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**OFFICE OF THE LEGISLATIVE AUDITOR**  
**STATE OF MINNESOTA**

**FINANCIAL AUDIT DIVISION REPORT**

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**Department of Education**  
**Federal Compliance Audit**  
**Year Ended June 30, 2009**

**March 12, 2010**

**Report 10-08**

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FINANCIAL AUDIT DIVISION

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## OFFICE OF THE LEGISLATIVE AUDITOR

State of Minnesota • James Nobles, Legislative Auditor

March 12, 2010

Senator Ann H. Rest, Chair  
Legislative Audit Commission

Members of the Legislative Audit Commission

Ms. Alice Seagren, Commissioner  
Department of Education

This report presents the results of our audit of certain federal financial assistance programs administered by the Department of Education during fiscal year 2009. We conducted this audit as part of our audit of the state's compliance with federal program requirements. We emphasize that this has not been a comprehensive audit of the Department of Education.

We discussed the results of the audit with department staff at an exit conference on March 1, 2010. This audit was conducted by David Polisen, CPA, CISA, CFE, (Audit Manager) and Tim Rekow, CPA, (Auditor-in-Charge), assisted by Zach Yzermans, CPA, Kathy Rootham, Blake Schwagel, and Mai Na Yang.

This report is intended for the information and use of the Legislative Audit Commission and the management of the Department of Education. This restriction is not intended to limit the distribution of this report, which was released as a public document on March 12, 2010.

We received the full cooperation from the department's staff while performing this audit.

*/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

## Conclusion

The Department of Education generally complied with and had controls to ensure compliance with provisions of laws, regulations, contracts, and grants applicable to the federal programs we audited for fiscal year 2009. However, the department had several weaknesses as noted in the four findings presented in this report. The department resolved four of five fiscal year 2008 findings.

## Key Findings

- Prior Finding Partially Resolved: The Department of Education did not identify, analyze, and document its internal controls over compliance with federal single audit requirements. ([Finding 1, Page 5](#))
- The Department of Education did not always verify that it paid local education agencies for actual special education program expenditures. ([Finding 2, Page 6](#))
- The Department of Education did not comply with federal subrecipient monitoring requirements for the special education program. ([Finding 3, page 7](#))

## Audit Scope

Programs material to the State of Minnesota's federal program compliance for fiscal year 2009:

- Child Nutrition Cluster<sup>1</sup> (CFDA 10.553, 10.555, 10.556, and 10.559)
- Child and Adult Care Food (CFDA 10.558)
- Title 1 – Grants to Local Education Agencies (CFDA 84.010)
- Special Education Cluster (CFDA 84.027 and 84.173)
- Improving Teacher Quality State Grants (CFDA 84.367)

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<sup>1</sup> A cluster of programs is a group of closely related programs that have similar compliance requirements and are treated as a single program.

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# Department of Education

## Federal Program Overview

The Department of Education administered federal programs that we considered major federal programs for the State of Minnesota, subject to audit under the federal Single Audit Act.<sup>2</sup> Table 1 identifies these major federal programs.

**Table 1**  
**Major Federal Programs**  
**Administered by the Department of Education**  
**Fiscal Year 2009**

<u>CFDA<sup>1</sup></u>	<u>Program Name</u>	<u>Expenditures</u>
	<u>Child Nutrition Cluster:<sup>2</sup></u>	
10.553	School Breakfast Program	\$ 27,539,703
10.555	National School Lunch Program	114,049,030
10.556	Special Milk Program for Children	847,865
10.559	Summer Food Service Program for Children	3,439,853
	Total Child Nutrition Cluster	<u>\$145,876,451</u>
10.558	Child and Adult Care Food Program	\$ 61,432,663
84.010	Title 1—Grants to Local Education Agencies	\$125,235,105
	<u>Special Education Cluster:</u>	
84.027	Special Education Grants to State	\$196,042,068
84.173	Special Education Preschool Grants	8,222,849
	Total Special Education Cluster	<u>\$204,264,917</u>
84.367	Improving Teacher Quality State Grants	\$ 41,057,067

<sup>1</sup>The Catalog of Federal Domestic Assistance (CFDA) is a unique number assigned by the federal government to identify its programs.

<sup>2</sup>A cluster of programs is a grouping of closely related programs that have similar compliance requirements and is treated as a single program for audit purposes.

Source: Minnesota Accounting and Procurement System.

<sup>2</sup> We defined a major federal program for the State of Minnesota in accordance with a formula prescribed by the federal Office of Management and Budget as a program or cluster of programs whose expenditures for fiscal year 2009 exceeded \$30.1 million.

## Objective, Scope, and Methodology

The objective of our audit was to determine whether the Department of Education complied with federal program requirements in its administration of these federal programs for fiscal year 2009 and to determine whether the department had resolved issues from past audits. This audit is part of our broader federal single audit objective to obtain reasonable assurance about whether the State of Minnesota complied with the types of compliance requirements that are applicable to each of its federal programs.<sup>3</sup> In addition to specific program requirements, we examined the department's general compliance requirements related to federal assistance, including its cash management practices.

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 the *Government Auditing Standards*, issued by the Comptroller General of the United States of America and with the U.S. Office of Management and Budget's *Circular A-133 Compliance Supplement*.

## Conclusion

The Department of Education generally complied with and had controls to ensure compliance with certain provisions of laws, regulations, contracts, and grants applicable to its major federal programs for fiscal year 2009. However, the department had some weaknesses, as noted in the following *Findings and Recommendations* section.

We have reported these weaknesses to the federal government in the *Minnesota Financial and Compliance Report of Federally Assisted Programs*, prepared by Department of Management and Budget. This report provides the federal government with information about the state's use of federal funds and its compliance with federal program requirements. The report includes the results of our audit work, conclusions on the state's internal controls over and compliance with federal programs, and findings about control and compliance weaknesses.

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<sup>3</sup> The State of Minnesota's single audit is an entity audit of the state that includes both the financial statements and the expenditures of federal awards by all state agencies. We issued an unqualified audit opinion, dated December 11, 2009, on the State of Minnesota's basic financial statements for the year ended June 30, 2009. In accordance with *Government Auditing Standards*, we also issued our report on our consideration of the State of Minnesota's internal control over financial reporting and our tests of compliance with certain provisions of laws, regulations, contracts, and grants. (Office of the Legislative Auditor's Financial Audit Division Report 10-01, *Report on Internal Control Over Financial Reporting*, issued February 11, 2010.) This report included control deficiencies related to the Department of Education.

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# Findings and Recommendations

## Finding 1

**Prior Finding Partially Resolved: The Department of Education did not identify, analyze, and document its internal controls over compliance with federal single audit requirements.**

The department did not have a comprehensive risk assessment pertaining to its internal controls over compliance with federal single audit requirements. The department had an increased likelihood of a control deficiency if it did not clearly communicate to all staff its risks, control activities, and monitoring policies and procedures.

State policy states that each agency head has the responsibility to identify, analyze, and manage business risks that impact an entity's ability to maintain its financial strength and the overall quality of its products and government services.<sup>4</sup> This policy also requires communication of the internal control policies and procedures to all staff so they understand what is expected of them and the scope of their freedom to act. The policy further requires follow-up procedures that, at a minimum, should include ways to monitor results and report significant control deficiencies to individuals responsible for the process or activity involved, including executive management and those individuals in a position to take corrective action. Audit standards reinforced management's responsibility to have effective internal controls over its financial operations.<sup>5</sup> The federal government expects that those controls also ensure compliance with federal program requirements.

The Department of Education is aware of certain risks, has many control activities in place, and performs selected internal control monitoring functions. However, the department did not comprehensively identify and analyze the risks, design its controls to address significant risks, or develop monitoring procedures to ensure that controls are in place and are effective to reduce the significant risks identified. Since the last audit, the department completed risk assessments for the Child Nutrition Cluster and Child and Adult Care Food programs.

A comprehensive control structure has the following key elements:

- Personnel are trained and knowledgeable about federal single audit requirements and applicable policies and procedures.

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<sup>4</sup> Department of Management and Budget Policy Number 0102-01.

<sup>5</sup> Statement on Auditing Standards #109.

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- Management identifies risks associated with federal single audit requirements and develops policies and procedures to effectively address the identified risks.
- Management continuously monitors the effectiveness of the controls, identifies weaknesses and breakdowns in controls, and takes corrective action.
- Management focuses on continual improvement to ensure an acceptable balance between controls and costs.

Findings 2 through 4 identify deficiencies in the department's internal control procedures and specific noncompliance with federal requirements that were not prevented or detected by the department's internal control structure. These deficiencies created an unacceptable risk of noncompliance or did not prevent or detect the noncompliance. It is likely that the department will continue to have noncompliance and weaknesses in internal controls over compliance until it operates within a comprehensive internal control structure.

#### *Recommendation*

- *The department should frequently review and clearly document its risks, control activities, and internal control monitoring functions for federal program requirements.*

## **Finding 2**

**The Department of Education did not always verify that it paid local education agencies for actual special education program expenditures.**

The department did not determine whether its payments for two federal programs agreed with actual expenditures reported by the local education agencies. For the Special Education Grants to States (CFDA 84.027<sup>6</sup>) and Special Education Preschool Grants (CFDA 84.173<sup>7</sup>), the department used information from its Electronic Data Reporting System as the basis to determine periodic payments to the local education agencies. However, the local education agencies reported actual expenditures and, ultimately, audited expenditures on the department's Uniform Financial Accounting and Reporting Standards.

For 10 out of 13 local education agencies we tested, the amounts disbursed by the department through the Electronic Data Reporting System did not agree to the expenditures reported by the local education agencies at year end in the Uniform Financial Accounting and Reporting Standards system. For these 10 local education agencies, discrepancies between the department's payment amounts

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<sup>6</sup> Federal Award H027A070087A.

<sup>7</sup> Federal Award H173A070086.

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and the local education agencies' reported actual expenditures at year end ranged from about \$1,000 to \$600,000.

Without a determination of the reasons for these discrepancies between the department's payments and the local education agencies' reported actual costs, the department could over or underreimburse the agencies for their special education expenditures.

*Recommendation*

- *The department should verify that its payments to local education agencies agreed with actual special education expenditures reported at year end.*

**The Department of Education did not comply with federal subrecipient monitoring requirements for the special education program.**

**Finding 3**

The department did not perform adequate subrecipient monitoring for the Special Education Grants to States (CFDA 84.027<sup>8</sup>) and Special Education Preschool Grants (CFDA 84.173<sup>9</sup>) programs. Although the department conducted site visits of local education agencies, it did not formally communicate the results of those site visits to the local education agencies or the department's management. The purpose of the site visits was to determine whether the local education agency complied with federal regulations and program eligibility requirements. The department said that during fiscal year 2009 it conducted 33 site visits, but only one site visit had a documented report of its results. That report identified \$12,925 of unallowable costs.

Federal regulations required the department to provide reasonable assurance that subrecipients used federal awards for authorized purposes, complied with laws, regulations, and the provisions of contracts and grant agreements, and achieved performance goals.<sup>10</sup> The department used site visits as a part of its monitoring activities. The department did not have policies or procedures that established standards for documenting and reviewing the work performed, reporting on the results, and tracking the resolution of issues identified.

*Recommendation*

- *The department should establish policies and procedures to ensure special education site visits are reviewed, results are reported, appropriate corrective action plans are completed, and instances of noncompliance are resolved in a timely manner.*

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<sup>8</sup> Federal Award H027A070087A and H027A080087.

<sup>9</sup> Federal Award H173A070086 and H173A080086.

<sup>10</sup> OMB Circular No. A-133.

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## Finding 4

### **The Department of Education did not always document time charged to federal programs in compliance with federal requirements.**

The department did not always document payroll costs charged to applicable federal programs, including Special Education Grants to States (CFDA 84.027<sup>11</sup>), Special Education Preschool Grants (CFDA 84.173<sup>12</sup>), and Title I -- Grants to Local Education Agencies (CFDA 84.010<sup>13</sup>). The documentation to support payroll costs for four of seven employees we tested did not comply with federal requirements. Specifically, the department's documentation was deficient as follows:

- Two employees did not have required personnel activity reports to support the allocation of their payroll costs to the federal program.
- Two employees had personnel activity reports that were not consistent with the time reported on the state's payroll system.

Federal regulations require that payroll costs charged to specific programs must be supported by evidence to show that the employees worked on those programs.<sup>14</sup> The regulations require each employee who works on multiple programs to periodically complete a personnel activity report. This report tracks the time the employee actually spends on each program's duties and should either support that the payroll system's allocation of payroll hours reasonably approximates the employee's actual hours or should prompt a change to the payroll system's allocation.

#### *Recommendation*

- *The department should ensure that employees understand federal requirements for documenting time charged to federal programs and monitor whether employees appropriately and accurately complete personnel activity reports.*

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<sup>11</sup> Federal Award H027A080087.

<sup>12</sup> Federal Award H173A070086.

<sup>13</sup> Federal Award S010A070023A and A010A080023.

<sup>14</sup> OMB Circular No. A-87.

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March 8, 2010

James Nobles  
Office of the Legislative Auditor  
Room 140 Centennial Building  
658 Cedar Street  
St. Paul, MN 55155-1063

Dear Mr. Nobles:

Thank you for the opportunity to respond to the findings for the Minnesota Department of Education ("Department") which are included in the single audit work on selected federal programs for the Department for the year ended June 30, 2009. Specific issues for the Department are included in findings 1-4. The response, person responsible for implementation and timeframe is included with each finding.

The Department is in agreement with the findings and plans to begin corrective action and/or implementation immediately.

**Finding 1: "Prior Finding Partially Resolved: The Department did not identify, analyze, and document its internal controls over compliance with federal single audit requirements."**

*OLA Recommendation: "The Department should frequently review and clearly document its risks, control activities, and internal control monitoring functions for federal program requirements"*

The Department agrees with this recommendation and will continue to work on the risk assessment and internal control structure. The Department has and will be working with and through the guidance being provided by the Internal Controls group at Minnesota Management and Budget. With their direction, it is expected the Department will be on track to complete the assessment and analysis by the end of state fiscal year 2011.

The manager responsibility for implementation of this finding will be Tammy McGlone, Director of Administrative Services.

**Finding 2: “The Department of Education did not always verify that it paid local education agencies for actual special education program expenditures.”**

*OLA Recommendation: “The department should verify that its payments to local education agencies agreed with actual special education expenditures reported at year end.”*

For state fiscal year (FY) 2009, MDE will verify that its special education payments to local education agencies (LEAs) agree with audited expenditures reported under the Uniform Financial Accounting and Reporting Standards (UFARS) by implementing the following procedures:

- LEAs will be required to reconcile expenditures reported through the Electronic Data Reporting System (EDRS), which were used to make state special education aid payments and federal aid payments for IDEA Part B, Sections 611 and 619, with audited expenditures reported through UFARS. This will be completed by June 30, 2010.
- MDE is currently transitioning away from the use of EDRS for payment of special education aids. For state FY 2010 and later, federal aid payments for IDEA Part B, Sections 611 and 619, are being made using the new State Educational Record View and Submission (SERVS) system. MDE will require expenditures reported through SERVS to match the audited expenditures reported through UFARS.
- The reconciliation process outlined above for state FY 2009 will continue to be used for state special education for state FY 2010 and until the transition is completed to the new system.

Tom Melcher, Director of Program Finance, will be responsible for resolving this finding and the Department expects the finding to be resolved by July 1, 2010.

**Finding 3: “The Department of Education did not comply with federal sub-recipient monitoring requirements for special education program.”**

*OLA Recommendation: “The department should establish policies and procedures to ensure special education site visits are reviewed, results are reported, appropriate corrective action plans are completed, and instances of noncompliance are resolved in a timely manner.”*

The Department will implement the recommendations of the auditor. Policies and procedures will be established to ensure findings are reviewed, reported and corrective action plans completed

Elizabeth Stephens, Acting Director of Program Accountability and Compliance, will be responsible for resolving this finding and the Department expects the finding to be fully resolved by July 1, 2010.

**Finding 4: “The Department of Education did not always document time charged to federal programs in compliance with federal requirements.”**

*OLA Recommendation: "The department should ensure that employees understand federal requirements for documenting time charged to federal programs and monitor whether employees appropriately and accurately complete personnel activity reports."*

The Department agrees with the auditors findings and has already implemented corrective action. In addition to auditing the payroll labor distribution sheets each payroll period, we will now audit that labor distribution against personnel activity reports. We are also creating a standard form for PARS that will be used consistently by all employees. Finally, we have reinstituted the quarterly certification of labor distribution posting for all salary and benefits charges to state and federal funds as an additional verification that payroll charges are properly reflected in all accounts in all funds.

Tammy McGlone, Director of Administrative, is responsible for resolving this finding and the Department expects the finding to be fully resolved by May 1, 2010.

I appreciate the opportunity to respond to the findings for the Department of Education. Please contact Tammy McGlone at 651-582-8835 if you have any questions or comments.

Sincerely,

A handwritten signature in cursive script, reading "Alice Seagren".

Alice Seagren  
Commissioner

C: Chas Anderson  
Tom Melcher  
Tammy McGlone  
Cathy Wagner