



OFFICE OF THE LEGISLATIVE AUDITOR
STATE OF MINNESOTA

Financial Audit Division Report

State Agricultural Society
Year Ended October 31, 2003



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 forty 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.

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, or evaluation, please contact us at 651-296-4708 or by e-mail at auditor@state.mn.us

State Agricultural Society

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Audit Participation

Claudia Gudvangen, CPA	Deputy Legislative Auditor
Jeanine Leifeld, CPA, CISA	Audit Manager
Scott Tjomsland, CPA	Auditor-in-Charge
Gena Hoffman	Auditor
Trinh Bui	Intern

Exit Conference

We discussed the results of the audit at an exit conference with the following staff of the State Agricultural Society on April 28, 2004:

Jerry Hammer	Executive Vice President
Marshall Jacobson	Controller

Report Summary

Key Conclusions and Finding:

- We issued an unqualified opinion on the State Agricultural Society's financial statements for the year ended October 31, 2003.
- We found that the Society has not appropriately safeguarded its computer system from unauthorized access. (Finding 1, page 4)

Other Findings:

- The Society did not promptly correct its general ledger for differences found while reconciling the bank account. (Finding 2, page 4)
- One Society employee was responsible for all payroll and personnel duties. The Society did not ensure that an independent person verified the payroll transactions for accuracy. (Finding 3, page 5)

The report contained a total of 3 findings relating to internal control. Two of the findings were prior issues partially resolved.

Audit Scope:

Audit Period: The year ended October 31, 2003

Programs Audited:

- Midway Activity
- Coliseum and Grandstand Revenue
- Gate and Parking Revenue
- Fair-Time Concession Revenue
- Non-Fair Event Revenue
- Payroll Expense
- Payout and Other Expenses
- Revenue Bond Issuance
- Fixed Assets
- Cash and Cash Equivalents

Agency Background:

The State Agricultural Society runs Minnesota's annual state fair and maintains the state fairgrounds. It earned about \$27.5 million in operating revenues during FY03 and had total assets of over \$45 million on October 31, 2003. It issued revenue bonds for the first time in FY03, with a principal amount of \$11.11 million, due over the next 20 years.



**Report on Compliance and on Internal Control over Financial Reporting
Based on an Audit of Financial Statements Performed in Accordance with
*Government Auditing Standards***

Representative Tim Wilkin, Chair
Legislative Audit Commission

Members of the Legislative Audit Commission

Ms. Clarice Schmidt, President
Board of Managers
State Agricultural Society

Members of the State Agricultural Society

Mr. Jerry Hammer, Executive Vice President
State Agricultural Society

We have audited the financial statements of the State Agricultural Society as of and for the year ended October 31, 2003, and have issued our report thereon dated March 19, 2004. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether the State Agricultural Society's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the State Agricultural Society's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies

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in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the State Agricultural Society's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. We describe reportable conditions as Findings 1 through 3 in the accompanying section entitled *Current Findings and Recommendations*.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce, to a relatively low level, the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we consider the reportable condition described in Finding 1 to be a material weakness.

This report is intended solely for the information and use of the State Agricultural Society's management and the Legislative Audit Commission and is not intended to be and should not be used by anyone other than these specified parties.

/s/ James R. Nobles

James R. Nobles
Legislative Auditor

March 19, 2004

/s/ Claudia J. Gudvangen

Claudia J. Gudvangen, CPA
Deputy Legislative Auditor

Current Findings and Recommendations

1. PRIOR FINDING PARTIALLY RESOLVED: The State Agricultural Society has not appropriately resolved its information technology security risks.

Our prior audit of the State Agricultural Society identified significant information technology security weaknesses. The Society lacked a comprehensive security foundation and had not addressed many relevant technology risks. We communicated the general nature of these weaknesses to Society's management in our written audit report. However, to minimize exposure to the organization, we also provided the Society with a confidential report of specific, detailed security findings and recommendations.

The Society's systems remain vulnerable to unauthorized access. It has taken steps to secure its systems from external harm. However, more work needs to be done to reduce the organization's exposure to an acceptable level. We are concerned that the Society still does not have complete written information technology security policies, procedures, or standards. This documentation is important because it constitutes the framework to positively control information technology resources. We also are concerned that many high-risk findings in our confidential report have not been addressed.

Recommendation

- *The State Agricultural Society should build a comprehensive security infrastructure that addresses current information technology risks.*

2. The Society did not promptly make adjusting entries to its general ledger cash account to correct recording discrepancies.

During fiscal year 2003, the Society did not timely adjust its general ledger cash account to correct recording differences identified during its reconciliation process. Although, as part of its monthly bank reconciliation process, the Society identified several reconciling items that were caused by recording differences in the general ledger, it did not make immediate corrections to the general ledger to resolve those items. As a result, the year-end cash balance recorded in the general ledger was originally overstated by about \$48,000. \$46,000 of the difference was a batch of checks, which the Society disbursed shortly before year-end. The checks were posted to accounts payable instead of cash in the general ledger. The remainder involved differences between recorded check disbursement amounts in the general ledger and actual check amounts, and unrecorded bank charges. The Society made our proposed adjusting entries to resolve the differences before it finalized the financial statements.

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Recommendation

- *The Society should promptly make adjusting entries to its general ledger cash account to correct differences identified through its bank reconciliation process.*

3. The Society did not adequately segregate duties related to payroll and human resources activity.

The Society employee responsible for processing payroll, including the employee's own transactions, was also responsible for recording human resources data in the payroll system. Besides processing bi-weekly payroll expenses, that employee was responsible for creating new employee records, changing pay rates, and changing leave accrual rates in the payroll system. Ideally, employees that process payroll should not have the ability to create new employee records, to adjust pay and leave accrual rates, or to process their own transactions. Without proper segregation, employees could manipulate payroll transactions to benefit themselves, without detection. If segregating duties is not plausible, the Society should establish mitigating controls, such as independent reviews of transactions or output reports, to alleviate the risk caused by the lack of segregation.

Recommendation

- *The Society should segregate duties related to payroll and human resources activity, or establish effective mitigating controls to alleviate the risk.*

**Status of Prior Audit Issues
As of March 19, 2004**

Most Recent Audit

The Office of the Legislative Auditor performs an annual audit of the State Agricultural Society. Legislative Audit Report 03-22, dated April 24, 2003, covered the fiscal year ended October 31, 2002. The audit scope included those areas material to the Society's financial statements. The report contained four findings. One finding related to the Society's information technology security risks. While the Society has taken some steps to address the issue, further action is necessary to fully resolve the finding, and we repeat the issue as Finding 1 in this report. Another finding concerned the Society's bank reconciliation process, which was substantially resolved. We report a related issue, however, as Finding 2 in this report. The Society resolved the other two findings, one related to the accuracy of the daily average ticket price of carnival tickets sold at the State Fair, and one related to contributions to deferred compensation plans.

MINNESOTA STATE

FAIR

THE GREAT MINNESOTA GET-TOGETHER
TWELVE DAYS OF FUN ENDING LABOR DAY

Jeanine Leifeld, CPA, CISA
Office of the Legislative Auditor
Room 140 Centennial Building
658 Cedar St.
St. Paul, MN 55155

May 5, 2004

Dear Jeanine,

Response to finding number one:

When the OLA initially recommended that the Society improve its computer security systems, it was agreed that the project would take a few years. During fiscal '03, the Society dedicated substantial time and resources to address areas of specific concern, and significant progress was made – particularly in securing the fair's systems from outside access. Additional IT staff has been added and will focus in the coming year on continuing to reduce exposure risks as well as completing written information technology security policies, procedures and standards.

Response to finding number two:

The \$46,000 in checks issued immediately before year's end were cash awards for winning participants in the fair's 4-H championship livestock auction and post-fair Beef Expo cattle show. Cash to cover the checks was not transferred to the fair's premium fund account until just after the start of the new fiscal year, and our statements were written accordingly. An adjusting entry was made, and the statements are correct as published.

Response to finding number three:

The State Fair will establish additional mitigating controls for its payroll and human resources activities.

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Jeanine Leifeld
Office of the Legislative Auditor

Our thanks to you and the audit team for your efforts on our behalf.

Sincerely,

/s/ Jerry Hammer

Jerry Hammer
Executive Vice President