused some subrecipients to return excess funds to CFL. As of November 29, 1999, the amount refunded by subgrantees for fiscal year 1999 grants totaled $271,494. The Cash Management Improvement Act states that when advance payment procedures are used, recipients must minimize the time elapsing between the drawdown of cash from the federal government and actual disbursement of the funds. CFL should monitor cash drawdowns by their subrecipients to ensure compliance with the act. CFL should also consider reimbursing subrecipients for actual expenditures rather than advancing funds. Certain other federal programs that CFL administers operate on a reimbursement basis.

In addition, we found that subrecipients did not return interest earned on the advances to the federal government. The Cash Management Improvement Act states that interest earned on advances by local governments and subrecipients is required to be submitted promptly, on at least a quarterly basis, to the federal funding agency. The act also states that up to $100 may be kept for administrative expenses. Interest earned by nonstate, nonprofit entities on federal fund balances in excess of $250 should be returned to the federal agency.

Finally, we found improper separation of duties over the refund process. Program staff with access to the database records for program activity, including grants, expenditures, and refunds, also were in control of the refund checks. This increases the risk of loss or theft by not properly separating these duties. Someone who does not have access to the database should control the refund checks.

Recommendations

- *CFL should monitor the payment of cash to its subrecipients to ensure compliance with the Cash Management Improvement Act.*
- *CFL should ensure that interest earned by subgrantees on advances is returned to the federal agency.*
- *CFL should ensure that proper controls are in place for refunds.*

3. CFL did not comply with the provisions of the cash management agreement with the Department of Finance.

CFL did not draw federal funds for some programs in accordance with the approved method outlined in the Department of Finance's agreement with the U. S. Treasury. The agreement specifies that the state shall schedule receipt of federal funds in accordance with the approved clearance pattern.

CFL routinely requested federal funds for most of its major federal programs every two weeks. CFL requested some of its federal funds after negative cash balances were reported on the state's accounting system. For example, CFL processed payments totaling $3 million for the Special Education Programs on April 15, 1999. CFL did not draw federal funds until April 28, 1999. As a result, state funds were used to pay for some program expenditures, causing the state to lose investment income. CFL should draw funds in accordance with the state's agreement for its major federal programs.

Recommendation

- *CFL should request federal funds in accordance with the state's agreement with the U. S. Treasury.*

4. CFL did not comply with certain federal and state indirect cost requirements.

CFL overcharged some federal programs for indirect costs. The department did not use the correct expenditure amounts when calculating indirect cost charges for some federal programs. After charging the federal programs for indirect costs, CFL discovered 12 instances where incorrect expenditure amounts were used. This resulted in a total overcharge of $16,046.

CFL did not properly reimburse the General Fund on a timely basis as required by the Department of Finance's operating policy and procedure 304-02. The Finance policy requires reimbursement of statewide and agency indirect costs on a quarterly basis where the annual liability exceeds $2,000. CFL made two payments to Finance for its fiscal year 1999 statewide indirect costs. CFL paid $205,356 for the first three quarters of fiscal year 1999 on April 20, 1999, and paid $145,602 on September 8, 1999.

Children, Families & Learning

Recommendations

- *CFL should ensure that it uses the correct expenditure totals when calculating indirect cost charges to federal programs. In addition, CFL should adjust the charges to affected federal programs.*
- *CFL should make statewide indirect cost payments quarterly as outlined in the DOF policy.*

This report is intended for the information of the Legislative Audit Commission and the management of the Department of Children, Families & Learning. This restriction is not intended to limit the distribution of this report, which was released as a public document on March 10, 2000.

/s/ James R. Nobles	*/s/ Claudia J. Gudvangen*
James R. Nobles Legislative Auditor	Claudia J. Gudvangen, CPA Deputy Legislative Auditor

End of Fieldwork: January 7, 2000

Report Signed On: March 7, 2000

Status of Prior Audit Issues
As of January 7, 2000

March 5, 1999, Legislative Audit report 99-13 examined the CFL activities and programs material to the State of Minnesota's Annual Financial Report or the Single Audit for the year ended June 30, 1998. The scope included General Education Aids, Title I Grants to Local Educational Agencies, Special Education Aid, and other federal and state programs. The audit found that the department did not certify some liabilities to the Department of Finance. In addition, the prior audit found that the department did not accurately and timely prepare supplemental federal expenditure schedules. The prior audit also identified concerns relating to the refund process, Cash Management Improvement Act, recording of grant amounts, and monitoring of subrecipients for the Low Income Home Energy Assistance Program. In addition, we found that the department did not accurately prepare a report for the Child Care and Development Program and did not review the manual entries for the program. Finally, the prior audit found the department did not monitor adult education administrative expenditures. Except for the issue regarding noncompliance with the Cash Management Improvement Act for the LIHEAP program, our 1999 audit found that the department implemented the recommendations discussed in the prior audit.

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, any quasi-state organizations, such as metropolitan agencies or the State Agricultural Society, the state constitutional officers, or the judicial branch.

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March 3, 2000

James Nobles
Legislative Auditor
658 Cedar Street
Saint Paul, MN 55155

Dear Mr. Nobles:

I have received the draft audit report for the Department of Children, Families and Learning Fiscal Year Ended June 30, 1999. The Department has implemented changes to address all four of the findings in the report.

The Management Assistance Section has changed its form and procedures for construction grants to correctly record the date of liability for construction grant expenditures. The new process has been in place since January, 2000. The contact person for this area is Norm Chaffee.

The Energy Assistance Program has worked with Agency Finance to change the payment cycle for subrecipients to ensure that they receive funds based on their current needs. Payments are processed daily rather than twice a month and cash drawdowns are monitored. This should eliminate the need for recipients to refund overpaid advances. Also, the Program has instituted new procedures to ensure that staff processing refunds do not have access to database records for program activity. Mark Kaszynski is the manager of the program and responsible for these procedural changes. The changes are already in place.

Cash management procedures have also been changed to comply with the Department of Finance's agreement with the U.S. Treasury. Katie Shea is the responsible manager for this area.

Finally, the department is currently making its indirect cost payments on a quarterly basis, as required by the Department of Finance. In addition, calculation methods have been corrected so that federal programs are not overcharged for indirect costs. We are seeking to recover previous repayments from the Department of Finance with the third quarter fiscal year 2000 payment. Katie Shea is the manager overseeing this area as well.

Thank you for your work and recommendations.

Sincerely,

/s/ Christine Jax

Christine Jax, PhD.
Commissioner