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OFFICE OF THE LEGISLATIVE AUDITOR
STATE OF MINNESOTA

FINANCIAL AUDIT DIVISION REPORT

State Agricultural Society

Financial Statement Audit

Two Years Ended October 31, 2008

June 4, 2009 **Report 09-21**

FINANCIAL AUDIT DIVISION
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OFFICE OF THE LEGISLATIVE AUDITOR
State of Minnesota • James Nobles, Legislative Auditor

June 4, 2009

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Mr. Bob Lake, President
State Agricultural Society Board of Managers

Members of the State Agricultural Society

Mr. Jerry Hammer, Executive Vice President
State Agricultural Society

This report presents the results of our audit of the State Agricultural Society's (society) basic financial statements for the two years ended October 31, 2008. This report meets the audit standard requirements of the American Institute of Certified Public Accountants and the Government Accountability Office to communicate internal control matters identified in a financial statement audit. The audit was conducted by Jim Riebe, CPA, (Audit Manager) and Carl Otto, CPA, CISA (Auditor-in-Charge), assisted by auditors Lat Anantaphong and Paul Thompson.

We discussed the results of the audit with the society's staff on May 21, 2009. Management's response to our finding and recommendation is presented in the accompanying section of this report titled, Agency Response. We did not audit the response and, accordingly, we express no opinion on it.

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. This restriction is not intended to limit the distribution of this report, which was released as a public document on June 4, 2009.

/s/ James R. Nobles

James R. Nobles
Legislative Auditor

/s/ Cecile M. Ferkul

Cecile M. Ferkul, CPA, CISA
Deputy Legislative Auditor

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Report Summary

Conclusions

- The State Agricultural Society's (society) financial statements for the two years ended October 31, 2008, were presented fairly in accordance with generally accepted accounting principles in all material respects.

- Generally, the society's internal controls for selected financial operations were adequate, and the society complied with finance-related legal requirements. However, the fair had one control weakness that resulted in noncompliance with a bond covenant.

- The society implemented the prior audit recommendation by improving its monitoring of receipts from the Minnesota State Fair Foundation.

Finding

- The State Agricultural Society did not comply with a requirement in the bond covenant for its 2003 revenue bonds; it under-funded its debt service account by $107,161. (Finding 1, page 7)

Audit Objectives and Scope

Audit Objectives:

- To give an opinion on the society's financial statements.
- To review internal control and compliance with financial-related legal requirements over material financial operations.
- To determine the status of a prior audit recommendation.

Audit Period: The two years ended October 31, 2008.

Programs Audited:

- Cash and Cash Equivalents
- Revenue Bond and Note Liabilities
- Entertainer Payouts and Other Expenses
- Capital Assets
- Ticket Sales
- Payroll Expense

Background

The State Agricultural Society operates Minnesota's annual state fair and maintains the state fairgrounds. The society had a profit of about $900,000 for the year ended October 31, 2008 and had total assets of nearly $55 million at year-end.

State Agricultural Society

Agency Overview

The State Agricultural Society oversees the operation of the annual state fair and the maintenance of the fairgrounds. Under the authority of *Minnesota Statutes* 2008, Chapter 37, the society is a self-governing body and is exempt from the finance-related rules and regulations applicable to most state agencies. The ten-member board is comprised of one representative from each of the society's nine regional districts and a president.

The society publishes an annual report that includes its financial statements and our audit opinion on the financial statements. The society realized net income of about $900,000 in 2008. It had $36 million in operating revenues earned chiefly through ticket sales and rental of its facilities during non-fair time. Significant expenses included $17.9 million for activities and support, plant operations and maintenance of approximately $7.6 million, and depreciation of about $2.3 million. The society has not received state appropriations since approximately 1950.

The society had net assets of $38.1 million at October 31, 2008. Capital assets, net of depreciation, totaled $45.3 million; revenue bonds payable of about $9.2 million represented the society's largest liability.

Objectives, Scope, and Methodology

Our audit of the society's financial statements focused on the following objective, which included the consideration of internal controls and compliance with significant legal requirements over financial reporting:

- Were the society's basic financial statements for the two years ended October 31, 2008, fairly presented in accordance with generally accepted accounting principles in all material respects?

In addition to the financial statement objective, we considered these objectives:

- Were the society's internal controls over revenues, payroll and administrative expenses, cash and investments, debt service, and fixed assets adequate to ensure that it safeguarded receipts and other assets, accurately paid employees and vendors in accordance with management's authorization, and complied with significant finance-related legal requirements?

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

- Did the society implement a prior audit recommendation that it strengthen controls over the Minnesota State Fair Foundation's receipts?[1]

To answer these questions, we reviewed the accounting principles applicable to the society's financial statements. We gained an understanding of the society's accounting policies and procedures and the business systems used to administer its financial activities and to prepare the financial statements. We obtained and analyzed electronic accounting data and other audit evidence and reconciled the supporting data to the society's accounting system. We interviewed key personnel to gain an understanding of the control process for each audited area, including cash, capital assets, revenue bond liabilities, ticket sales, payroll expense, entertainer payouts, and other expenses.

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. We used the guidance contained in the Internal Control-Integrated Framework,[2] published by the Committee of Sponsoring Organizations of the Treadway Commission, as our criteria to evaluate agency controls. We also used the society's internal policies and procedures as evaluation criteria.

Conclusions

The society's financial statements for the two years ended October 31, 2008, were fairly presented in accordance with generally accepted accounting principles in all material respects.

Given the limited nature of our audit work on the financial statements, we do not express an overall opinion on the effectiveness of the society's internal controls or compliance over financial reporting. In addition, our work may not have identified all significant control deficiencies or instances of noncompliance with legal requirements. However, the State Agricultural Society did not comply with a requirement in the bond covenant for its 2003 revenue bonds; it under-funded its

[1] Office of the Legislative Auditor's Financial Audit Division Report 08-16, *State Agricultural Society*, issued June 12, 2008.

[2] The Treadway Commission and its Committee of Sponsoring Organizations were established in the 1980s 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.

debt service account by $107,161. We consider this weakness to be a significant deficiency.[3]

In relation to our additional control and compliance objectives, the society had adequate controls and complied with the finance-related legal requirements we tested and implemented a prior audit recommendation to strengthen controls over the Minnesota State Fair Foundation's receipts.

The following *Finding and Recommendation* section explains the weakness noted above.

[3] According to auditing standards, a material weakness is a deficiency, or combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented or detected and corrected on a timely basis. A significant deficiency is a deficiency, or combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Finding and Recommendation

Finding 1

The State Agricultural Society did not comply with a requirement in the bond covenant for its 2003 revenue bonds; it under-funded its debt service account by $107,161.

The society's bond covenants require that the society deposit a sufficient amount in the debt service account on September 16 each year to fund the debt service principal and interest amounts due in the following fiscal year.[4] However, as of October 31, 2008, the $731,335 balance in the debt service account was not sufficient to pay the $874,705 debt service principal and interest amount due in September 2009. The society transferred an additional $107,161 into the account in March 2009 in order to fund the account to the required level. Since the account earns interest, the society relied on the bank to determine the proper amount to deposit. However, the society is ultimately responsible for ensuring compliance with the bond covenant.

Recommendation

- *The society should compare the balance in the debt service account on September 16 each year to the debt service payment schedule to ensure compliance with the funding requirement specified in the bond covenants.*

[4] Section 505 (1) - Payments into Certain Funds.

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

Mr. James R. Nobles
Office of the Legislative Auditor
Room 140 Centennial Building
658 Cedar St.
St. Paul, MN 55155

May 28, 2009

Dear Mr. Nobles,

Our thanks to you, Jim Riebe and the audit team for your efforts on our behalf. We appreciate your help.

Regarding the finding, the Society replenishes its bond debt service account each September according to an amount specified by invoice from the bank that maintains the account. In September 2008, we paid an invoice provided by the bank that reflected a lower amount than required. In March of 2009, the discrepancy was discovered and we paid the balance due. In the future, the Society's controller will review and verify that the bank invoices reflect the proper amount to be deposited in the bond debt service account.

Again, our thanks to the audit team for their help.

Sincerely,

Jerry Hammer

Jerry Hammer
Executive Vice President

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