OFFICE OF THE LEGISLATIVE AUDITOR
STATE OF MINNESOTA

Management Letter

Department of Employee Relations

Fiscal Year Ended June 30, 1999

MARCH 16, 2000 **00-09**

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.

This document can be made available in alternative formats, such as large print, Braille, or audio tape, by calling 651-296-1727 (voice), or the Minnesota Relay Service at 651-297-5353 or 1-800-627-3529.

All OLA reports are available at our Web Site: http://www.auditor.leg.state.mn.us

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 Employee Relations
Fiscal Year Ended June 30, 1999

Key Findings and Recommendations:

- The department did not transfer any portion of the available June 30, 1999, Minnesota Private Employers' Insurance Fund (MEIP) cash balance to the Health Care Access Fund, as directed by state statutes. We recommended that the department should transfer the uncommitted portion of the MEIP's available balance to the Health Care Access Fund and work to resolve any outstanding obligations. (Finding 1, page 3)

- The department did not adequately administer the vacation donation to sick leave program. We noted several concerns including a lack of program procedures, employees that received more hours than were donated, and an overall program deficit of over $1 million which was paid from state agency operating budgets. We recommended that the department implement and enforce a vacation donation policy that complies with Minn. Stat. Section 43A.1815. We also believe the department should consider a funding policy requiring the donor agency to provide financial resources to the agency employing the eligible program recipient. The funding mechanism would lessen the financial burden caused by the additional sick leave costs and replacement staff wages. (Finding 2, page 3)

- A provision in the Minnesota Law Enforcement Association's employment agreement contradicts Minn. Stat. Section 43A.04, Subd. 8. The provision governs the amount of vacation leave an employee can donate to their union representative to carry out union duties. We recommended that the department seek clarification from the Office of the Attorney General on the validity of this bargaining agreement provision. (Finding 3, 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 Employee Relations focused on payroll expenditures, public and private insurance programs, and liabilities for employee leave benefits and workers' compensation. The department's response to our recommendations is included in the report.

Room 140, 658 Cedar Street, St. Paul, Minnesota 55155-1603 • Tel: 651/296-4708 • Fax: 651/296-4712
E-mail: auditor@state.mn.us • TDD Relay: 651/297-5353 • Website: www.auditor.leg.state.mn.us

Table of Contents

Audit Participation

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

Claudia Gudvangen, CPA	Deputy Legislative Auditor
Brad White, CPA, CISA	Audit Manager
Mark Mathison, CPA, CISA	Auditor-in-Charge
Mike Byzewski	Auditor
April Snyder	Auditor
Loren Louwagie	Audit Intern

Exit Conference

The findings and recommendations in this report were discussed with the following officials of the Department of Employee Relations at an exit conference held on March 1, 2000:

Wayne Simoneau	Acting Commissioner
Edward Anderson	Accounting Director
Laurie Hansen	SEMA4 Human Resources Manager
Carolyn Hoel	Accountant
Elizabeth Houlding	Employee Insurance Division Manager
Steve Jorgenson	Chief Informations Officer
Paul Larson	Assistant State Negotiator

Representative Dan McElroy, Chair
Legislative Audit Commission

Members of the Legislative Audit Commission

Mr. Wayne Simoneau, Acting Commissioner
Department of Employee Relations

We have performed certain audit procedures at the Department of Employee Relations 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 reviewed certain departmental procedures related to the state's compliance with 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 Employee Relations.

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.

Table 1 identifies the financial activities within the Department of Employee Relations 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 are free of material misstatement.

In addition to reviewing the financial activities within the Department of Employee Relations that were material to the state's financial statements, we also reviewed the department's administration of the vacation donation program.

Room 140, 658 Cedar Street, St. Paul, Minnesota 55155-1603 • Tel: 651/296-4708 • Fax: 651/296-4712

E-mail: auditor@state.mn.us • TDD Relay: 651/297-5353 • Website: www.auditor.leg.state.mn.us

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

	Amount
Statewide Payroll Expenditures	$2,439,031,000
Revenue Areas	
Employees Insurance *(internal service fund)*	
Operating revenue	$290,186,000
Investment income	5,155,000
Public Employees Insurance *(enterprise fund)*	
Operating revenue	7,830,000
Investment income	267,000
Minnesota Private Employers Insurance *(enterprise fund)* (1)	
Operating revenue	53,000
Investment income	49,000
Expense Areas	
Employees Insurance *(internal service fund)*	$299,113,000
Public Employees Insurance *(enterprise fund)*	8,040,000
Minnesota Private Employers Insurance *(enterprise fund)* (1)	238,000
Other Areas	
Compensated Absences Liability *(general long-term obligation account group)*	$265,063,000
Compensated Absences Liability *(proprietary and other funds)*	15,312,000
Workers' Compensation Liability *(general long-term obligation account group)*	116,135,000

(1) The Minnesota Private Employers Insurance Fund ceased operations during fiscal year 1999.

Source: State of Minnesota Comprehensive Annual Financial Report and the Minnesota Accounting and Procurement System (MAPS) for fiscal year 1999.

Conclusions

We have issued an unqualified opinion, dated December 1, 1999, on the general purpose financial statements reported in the State of Minnesota's Comprehensive Annual Financial Report. 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 procedures, we identified the following reportable conditions at the Department of Employee Relations:

Department of Employee Relations

1. The Department of Employee Relations did not transfer any portion of the available MEIP cash balance to the Health Care Access Fund, as directed by Minnesota statutes.

The Department of Employee Relations did not transfer funding from the Minnesota Private Employers Insurance Program (MEIP) to the Health Care Access Fund, as required by Minn. Stat. Section 43A.317, Subd.,8 (b). In 1993, the Health Care Access Fund provided MEIP with a start-up loan of $2,075,000. Due to a lack of participants, the MEIP fund ceased operation in October 1998.

In our 1998 audit report to the department (Report 98-17), we concluded that the MEIP financial activity did not appear to be sufficient to re-pay the entire loan amount by the required date of July 1, 1998. As a result, the Legislature modified Minn. Stat. Section 43A.317 Subd. 8(b) during the 1998 Legislative Session forgiving a portion of the loan.

The revised statutory language required the department to return any remaining balance in the MEIP fund, up to $2,075,000, to the Health Care Access Fund on June 30, 1999, after paying all necessary and reasonable expenses. As of December 1999, the department had not transferred any of the $846,000 MEIP fund balance to the Health Care Access Fund. The department did not transfer the balance because it anticipated approximately $100,000 of additional expenditures related to a lengthy legal dispute involving the MEIP fund. We think the department could have transferred the majority of the MEIP fund's cash balance to the Health Care Access Fund.

Recommendation

- *The Department of Employee Relations should transfer the uncommitted portion of the Minnesota Private Employers Insurance Program's available balance to the Health Care Access Fund and work to resolve any outstanding obligations.*

2. The Department of Employee Relations did not adequately administer the vacation donation to sick leave program.

The department did not administer the state employee vacation donation program in accordance with Minn. Stat. Section 43A.1815. The donation program provides additional sick leave hours to state employees who have exhausted all other paid leave and have a serious medical hardship or catastrophic illness or injury. Beginning in July 1996, the statute allowed state employees to annually donate up to 12 hours of accrued vacation leave to the sick leave account of one or more state employees. The statute required that the Department of Employee Relations establish procedures for eligibility, duration of need, monitoring and evaluating eligibility status, and other topics related to the administration of the program.

Department of Employee Relations

We identified several concerns with the department's administration of this program:

- The department did not finalize procedures on how the program should be administered, as required by statute. Administrative Procedure #18 remained in draft status until September 1999 when new interim procedures were developed.

- Employees were permitted by statute to donate up to 12 hours per year. We noted that approximately 25,000 hours were given by employees donating in excess of 12 hours annually.

- The department allowed employees to use more sick leave hours than were donated, resulting in a significant deficit. We believe the legislative intent of the program is to allow sick leave up to the extent of donated vacation leave individually, as well as in total. Since its inception through September 1999, the program received 131,500 donated vacation hours, however, the program paid recipients for more than 159,700 hours of leave. We estimate that the deficit, as a whole, cost the state over $1 million for additional sick leave and benefits funded from state agencies' operating budgets.

  The department pooled donated hours rather than applying the hours to the intended recipient's sick leave account, as required under the statute. Approximately 70 of the 160 benefit recipients were paid for hours that were not donated to them individually. Some individual recipients were paid for over 2,000 hours more than what was donated.

- Finally, the department currently does not require a transfer of funds between agencies. The donating agency does not use any financial resources to fund the donation; they simply reduce the donor's vacation leave balance. The primary financial burden rests with the agency paying the additional sick leave benefits provided to an eligible program recipient. Besides the sick leave costs, the agency also incurs payroll costs for replacement staff to perform the necessary job duties. It seems logical to expect an agency to provide financial resources to fund the donation since its compensated absence liability is reduced.

The department had identified some of these concerns, releasing a revised draft policy in September 1999 that outlined the program administration, prohibited payment of hours that were not specifically donated to an individual, and limited donations to 12 hours per fiscal year. Further, the department has consulted with the Office of the Attorney General on program legal issues.

Recommendations

- *The Department of Employee Relations should implement and enforce a vacation donation policy that complies with Minn. Stat. Section 43A.1815.*
- *The department should also consider whether a transfer of funds from the donating employees' agency to the recipient agency would be appropriate.*

3. The Minnesota Law Enforcement Association's employment agreement contradicts Minn. Stat. Section 43A.04, Subd. 8.

The Department of Employee Relations approved the Minnesota Law Enforcement Association employment bargaining agreement, which did not comply with Minn. Stat. Section 43A.04, Subd. 8. The statute permits an employee who is a member of the law enforcement union to annually donate up to ***three*** hours of accumulated vacation time to their union representative, for the purpose of carrying out the duties of the office. However, Article 32 of the bargaining agreement permits the donation of up to ***eight*** hours of accumulated vacation time each year. The department allowed each employee to donate up to eight hours.

During fiscal year 1999, 97 employees donated more than three hours of vacation hours to union representatives. Out of a total 710 hours donated, 419 hours were from employees donating more than the level specified in statute.

Recommendation

- *The Department of Employee Relations should seek clarification from the Office of the Attorney General on the validity of this bargaining agreement provision.*

This report is intended for the information of the Legislative Audit Commission and the management of the Department of Employee Relations. This restriction is not intended to limit the distribution of this report, which was released as a public document on March 16, 2000.

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

End of Fieldwork: December 22, 2000

Report Signed On: March 13, 2000

Status of Prior Audit Issues
As of December 1, 1999

<u>February 1999, Legislative Audit Report 99-7</u> examined the department's activities and programs material to the State of Minnesota's Comprehensive Annual Financial Report for the year ended June 30, 1998. The scope included the state's payroll expenditures, state employee insurance fund, public employees insurance fund, private employees insurance fund, workers' compensation liability, and compensated absences liability.

That audit cited one finding which has been resolved. In summary, the department has made significant efforts to improve its reporting of financial activity in accordance with generally accepted accounting principles, and properly valued its investments for the year ending June 30, 1999.

<u>December 1998, Legislative Audit Report 98-63</u> examined how the Department of Employee Relations and the Department of Finance jointly prevented unauthorized users from directly accessing the database which stores data for the Statewide Employee Management System (SEMA4), the state's integrated human resource and payroll system.

That audit cited four findings. The department had resolved all four findings. In summary, to better secure the data, the department assessed its vulnerabilities, and designed administrative procedures to protect the data. The department modified security clearances and reduced the number of users with access to the database. The department now monitors all access to the database and it has implemented new software to better secure users' passwords.

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.

Minnesota
Department of
Employee
Relations

State of Minnesota: Employer of Choice

March 14, 2000

James Nobles
Legislative Auditor
Centennial Building, First Floor
658 Cedar Street
St. Paul, MN 55155

Dear Mr. Nobles:

Thank you for the opportunity to respond to the Audit Report for the Department of Employee Relations.

Enclosed is our response to your findings and recommendations from your audit report for the fiscal year ending June 30,1999. We will work toward implementing the recommendations made by your audit as quickly as possible.

I want to thank you and your staff for the cooperation and assistance given us.

Sincerely,

/s/ Wayne Simoneau

Wayne Simoneau
Acting Commissioner

Enclosure

nobles99.doc

200 Centennial Office Building • 658 Cedar St. • St. Paul, MN 55155-1603 • (651) 297-1184 • TTY (651) 282-2699
An equal opportunity employer

Department of Employee Relations
Response to Audit Findings and Recommendation's

A. Internal control and noncompliance issues found during the annual audit

Finding #1. The Department of Employee Relations (DOER) did not transfer any portion of the available MEIP cash balance to the Health Care Access Fund, as directed by Minnesota statutes.

DOER Response:

The final administrative issues of Minnesota Employer's Insurance Program have not yet been resolved. Program administrators currently estimate that approximately $100,000 may be needed to resolve the current issues. At issue is the retroactive risk adjustment rate that is determined by the actuarial firm retained by the department. Several requests have been made to the firm to resolve these issues and allow the department to finalize the closing of the program. The current estimates by the program administrators to resolve these issues are that it could possibly extend into the next fiscal year. In the interim, the balance of the account has been returned to the Health Care Access Fund as suggested by the audit recommendation.

.

Finding #2. The Department of Employee Relations (DOER) did not adequately administer the vacation donation to sick leave program.

DOER Response:

The department has created an administrative procedure that will enforce vacation donation policy in compliance with M.S.43A.1815. The draft policy has been posted for comment as outlined in M.S. 43A04. Subd. 4. When the comment period expires and all comments have been considered, the policy will be implemented and enforced. A copy of the policy will be made available to the Office of the Legislative Auditor when it is published.

The recommendation of transferring funds was discussed with the Department of Finance during the development of the administrative procedure. At that time the decision was made that funds would not be transferred from a donating to a receiving agency. Information gathered from Finance shows that approximately two-thirds of all donations stay within the same agency, and the changes required to the States HR/Payroll system to facilitate the fund transfers would cost in excess of $80,000.

Finding #3. The Minnesota Law Enforcement Association's employment agreement contradicts Minn. Stat. Section 43A.04, Subd. 8.

DOER Response:

DOER is of the opinion that the vacation donation language in Article 32 of the agreement between the State of Minnesota and the Minnesota Law Enforcement Association is valid based on the legislative ratification of the agreement. However, as recommended by the Office of the Legislative Auditor, DOER will seek clarification from the Office of the Attorney General, and consider amending M.S. 43A.04 to incorporate this provision as a "term and condition" of employment that should be brought to the bargaining table.

99audit.doc