



OFFICE OF THE LEGISLATIVE AUDITOR
STATE OF MINNESOTA

Management Letter

Department of Labor and Industry
Fiscal Year Ended June 30, 2000



MARCH 1, 2001

01-06

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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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

Department of Labor and Industry

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Audit Participation

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

Claudia Gudvangen, CPA	Deputy Legislative Auditor
Brad White, CPA, CISA	Audit Manager
Charlie Gill	Auditor-in-Charge
April Snyder	Auditor

Exit Conference

The findings and recommendations in this report were discussed with the following officials of the Department of Labor and Industry at an exit conference held on February 21, 2001:

Gretchen Maglich	Commissioner
Michael Houliston	Deputy Commissioner
Roslyn Wade	Assistant Commissioner
Carolyn Ganz	Assistant Commissioner
Brandon Miller	Director, Special Compensation Fund
Cindy Farrell	Chief Financial Officer
John Kufas	Accounting Officer

Report Summary

Key Finding and Recommendation:

- The Department of Labor and Industry did not properly calculate the general long-term obligation for injured workers of uninsured or bankrupt employers. We found that the department overstated the liability due to historical data that had not been properly updated in its computerized system. We also noted inconsistent use of the computerized system by department claims managers. Recommendations were made to develop consistent practices and to consider training for claims managers. (Finding 1, page 3)

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 2000 audit, our work at the Department of Labor and Industry focused on financial activities of the Special Workers' Compensation Fund and the Occupational and Safety Health Act (OSHA) federal program administered by the department. The department's response to our recommendations is included in the report.

Department of Labor and Industry

Table 2
Major Federal Programs Administered by the Department of Labor and Industry
Fiscal Year 2000

CFDA #	Program Name	Expenditures
17.503	Occupational Safety and Health Act (OSHA)	\$3,555,000

Source: Department of Labor and Industry financial records for fiscal year 2000.

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, 2000, report included an unqualified opinion on the general purpose financial statements included in the State of Minnesota's Comprehensive Annual Financial Report for fiscal year 2000. In accordance with *Government Auditing Standards*, we also issued our report, dated December 1, 2000, 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 weaknesses in internal control at the Department of Labor and Industry.

1. The department did not properly calculate the general long-term obligation for injured workers of uninsured or bankrupt employers.

The Department of Labor and Industry estimated the long-term liability for the costs of ongoing claims of an uninsured or bankrupt employer. The Department of Finance includes this estimated obligation in the state's financial statements for the General Long-Term Obligation Account Group. These costs will be funded from future resources. The department utilized a new computerized system to derive its estimate for future permanent and temporary wage replacement and medical and rehabilitation costs for each injured worker. Our tests determined that the department's initial estimate of \$56 million was overstated by \$3.2 million. Adjustments were necessary to properly reduce the balance to our calculated balance of \$52.8 million. We noted the following problems.

- Upon acquiring a new computerized system, the department began updating historical liability estimates and payments into its database. We noted several cases where the individual's historical liability had been updated before fiscal year-end, but historical payments had not. This resulted in the liability being overstated by nearly \$3 million.

Department of Labor and Industry

- Claims managers do not always reduce estimates when a liability no longer exists. They inconsistently used, or were not familiar with, the department's computer system. An overstatement of \$256,000 resulted from one claims manager's assumption that when an individual's status changed it would reduce one category to zero when another was initiated. Another claims manager overstated estimates by \$36,000 when a claimant's status was changed from temporary to permanent disability. A new permanent disability estimate was determined, but the temporary estimate was not cancelled.
- Some managers were inconsistent with their treatment of certain estimated miscellaneous expenses. For example, one claims manager included a \$500 estimate for an independent medical evaluation. Other claims managers typically did not reserve for such costs.

We feel that many of these liability overstatements would be rectified if department claims managers were better trained on consistent practices for using the new computerized system.

Recommendation

- *The Department of Labor and Industry should develop consistent practices for determining its estimated long-term liability for injured workers of uninsured or bankrupt employers. The department should consider training needs for claims managers.*

This report is intended for the information of the Legislative Audit Commission and the management of the Department of Labor and Industry. This restriction is not intended to limit the distribution of this report, which was released as a public document on March 1, 2001.

/s/ James R. Nobles

James R. Nobles
Legislative Auditor

/s/ Claudia J. Gudvangen

Claudia J. Gudvangen
Deputy Legislative Auditor

End of Fieldwork: December 20, 2000

Report Signed On: February 27, 2001

**Status of Prior Audit Issues
As of December 20, 2000**

September 2000, Legislative Audit Report 00-47 examined the department's financial activities and programs for the three and one-half year period ending December 31, 1999. The scope included various fees and fines revenues, payroll and administrative expenditures, and grants. The report contained two findings involving the need for review of payroll reports and establishing reasonable timeframes for state safety grants. The department has worked to resolve the audit findings.

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 the metropolitan agencies, or the State Agricultural Society, the state constitutional officers, or the judicial branch.

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February 23, 2001

James R. Nobles
Legislative Auditor
Office of the Legislative Auditor
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658 Cedar Street
St. Paul, Minnesota 55155

Dear Mr. Nobles:

Thank you for the opportunity to review and comment on the finding addressed in the draft of your audit for the fiscal year ending June 30, 2000. This draft report accurately reflects the material that your staff discussed with us at the exit conference on February 21, 2001.

The fiscal year 2000 audit has one finding and recommendation for action. We find that the finding is reasonable and concur with the recommendation. We have enclosed a summary of your recommendation with our action response.

I would like to thank you and your staff for your review of our operations. The audit of our department is an opportunity for operation improvements, and we view it as a healthy learning experience.

Sincerely,

/s/ Gretchen B. Maglich

Gretchen Maglich
Commissioner

Enclosure

Recommendation

The Department of Labor and Industry should develop consistent practices for determining its estimated long-term liability for injured workers of uninsured or bankrupt employers. The department should consider training needs for claims managers.

Action Response

The most significant component of this finding deals with the conversion of data resulting from the implementation of the GenComp claims management system. Converting historical data to the new system has been an on-going process. The liability overstatement resulted from claims where an amount had been entered for the estimated liability, but the historical payment information had not.

The department's Financial Services unit has identified all claims where this overstatement has occurred, and will ensure that the historical payment information is entered prior to June 30, 2001. Procedures have also been modified to prevent this from occurring in the future as we continue to convert historical data.

Additional examples of inconsistency were noted for reserving practices by individual claims managers. To ensure that claim reserves are consistently entered and documented, the Special Compensation Fund claims managers will establish a procedure to reduce inconsistencies in reserving practices, review and retrain on the GenComp system's reserving capabilities, and document reserve changes with notes in the system. These changes will be implemented by May 1, 2001.