



OFFICE OF THE LEGISLATIVE AUDITOR
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FINANCIAL AUDIT DIVISION REPORT

Public Utilities Commission

Internal Control and Compliance Audit

July 1, 2007, through February 28, 2010

June 15, 2010

Report 10-21

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OFFICE OF THE LEGISLATIVE AUDITOR

State of Minnesota • James Nobles, Legislative Auditor

June 15, 2010

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Public Utilities Commission

Members of the Public Utilities Commission

Mr. Burl Haar, Executive Director
Public Utilities Commission

This report presents the results of our internal control and compliance audit of the Minnesota Public Utilities Commission for the period July 1, 2007, through February 28, 2010.

We discussed the results of the audit with the Public Utilities Commission on June 3, 2010. The audit was conducted by Brad White, CPA, CISA, CFE (Audit Manager) and Jamie Majerus, CPA (Auditor-in-Charge), assisted by auditors Anna Solomka and Alex Weber.

This report is intended for the information and use of the Legislative Audit Commission and the management of the Public Utilities Commission. This restriction is not intended to limit the distribution of this report, which was released as a public document on June 15, 2010.

We received the full cooperation of the Public Utilities Commission's staff while performing this audit.

A handwritten signature in black ink that reads 'James R. Nobles'.

James R. Nobles
Legislative Auditor

A handwritten signature in black ink that reads 'Cecile M. Ferkul'.

Cecile M. Ferkul, CPA, CISA
Deputy Legislative Auditor

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Report Summary

Conclusion

The Public Utilities Commission generally had adequate internal controls to ensure it safeguarded its assets, accurately paid employees and vendors in accordance with management's authorization, complied with finance-related legal requirements, and produced reliable financial data. For the items tested, the commission generally complied with finance-related legal requirements. However, the commission had weaknesses in its internal controls and noncompliance with certain finance-related legal requirements. The commission resolved four prior audit findings.

Key Findings

- The Public Utilities Commission did not identify, analyze, and document internal controls related to its business operations. ([Finding 1, page 7](#))
- The Public Utilities Commission provided an employee with incompatible access to the state's accounting system without defined mitigating controls and other staff with excessive access to update the commission's assessment system. ([Finding 2, page 8](#))
- The Public Utilities Commission made some errors in amounts assessed to utility companies. ([Finding 3, page 9](#))
- The Public Utilities Commission did not sufficiently coordinate and control the Telephone Assistance Plan surcharge revenues and grant expenditures. ([Finding 4, page 10](#))
- The Public Utilities Commission did not document management authorization for employee pay increases and achievement awards and did not complete written performance evaluations of staff. ([Finding 5, page 12](#))
- The Public Utilities Commission did not have a written agreement with the Department of Commerce for some shared staff and computer system costs. ([Finding 6, page 13](#))

Audit Objectives and Scope:

Objectives

- Internal Controls
- Compliance

Period Audited

July 1, 2007, through February 28, 2010

Programs Audited

- Assessments to Utility Companies
- Telephone Assistance Plan
- Equipment and Sensitive Assets

- Employee Personnel/Payroll
- Employee Travel Reimbursements
- Administrative Expenditures

Public Utilities Commission

Overview

The Public Utilities Commission is a state agency with regulatory jurisdiction over Minnesota's natural gas, electric, and telecommunications utilities. The commission has five members appointed by the governor to six-year staggered terms. By law, no more than three commissioners can be from the same political party. The commission employs approximately 50 staff. Mr. Burl Haar has served as the commission's executive secretary since 1993.

The commission's powers and responsibilities are specified principally in *Minnesota Statutes 2009*, Chapters 216, 216A, 216B, and 237.

The Public Utilities Commission is organized into various units, each with specific responsibilities:

- **Administration** includes the executive secretary and administrative support for the five commissioners. It provides human resources, information technology, and budget/fiscal support services for the commission.
- **Legal Unit** provides legal guidance to assist the commissioners in their decision-making process.
- **Consumer Affairs Unit** facilitates consumer education and dispute resolution for the commission. The unit's staff provide mediation assistance to consumers filing complaints against utilities under the commission's jurisdiction.
- **Energy Unit** reviews all natural gas and electric matters, including rate changes, energy resource planning and certification, service area matters, mergers and acquisitions, and formal complaints.
- **Energy Facilities Permitting Unit** is responsible for the site or route permitting of certain energy facilities, including power plants, wind turbines, transmission lines, and pipelines.
- **Telecommunications Unit** reviews matters relating to rates and services of telephone companies. The unit also assists the commission in addressing significant policy issues regarding the ongoing evolution of competition in the telecommunications industry.

The Public Utilities Commission receives the majority of its funding from state appropriations. Although the commission assesses utility companies to recover its operating costs, statutes require the commission to credit the assessment revenue to the state's General Fund. As a result, the assessment revenue is not available to fund

the commission's operating costs. Other significant revenues include telephone surcharges paid by consumers for the Telephone Assistance Plan and assessments to recover the cost of services provided by the Office of Administrative Hearings. These dedicated revenues are used to fund commission expenses for those purposes.

Table 1 summarizes the commission's sources and uses of financial resources by fund for fiscal year 2009.

Table 1
Sources and Uses of Financial Resources
Fiscal Year 2009

	<u>General Fund</u>	<u>Special Revenue Fund²</u>	<u>Telephone Assistance Plan</u>
Sources¹			
Appropriation	\$5,433,000	\$ 0	\$ 0
Dedicated Receipts ³	0	411,247	2,057,194
Balance Forward-In from fiscal year 2008	<u>645,893</u>	<u>101,677</u>	<u>4,455,303</u>
Total Sources	<u><u>\$6,078,893</u></u>	<u><u>\$512,924</u></u>	<u><u>\$6,512,497</u></u>
Uses			
Payroll	\$4,028,368	\$ 0	\$ 18,144
Grants	0	0	1,392,919
Services ⁴	703,831	406,857	0
Rent	414,085	0	0
Supplies and Equipment	275,416	0	0
Travel	39,422	0	0
Other	<u>198,058</u>	<u>0</u>	<u>12,138</u>
Subtotal	<u>\$5,659,180</u>	<u>\$406,857</u>	<u>\$1,423,201</u>
Appropriation Cancellation ⁵	418,713	0	0
Transfers-Out ⁶	1,000	0	4,000,000
Balance Forward-Out to fiscal year 2010	<u>0</u>	<u>106,067</u>	<u>1,089,296</u>
Total Uses	<u><u>\$6,078,893</u></u>	<u><u>\$512,924</u></u>	<u><u>\$6,512,497</u></u>

¹The commission also collected nondedicated receipts, totaling \$4,672,733, for assessments to utility companies. As required by statute, the commission deposited those receipts into the state's General Fund, and the receipts were not available for spending by the commission.

²The commission used a Special Revenue Fund predominantly for revenues and expenditures related to administrative hearing services.

³Dedicated receipts are collected and used to fund costs from the Office of Administrative Hearings and grants for the Telephone Assistance Plan.

⁴Services include purchased and professional-technical contract services and legal services provided by the Office of Administrative Hearings.

⁵Unspent appropriation amounts that reverted back to the state's General Fund.

⁶Pursuant to 2008 Minnesota Laws, Chapter 363, Article 6, Section 4, the commission transferred \$4 million from the Telephone Assistance Plan to the state's General Fund.

Source: Minnesota Accounting and Procurement System.

Objectives, Scope, and Methodology

Our audit of the Public Utilities Commission included the material revenues and expenditures for the period of July 1, 2007, through February 28, 2010, and focused on the following audit objectives:

- Were the commission's internal controls adequate to ensure that it safeguarded its assets, accurately paid employees and vendors in accordance with management's authorizations, complied with finance-related legal requirements, and created reliable financial data?
- Did the commission comply with significant finance-related legal requirements?
- Did the commission resolve prior audit findings?¹

To meet the audit objectives, we gained an understanding of the commission's financial policies and procedures. We considered the risk of errors in the accounting records and noncompliance with relevant legal requirements. We analyzed accounting data to identify unusual trends or significant changes in financial operations. In addition, we selected a sample of financial transactions and reviewed supporting documentation to test whether the controls were effective and if the transactions complied with laws, regulations, policies, and grant, contract, and loan provisions.

We conducted the audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives.

We used the guidance contained in the *Internal Control-Integrated Framework*, published by the Committee of Sponsoring Organizations of the Treadway Commission, as our criteria to evaluate the commission's internal controls.² We used state and federal laws, regulations, and contracts, as well as policies and procedures established by the Department of Management and Budget and the Department of Administration and the commission's internal policies and procedures as evaluation criteria over compliance.

¹ Minnesota Office of the Legislative Auditor, Financial Audit Division Report 06-19, *Public Utilities Commission*, issued July 14, 2006.

² The Treadway Commission and its Committee of Sponsoring Organizations were established in 1985 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. The resulting *Internal Control-Integrated Framework* is the accepted accounting and auditing standard for internal control design and assessment.

Conclusions

The Public Utilities Commission generally had adequate internal controls to ensure it safeguarded its assets, accurately paid employees and vendors in accordance with management's authorization, complied with finance-related legal requirements, and produced reliable financial data. For the items tested, the commission generally complied with finance-related legal requirements. However, the commission had weaknesses in its internal controls and noncompliance with certain finance-related legal requirements. The commission resolved four prior audit findings.

The following *Findings and Recommendations* further explain the commission's internal control and compliance weaknesses.

Findings and Recommendations

The Public Utilities Commission did not identify, analyze, and document internal controls related to its business operations.

The commission did not have a comprehensive approach to the design of its internal controls over financial operations and compliance with finance-related legal requirements. The commission had an increased likelihood of control weaknesses because it did not clearly document and communicate to all staff its risks, control activities, and monitoring policies and procedures.

State policy stipulates that each agency head has the responsibility to identify, analyze, and manage business risks that impact the agency's ability to maintain its financial strength and the overall quality of its products and government services.³ 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. This policy also 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.

The commission is aware of certain risks, has many control activities in place, and performs selected internal control monitoring functions. However, the commission had not comprehensively identified and analyzed the risks, designed its controls to address significant risks, or developed monitoring procedures to ensure the controls are in place and are effective to reduce the significant risks identified.

Findings 2 through 12 identify weaknesses in the commission's internal control procedures and specific noncompliance with finance-related legal requirements that the commission's internal control structure did not prevent or detect. If the commission had a comprehensive internal control structure, it could have identified these deficiencies, assessed the degree of risk of these weaknesses, designed control procedures to address significant risks, and monitored whether controls were working as designed and effective in reducing the risks to an acceptably low level. It is likely that the commission will continue to have noncompliance and weaknesses in internal controls over compliance until it operates within a comprehensive internal control structure.

Finding 1

³ Department of Management and Budget Policy 0102-01.

Recommendation

- *The commission should regularly review, clearly document, and communicate to staff its risks, control activities, and internal control monitoring functions for its key business processes.*

Finding 2

The Public Utilities Commission provided an employee with incompatible access to the state's accounting system without defined mitigating controls and other staff with excessive access to update the commission's assessment system.

The commission did not develop a strategy to mitigate the risks created by providing employees with incompatible and excessive access to various computerized systems they used. In a small agency, it may at times be necessary to allow some employees with incompatible access. The risk of errors and fraud increases when employees have incompatible or excessive access to computerized systems unless controls are designed to mitigate those risks. The commission had the following weaknesses in its system access controls:

- The commission assigned one employee with incompatible access to accounting system functions. This access allowed the employee to control the entire transaction (initiate purchases, acknowledge receipt of the purchased items, and pay the vendors). State policies require agencies to avoid allowing their employees to have incompatible access to the state's accounting systems.⁴ State policies also require that if incompatible access is unavoidable, the agency must develop effective mitigating controls to reduce the risk that an employee will exploit the weakness without detection. Although the employee's supervisor periodically scanned transaction reports, this was not an effective mitigating control because it did not include a comparison to original transaction documentation, such as purchase orders and invoices.
- The commission also allowed three employees excessive or unnecessary access to update the assessment system. They provided access to certain employees that did not need system access to perform their job responsibilities. In addition, once the commission determined that an employee needed access to the assessment system, it did not limit that access to the minimum level necessary for the employee's job duties.

⁴ Department of Management and Budget Policy 1101-07.

Recommendations

- *The commission should eliminate incompatible access to the state's accounting system. If incompatible access cannot be segregated, the commission should design, document, and implement an effective mitigating control review.*
- *The commission should eliminate unnecessary access to the utility assessment system and limit system access to employees as needed to fulfill their job responsibilities.*

The Public Utilities Commission made some errors in amounts assessed to utility companies.

The commission used an incorrect overhead rate and inaccurate settlement percentages in its assessments to bill energy and telephone companies. The commission bills utility companies for costs related to specific projects (direct assessments) and for costs that cannot be assigned to a specific project (indirect assessments). *Minnesota Statutes* require the commission to recover costs spent on an investigation, appraisal, or services provided to public utility companies.⁵ The commission had the following errors in assessments we tested:

- The commission used the wrong overhead rate for two quarters in 2008 causing utility companies to be undercharged by \$15,600. Although it calculated an overhead rate of 1.88 percent based on labor costs and other operating expenses, it used an overhead rate of 1.81 percent in its billings to utility companies. (The erroneous overhead rate was multiplied by the number of direct hours charged to an investigation, service, or specific project performed for a utility company.) The commission plans to add the amount previously underbilled to the third quarter assessments for fiscal year 2010.
- The commission used inaccurate settlement percentages for the 2009 indirect cost amounts assessed to utility companies. *Minnesota Statutes* require the commission to estimate the indirect assessments each quarter based on a utility company's gross revenues and then settle the difference between estimated and actual costs on a subsequent assessment.⁶ The commission had errors in the percentages it calculated for each industry type (electric, gas, telephone) causing the settlement amounts to be

Finding 3

⁵ *Minnesota Statutes* 2009, 216B.62, Subd. 2.

⁶ *Minnesota Statutes* 2009, 216B.62, Subd. 3, requires the commission to estimate the indirect assessments for each quarter and bill utility companies 30 days prior to the start of each quarter. The assessment for the third quarter of each fiscal year shall be adjusted to settle for differences between estimated and actual expenditures for the preceding fiscal year.

over/under allocated between the utility companies by the amounts shown in Table 2. Although in total the commission collected the correct amount, staff did not review the calculation to ensure it was accurate and compliant with statutory requirements.

Table 2
Over/Under Billing by Utility Type
Fiscal Year 2009

<u>Utility Company Type</u>	<u>Over (Under) Billed</u>
Telephone	\$ 218,870
Gas	\$ 75,250
Electric	\$(294,120)

Source: Auditor calculation from Public Utility Commission's records.

Recommendation

- *The commission should have an independent employee review overhead rate calculations and settlements to ensure amounts are accurately assessed to utility companies.*

Finding 4

The Public Utilities Commission did not sufficiently coordinate and control the Telephone Assistance Plan surcharge revenues and grant expenditures.

The commission did not have sufficient controls to ensure that it collected all Telephone Assistance Plan surcharge revenues and that it accurately paid grant assistance based on reports filed by telephone companies. As authorized by statutes, the commission administers the Minnesota Telephone Assistance Plan.⁷ This plan uses surcharges charged to all state landline users to provide grants for telephone service to low-income individuals. The commission uses the Department of Public Safety to collect the surcharges from telephone companies and the commission directly disburses grants back to those companies for qualified discounts to eligible individuals. The telephone companies report monthly to the commission the surcharges remitted and requested reimbursement for grants they provided.

The commission had the following control weaknesses in the Telephone Assistance Plan:

- The commission did not monitor whether all telephone companies submitted the reports or if the commission's staff reviewed the reports. Three companies that submitted surcharge revenue did not file reports, and

⁷ Minnesota Statutes 2009, 237.70 and Minnesota Rules 7817.0300.

commission staff did not have evidence to support its review of two companies' reports.

- The commission did not compare surcharge revenues reported by the service providers on their reports to the deposited amounts recorded in the state's accounting system by the Department of Public Safety.⁸ The commission accepted the Department of Public Safety's deposit and the telephone companies' reports as accurate without determining whether they agreed.
- The commission did not independently review grants paid to telephone companies for assistance discounts the companies provided to eligible participants. Without a review, payment errors could occur. For the 15 grant payments we tested, the commission had the following errors:
 - The commission did not pay one company its \$77 grant for December 2008 and did not pay another company its \$1,500 grant for October 2006 until December 2007.
 - The commission inappropriately paid a \$292 grant to the wrong company instead of the \$1,160 grant that company was owed. The commission did not pay any grant to the company owed the \$292 grant.
 - The commission incorrectly paid a grant to one company for \$1,575 instead of \$15.75 requested by the company. The company identified the error and repaid the difference to the commission.

Recommendation

- *The commission should improve control over financial activities of the Telephone Assistance Plan by:*
 - *Ensuring that telephone companies file required reports with the commission.*
 - *Comparing deposits made by the Department of Public Safety to surcharge revenue amounts reported by the telephone companies.*
 - *Having an independent review of grant payments to ensure that it accurately pays telephone companies.*

⁸ The Department of Public Safety collected revenue from telephone companies for 911 services, Telephone Assistance Plan surcharges that it submits to the Public Utilities Commission, and Telecommunications Access Minnesota Program surcharges that it submits to the Department of Commerce.

Finding 5

The Public Utilities Commission did not document management authorization for employee pay increases and achievement awards and did not complete written performance evaluations of staff.

The commission did not have documentation to show that the executive director or other managers had authorized important personnel decisions, including pay increases, achievement awards, and employee performance evaluations. The commission had the following weaknesses:

- The commission's human resources officer processed annual salary increases based on her monitoring of employee anniversary dates. In a few instances, the human resources officer processed pay increases that were later contested by the employees' supervisors; the human resources officer reversed the pay increases and recovered the additional compensation from the employees. In addition, the commission did not have someone independently validate the accuracy of the pay increases effective date.
- The commission did not document management authorization for 1 of 3 achievement awards tested. One employee inappropriately received two achievement awards in the same year; the bargaining agreement only allows for one achievement award per year. The employee repaid the commission for the \$1,600 inappropriate award. If the employee's personnel file had contained documentation of the initial achievement award, the inappropriate second award may not have occurred.
- The commission did not have evidence that it completed annual employee performance evaluations for 17 of 27 employees tested, as required in *Minnesota Statutes* and the respective state personnel plans (managerial and commissioners plans) or bargaining unit contracts.⁹ Commission staff stated that they did periodically meet with employees to verbally discuss their performance. Annual written performance reviews provide employees with important feedback on the quality of their work and serve as a basis for pay increases or performance awards and any possible disciplinary actions.

Without written authorization supporting compensation decisions, human resources personnel could make unauthorized or erroneous pay increases or achievement awards. Evidence of management's authorization is a fundamental internal control. An independent verification of transactions processed to the authorization of those transactions provides further assurance that staff accurately entered the transactions in the personnel/payroll system.

⁹ *Minnesota Statutes* 2009, 43A.20, requires annual performance evaluations for employees of the executive branch.

Recommendation

- *The commission should improve internal controls over compensation decisions by:*
 - *Documenting management authorization and effective date of pay rate increases, along with an independent review of the calculation and entry of any retroactive payments.*
 - *Documenting management authorization of achievement awards based on employee performance.*
 - *Providing all employees with a written, annual performance evaluation.*

The Public Utilities Commission did not have a written agreement with the Department of Commerce for some shared staff and computer system costs.**Finding 6**

The Public Utilities Commission did not have a written agreement with the Department of Commerce for certain functions the department performed for the commission. The commission relied on the Department of Commerce's staff and computer systems to determine, bill, and collect assessments to energy and telecommunications companies. Although the understanding between the commission and the department generally had not included cost reimbursements, during fiscal year 2009, the commission paid the Department of Commerce over \$500,000 for part of the cost of a new computer system. *Minnesota Statutes* provide authority for the commission to enter into a cooperative agreement for the sharing of costs with the department.¹⁰ State policy provides further guidance for interagency agreements that define the services provided, duration of the agreement, financial obligations, and responsibilities of each agency.¹¹ Without an authorized written agreement, disputes about responsibilities or cost could arise.

Recommendation

- *The commission should develop a written interagency agreement with the Department of Commerce to clarify responsibilities and financial obligations between the agencies.*

¹⁰ *Minnesota Statutes 2009, 216A.095.*

¹¹ Department of Management and Budget Policy 0705-05.

Finding 7

The Public Utilities Commission did not comply with certain statutory requirements for professional/technical services contracts.

The commission did not properly monitor, evaluate, or pay certain professional/technical services contracts. Contracts for professional/technical services generally are for services that are intellectual in nature and result in the production of a report or completion of a task. The commission did not always follow statutory¹² or state policy¹³ contract requirements. The commission had the following weaknesses in five of eight professional/technical service contracts that we tested, ranging in value from \$4,820 to \$93,000:

- The commission allowed the Office of Enterprise Technology to provide services three months before it executed an amendment to an interagency agreement, and it allowed the office to continue to provide services for a month after the amendment's expiration. In addition, the commission paid the interagency agreement on a different schedule than the payment terms stated in the agreement. As a result, at one point in the project, the commission had paid the office about \$11,000 in advance of the services provided.
- The commission paid a contractor \$13,158 for services provided after the contract expired in August 2007. Although the contractor provided services to earn those payments, the commission was not monitoring the contract to ensure that it either limited the work to the contract amount or amended the contract for additional work needed.
- For three contracts we tested, the commission did not retain a percentage of the contract amount and did not complete the required final payment approval form. *Minnesota Statutes* requires state agencies to retain ten percent of the contract amount until the head of the agency certifies that the contractor has satisfactorily fulfilled the terms of the contract.¹⁴ State contract policy includes a final payment form for state agencies to make the required certification.¹⁵
- The commission did not complete the required performance evaluation report for a \$93,000 contract. *Minnesota Statutes* require that an evaluation be submitted to the Department of Administration when a contract exceeds \$50,000.¹⁶

¹² *Minnesota Statutes* 2009, 16C.08.

¹³ Department of Administration's Professional/Technical Services Contract Manual.

¹⁴ *Minnesota Statutes* 2009, 16C.08, Subd. 5(b).

¹⁵ Department of Administration's Professional/Technical Services Contract Manual, Section 19.

¹⁶ *Minnesota Statutes* 2009, 16C.08, Subd. 4 (c).

Recommendation

- *The commission should comply with professional/technical service contract requirements established by statute and the Department of Administration.*

The Public Utilities Commission did not receive approval from the Department of Administration for an agreement providing public transportation subsidies to its employees.

Finding 8

The commission did not obtain approval from the Department of Administration before it entered into an agreement with Metro Transit to buy 15 bus passes for its employees at about \$76 each per month. The commission subsidized about \$53 of the monthly cost for each bus pass and employees paid about \$23 each per month. In total, from July 2007 through February 2010, the commission paid about \$30,000 for the bus passes; the commission subsidized about \$18,000 and employees reimbursed the commission about \$12,000. *Minnesota Statutes* require that the commissioner of the Department of Administration approve agreements with Metro Transit before execution.¹⁷

Recommendation

- *The commission should obtain Department of Administration's contract approval for agreements with Metro Transit subsidies provided to employees.*

The commission lacked appropriate support for some transactions and did not accurately record certain expenditure transactions in the state's accounting system.

Finding 9

The commission did not accurately code transactions, encumber funds, obtain special expense approval, and document receipt of goods to support expenditures in the state's accounting system. A supervisory review of transactions could prevent or detect these coding and documentation errors prior to payment to the vendor. The commission had the following deficiencies for transactions we tested:

- The commission miscoded more than half of the transactions it recorded as supply purchases, totaling about \$182,000. The commission should have coded these transactions as equipment, cell phone service, conference or registration fees, or other miscellaneous nonsupply purchases. In addition, the commission incorrectly identified in the

¹⁷ *Minnesota Statutes* 2009, 473.409.

accounting system 4 of 16 miscellaneous purchase transactions, 2 of 6 equipment items, and 1 of 5 contract service transactions we tested. State policy requires agencies to accurately identify expense transactions in the accounting system to facilitate budget monitoring and accurate financial reporting.¹⁸

- The commission did not encumber funds in advance for 4 of 16 purchases and 1 of 9 leases we tested. *Minnesota Statutes*¹⁹ and state policies²⁰ require that agencies encumber funds before incurring an obligation to ensure that sufficient funds will be available when payment is due.
- The commission did not complete the required special expense form and did not obtain management authorization for 4 of 5 special expense transactions we tested. Special expenses are for items not typically allowable, such as providing food for employees who were not in travel status. To ensure that these types of expenses are reasonable and necessary, state policy requires that all special expenses have advance, documented management approval.²¹ Commission staff were unaware that the items were special expenses and had not documented management's approval.
- The commission did not always record the correct liability date for purchases of goods, services, and grant expenditures. The commission did not assign the correct liability date for 31 of 60 expenditure transactions that we tested. State policy requires agencies to use the record date to identify the date that the state became liable for the expenditure, which is usually when the agency received the goods or services were rendered.²²
- The commission did not always have evidence that it had received supply or equipment purchases. The commission was missing a packing slip for a supply purchase (1 of 6 tested) and did not always have staff acknowledge the accuracy of the shipment supplies (3 of 6 supply purchases tested and 1 of 6 equipment purchases tested). State policy²³ requires agencies to verify shipments to ensure accurate payment for the quantity actually received.
- The commission did not always stamp the date invoices were received for 10 of 35 transactions that we tested. The invoice's date of receipt provides the accounting staff with the date for measurement of prompt payment.

¹⁸ Department of Management and Budget Policy 0702-01.

¹⁹ Minnesota Statutes 2009, 16A.15.

²⁰ Department of Management and Budget Policy 0702-01.

²¹ Department of Management and Budget Policy 0809-07.

²² Department of Management and Budget Policy 0901-01.

²³ Department of Management and Budget Policy 0803-05.

Minnesota Statutes allow vendors to bill the state for interest on payments made later than 30 days after when a state agency received the invoice.²⁴

Recommendation

- *The commission should improve controls over expenditure processing by:*
 - *Coding transactions to properly identify the type of expense.*
 - *Encumbering funds before incurring the liability.*
 - *Completing and authorizing special expense forms.*
 - *Recording an accurate liability date for purchases.*
 - *Retaining shipping evidence and verifying quantity shipped.*
 - *Stamping the date received on the invoice to ensure prompt payment.*

Commission supervisors did not review and approve state purchase card purchases and the commission's purchase card coordinator did not review key on-line credit card reports.

Finding 10

The commission did not require employees to submit to their supervisors support for purchase card transactions to ensure that the purchases complied with state policy and were reasonable and necessary for the conduct of the commission's duties. Instead, employees submitted monthly credit card statements and receipts for purchases directly to the accounts payable staff for payment processing. From July 2007 through February 2010, commission staff purchased items totaling nearly \$138,500 using purchase cards. The state's purchase card policy requires that an employee's supervisor must review the purchase card statement and documentation supporting the purchases.²⁵ The policy also provides a purchase card log that state agencies can use to provide an itemization of what was purchased, the date of purchase, the business reason for the purchase, and the employee's signature verifying the information is accurate. The commission does not require its employees to use this form.

The commission's purchase card coordinator also did not access and review online reports available from the state's bank that processes the purchases. State policy indicates that agency purchasing card coordinators may manage their purchasing card accounts on the bank's website, which allows them to produce a variety of reports.²⁶ Analysis of the information available directly from the bank would allow the commission to monitor employee use of the cards, the

²⁴ Minnesota Statutes 2009, 16A.124.

²⁵ Department of Administration Purchasing Card Use Policy 2.0, paragraph 2.84.

²⁶ Department of Administration Purchasing Card Use Policy 2.0, paragraph 2.92.

appropriateness of card limits, and occasions when the credit card company rejected an attempted purchase.

Recommendation

- *The commission should improve its monitoring of employee purchasing cards by requiring supervisory review and approval and purchase card coordinator review of online reports.*

Finding 11

The commission did not have effective controls over equipment and sensitive assets.

The commission did not comply with state guidelines²⁷ to safeguard its fixed assets from loss or theft.²⁸ The commission had the following weaknesses in oversight of fixed assets:

- The commission did not have a policy to define its unique sensitive assets and establish asset tracking procedures, staff responsibilities for maintaining inventory, and physical inventory practices, as required by state guidelines.²⁹ Although the state has general guidelines for fixed asset inventory processes, the guidelines require each agency to develop specific policies to meet its unique inventory needs. For example, the state guidelines list computer equipment as sensitive assets for all state agencies, but leaves it to the agency's discretion to identify other items, such as cameras.
- Commission equipment records did not contain all information required by state guidelines, and it maintained separate lists of different types of sensitive items. The sensitive asset lists identified the asset serial number and the employee it was assigned to, but did not specify the asset number, description of asset, purchase order number, acquisition date, cost, and the date of disposal. Without this specific information, it is difficult to identify each individual asset during a physical inventory.
- The commissions failed to conduct a full physical inventory of its fixed assets and sensitive assets in accordance with state policy. Those guidelines require that a complete physical inventory be conducted at least

²⁷ Department of Administration User's Guide to Property Management, Sections 2 and 5.

²⁸ Fixed assets include capital assets and sensitive items. Capital assets include property that costs \$5,000 or more, has a normal useful life expectancy exceeding two years, and maintains its identity while in use. Sensitive items are generally for individual use and are often subject to theft or misuse, such as computers and laptops, cell phones, cameras, portable projectors, and other electronic devices.

²⁹ Department of Administration User's Guide to Property Management, Section 13.

biennially. By not periodically conducting a physical inventory, the commission is not assured that inventoried assets exist and are not missing or stolen.

Recommendation

- *The commission should improve internal control over its equipment and sensitive assets by:*
 - *Developing an agency policy and assigning staff responsibilities for managing assets inventory and performing periodic verification.*
 - *Tracking the required asset information in an established equipment and sensitive asset inventory record.*
 - *Performing periodic physical inventories.*

The Public Utilities Commission did not verify that it had accurately processed reimbursements to employees for travel and other expenses.

Finding 12

The commission did not sufficiently review a payroll report to ensure that it had accurately entered employee expense reimbursement claims. Although staff did review the report to ensure the accuracy of payroll transactions, they did not verify that reimbursement transactions agreed to the supporting employee expense reimbursement claim form. State policy requires agencies to independently verify the accuracy and coding of employee reimbursement each pay period.³⁰ The absence of a control increases the risk that errors or overpayments to employees could occur without detection. For example, commission staff miscoded some taxable meals as nontaxable mileage.

Recommendation

- *The commission should provide for an independent review of the accuracy of employee travel reimbursements entered into the payroll system.*

³⁰ Department of Management and Budget Policy PAY0021.



STATE OF MINNESOTA PUBLIC UTILITIES COMMISSION

June 10, 2010

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

Re: Legislative Audit Report for July 1, 2007 through February 28, 2010

Dear Mr. Nobles:

Thank you for the opportunity to respond to the internal control and compliance audit of the Public Utilities Commission (PUC) for the period July 1, 2007, through February 28, 2010. The Commission agrees with the overall conclusion of the audit report that ... "The Public Utilities Commission generally had adequate internal controls to ensure it safeguarded its assets, accurately paid employees and vendors in accordance with management's authorization, complied with finance-related legal requirements, and produced reliable financial data." We also acknowledge the internal control and compliance weaknesses identified in the report. This letter represents our response to the findings in the draft report.

Finding: The Public Utilities Commission did not identify, analyze and document internal controls related to its business operations.

We agree with the report recommendations. The PUC does have internal controls in many areas identified in the report that, to date, have not been adequately documented. The Commission will coordinate with MMB's internal audit program to document existing controls and complete a comprehensive self assessment of the control environment and an agency risk assessment by the first quarter of 2011. PUC staff will be informed of the content and requirements related to established internal controls.

Persons Responsible: Burl Haar, Marsha Battles-Jenks

Finding: The PUC provided an employee with incompatible access to the state's accounting system without defined mitigating controls and other staff with excessive access to update the commission's assessment system.

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We agree with the report recommendations. Given limited staff resources, it will not be possible to eliminate incompatible access to the state's accounting system. PUC has implemented review controls over most agency transactions. However, we recognize the need to document and enhance existing control procedures. We have already implemented enhanced controls over accounting transactions and will complete documentation by September 30, 2010. In addition, PUC limited staff access to the utility assessment system during the audit.

Persons Responsible: Marsha Battles-Jenks, Burl Haar

Finding: The Public Utilities Commission made some errors in amounts assessed to utility companies.

We agree with the report recommendation. The Commission has invested substantial resources in a new data system to ensure accurate billings. While the overall assessed dollar amount noted in the report was correct, the assessments were misallocated due to a clerical error. The PUC will identify staff to perform independent reviews of the assessment rates prior to the next billing cycle, at which time any errors made will be corrected. Procedures will be documented by September 30, 2010.

Persons Responsible: Battles-Jenks, Burl Haar

Finding: The Public Utilities Commission did not sufficiently coordinate and control the Telephone Assistance Plan (TAP) surcharge revenues and grant expenditures.

We agree with the report recommendations. The PUC recently implemented a new data system to better manage TAP revenues and expenditures, which should address some of the issues raised in the report. Additional procedures will need to be designed, documented and implemented to verify deposits made by the Department of Public Safety against surcharge revenue amounts reported by telephone companies and to ensure independent review of TAP grant payments. Procedures will be documented and in place by October 15, 2010.

Persons Responsible: Burl Haar, Debra Motz

Finding: The PUC did not document management authorization for employee pay increases and achievement awards and did not complete written performance evaluations of staff.

We agree with the report recommendations. PUC will ensure that supervisory staff is aware of the requirement for annual written performance reviews of their staff. PUC will document and distribute a policy requiring a written annual review prior to processing any salary increases. PUC will also formalize its requirement for written justifications (nomination memo) for Achievement Awards. Procedures

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will be documented and in place by August 31, 2010.

Persons Responsible: Marsha Battles-Jenks, Burl Haar

Finding: The PUC did not have a written agreement with the Department of Commerce (DOC) for some shared staff and computer system costs.

We agree with the report recommendation. The PUC and the DOC work closely together in a variety of areas related to utility regulation. Documenting the nature and cost of that relationship will assist both agencies in achieving their respective regulatory missions. An inter-agency agreement will be completed by December 31, 2010.

Person Responsible: Burl Haar

Finding: The PUC did not comply with certain statutory requirements for professional/technical services contracts.

We agree with the report recommendation. PUC will designate a contract administrator to ensure that all professional/technical service contract requirements are met. Accounting staff has received instructions on establishing vendor expenses in the accounting system to ensure proper withholding of payments until successful completion of each contract phase is verified. Procedures should be documented and in place by September 30, 2010.

Person Responsible: Marsha Battles-Jenks

Finding: The PUC did not receive approval from the Department of Administration for an agreement providing public transportation subsidies to its employees.

We agree with the report recommendation. PUC staff has forwarded a copy of the current agreement to the Department of Administration and indicated that we will be entering into a new agreement in August of 2010. The contract will be forwarded to them for approval prior to signing a new agreement with Metro Transit. Procedures will be documented and a new contract approved by August 31, 2010.

Person Responsible: Marsha Battles-Jenks

Finding: The PUC lacked appropriate support for some transactions and did not accurately record certain expenditure transactions in the state's accounting system.

We agree with the report recommendation. Procedures have been established to ensure proper

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transaction coding, timely encumbrances, verification of receipt of goods and date stamping of invoices received. Procedures for expenditure processing controls will be documented by July 15, 2010.

Person Responsible: Marsha Battles-Jenks

Finding: Commission supervisors did not review and approve state purchase card purchases and the commission's purchase card coordinator did not review key on-line credit card reports.

We agree with the report recommendation. PUC will publish and distribute a policy requiring supervisor review and approval of employee purchasing card transactions prior to submission to accounts payable staff. The credit card coordinator will work with management to develop a procedure for the timing and frequency of running reports from the on-line credit card data system. Procedures will be documented by September 30, 2010.

Person Responsible: Marsha Battles-Jenks, Burl Haar

Finding: The Commission did not have effective controls over equipment and sensitive assets

We agree with the report recommendation. The PUC has various tracking lists for sensitive equipment, which should be consolidated and provide more information on each asset. Policies and procedures will be established for managing asset inventories, tracking required asset information, and for performing physical inventories by April, 2011.

Person Responsible: Marsha Battles-Jenks

Finding: The PUC did not verify that it had accurately processed reimbursements to employees for travel and other expenses. A procedure will be developed and documented to verify the accuracy and coding of employee reimbursement each pay period by July 1, 2010.

Person Responsible: Marsha Battles-Jenks

Again, thank you for the opportunity to respond to the draft report. If you have any questions, please contact Marsha Battles-Jenks at 651-201-2219.

Sincerely,



Burl Haar

Executive Secretary