



FINANCIAL AUDIT DIVISION REPORT

Department of Commerce
Federal Compliance Audit
Fiscal Year 2010

April 22, 2011

Report 11-10

FINANCIAL AUDIT DIVISION

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OFFICE OF THE LEGISLATIVE AUDITOR

State of Minnesota • James Nobles, Legislative Auditor

April 22, 2011

Representative Michael Beard, Chair
Legislative Audit Commission

Members of the Legislative Audit Commission

Mr. Michael Rothman, Commissioner
Department of Commerce

This report presents the results of our audit of certain federal financial assistance programs administered by the Department of Commerce during fiscal year 2010. 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 Commerce.

We discussed the results of the audit with department staff at an exit conference on April 12, 2011. The audit was conducted by Brad White, CPA, CISA, CFE, (Audit Manager) and Kayla Borneman, CPA, (Auditor-in-Charge), assisted by auditors Lindsay Tietze, CPA and Kelsey Nistler.

This report is intended for the information and use of the Legislative Audit Commission and the management of the Department of Commerce. This restriction is not intended to limit the distribution of this report, which was released as a public document on April 22, 2011.

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

Handwritten signature of James R. Nobles in black ink.

James R. Nobles
Legislative Auditor

Handwritten signature of Cecile M. Ferkul in black ink.

Cecile M. Ferkul, CPA, CISA
Deputy Legislative Auditor

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Report Summary

Conclusion

The Department of Commerce generally complied with and had controls to ensure compliance with provisions of laws, regulations, contracts, and grants applicable to the major federal programs we audited for fiscal year 2010. However, the department had control weaknesses and noncompliance with federal requirements, as noted in the four findings presented in this report.

Findings

- The Department of Commerce did not adequately perform certain monitoring procedures designed to ensure that local service providers complied with federal requirements of the Weatherization Assistance for Low-Income Persons Program. ([Finding 1, page 5](#))
- The Department of Commerce overcharged \$117,324 of agency indirect costs to federal programs for the fourth quarter ending June 30, 2010. ([Finding 2, page 6](#))
- The Department of Commerce has not yet recovered disallowed expenditures totaling \$426,523 for the Weatherization Assistance for Low-Income Persons Program reimbursed to a local service provider that it suspended. ([Finding 3, page 7](#))
- The Department of Commerce did not adequately track equipment inventory purchased by local service providers with funds from the federal Weatherization Assistance for Low-Income Persons Program. ([Finding 4, page 8](#))

Audit Scope

Our scope included the Low-Income Home Energy Assistance Program and the Weatherization Assistance for Low-Income Persons Program, which were major federal programs for the State of Minnesota for fiscal year 2010.

Department of Commerce

Federal Program Overview

The Department of Commerce administered two federal programs that we considered major federal programs for the State of Minnesota, subject to audit under the federal Single Audit Act.¹ Table 1 identifies these major federal programs.

Table 1
Major Federal Programs
Department of Commerce
Fiscal Year 2010
(in thousands)

CFDA¹	Program Name	Federal Expenditures	Federal ARRA² Expenditures	Total
81.042	Weatherization Assistance for Low-Income Persons	\$ 11,058	\$46,818	\$ 57,876
93.568	Low-Income Home Energy Assistance	\$170,387	\$ 0	\$170,387

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

² American Recovery and Reinvestment Act.

Source: Minnesota Accounting and Procurement System for fiscal year 2010.

Objective, Scope, and Methodology

The objective of our audit was to determine whether the Department of Commerce complied with federal program requirements in its administration of these federal programs for fiscal year 2010. 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.² In addition to specific program requirements, we examined the department's general compliance requirements related to federal assistance, including its cash management practices.

¹ 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 2010 exceeded \$30 million.

² The State of Minnesota's single audit includes both the financial statements and the expenditures of federal awards by all state agencies. We issued an unqualified audit opinion, dated December 20, 2010, on the State of Minnesota's basic financial statements for the year ended June 30, 2010. 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 11-02, *Report on Internal Control Over Financial Reporting*, issued February 18, 2011.)

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 Commerce 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 2010. However, the department had some weaknesses, as noted in the following *Findings and Recommendations* section.

We will report these weaknesses to the federal government in the *Minnesota Financial and Compliance Report of Federally Assisted Programs*, prepared by the 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.

Findings and Recommendations

Finding 1

The Department of Commerce did not adequately perform certain monitoring procedures designed to ensure that local service providers complied with federal requirements of the Weatherization Assistance for Low-Income Persons Program.

The Department of Commerce did not adequately monitor service providers³ for compliance with certain federal requirements applicable to the Weatherization Assistance for Low-Income Persons Program (CFDA #81.042⁴ and #81.042 ARRA⁵). Local service providers distribute the program's financial assistance to eligible low-income households to improve the energy efficiency of their homes. The department developed a system to monitor local service provider compliance with federal requirements; however, it had the following weaknesses in its monitoring practices:

- Cost Savings Requirement – The department did not adequately monitor local service providers to ensure compliance with the cost savings requirement contained in federal regulations and in the state plan approved by the federal government. Federal regulations require that funds used for weatherization improvements result in energy cost savings over the lifetime of the improvement that is equal to or greater than the cost of materials and installation. The state plan states that the department will monitor the cost savings by comparing the cost of the improvement to the estimated energy savings. If the savings do not exceed the costs, the planned improvements are not an effective use of weatherization assistance funds. For fiscal year 2010, the department may have inappropriately reimbursed as much as \$141,802 to local service providers for improvements of 74 dwellings (out of 8,554 dwellings improved) where the energy savings did not exceed the cost of the improvement.
- Service Provider Monitoring – The department did not always comply with state plan requirements to monitor service providers by performing field visits and fiscal reviews. Field visits involve monitoring and inspecting the project to ensure that work was appropriate, the monitoring tool was updated, and any corrective actions were addressed. Of the 22 service provider field visits completed by the department, 5 did not have a completed monitoring tool on file, 8 did not have a written report completed in 30 days, and 10 did not show that concerns raised in the reviews were tracked by the department to ensure resolution. In addition, the department did not complete a second fiscal

³ Service providers are agencies that serve Weatherization Assistance clients at the local level including community action programs, tribal boards, and nonprofit organizations. Currently, the department has 32 service providers geographically dispersed around the state of Minnesota.

⁴ Federal Grant Award #DE-EE0000653.

⁵ Federal Grant Award #DE-EE0000103.

review for any service providers for fiscal year 2010; the state plan calls for two fiscal reviews. Fiscal reviews address the service provider's tracking and documentation of project expenditures and are important to provide department management with assurance that service providers are appropriately spending weatherization grant awards.

- Prevailing Wage Requirements – Prior to December 31, 2009, the department did not adequately ensure that local service providers paid workers providing weatherization services the prevailing wage, as required by the Davis-Bacon Act.⁶ The department required the service providers to submit payroll information to demonstrate compliance with Davis Bacon requirements. However, 4 of 13 providers we tested did not submit the required certified weekly payroll during early periods of fiscal year 2010. As a result, the department could not verify compliance.

Recommendations

- *The department should obtain written direction from appropriate federal officials on how to resolve the federal funds used for weatherization improvements that did not achieve an energy savings.*
- *The department should improve monitoring of local service providers to ensure compliance with federal Davis Bacon requirements and provider monitoring required in its state plan for the Weatherization Assistance for Low-Income Persons Program.*

Finding 2

The Department of Commerce overcharged \$117,324 of agency indirect costs to federal programs for the fourth quarter ending June 30, 2010.

The department did not use the correct indirect cost rate for the fourth quarter of state fiscal year 2010 when charging agency indirect costs to the federal programs it administers. The department's federally approved indirect cost rate was 11.3 percent for fiscal year 2010; however, the department mistakenly used the 14 percent indirect cost rate approved for fiscal year 2011.

The indirect cost rate proposal is created annually and submitted to the Division of Cost Allocation of the U.S. Department of Health and Human Services. The U.S. Department of Health and Human Services reviews and approves the

⁶ The federal Davis-Bacon Act requires contractors and subcontractors receiving federal grants to pay their laborers and mechanics employed under the contract no less than the locally prevailing wages and fringe benefits for corresponding work on similar projects in the area.

proposed rate and an agreement is signed with the state Department of Commerce.

The use of the incorrect indirect cost rate resulted in the department overcharging federal programs \$117,324, as shown in Table 2.

Table 2
Summary of Indirect Cost Overcharges by Federal Program
Fiscal Year 2010

<u>CFDA</u> ¹	<u>Program Name</u>	<u>Amounts</u>
Major Programs:		
81.042	Weatherization Assistance for Low-Income Persons ²	\$ 4,718
81.042	ARRA – Weatherization Assistance for Low-Income Persons ³	<u>\$ 27,712</u>
	Total Weatherization Assistance	<u>\$ 32,430</u>
93.568	Low-Income Home Energy Assistance ⁴	\$ 51,319
Non-Major Programs:		
81.041	State Energy Program ⁵	\$ 9,912
81.041	ARRA – State Energy Program ⁶	<u>\$ 19,983</u>
	Total State Energy Program	<u>\$ 29,895</u>
N/A	Other Non-Major Federal Programs	<u>\$ 3,680</u>
	Total	<u>\$117,324</u>

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

² Federal Grant Award #DE-EE0000653.

³ Federal Grant Award #DE-EE0000103.

⁴ Federal Grant Award #G-09B1MNLIEA and #G-10B1MNLIEA.

⁵ Federal Grant Award #DE-FG26-07NT43166.

⁶ Federal Grant Award #DE-EE0000164.

Source: Auditor created from the Department of Commerce's accounting records for fiscal year 2010.

Recommendation

- *The department should correct the indirect cost overcharges of \$117,324 and improve internal controls to ensure that indirect costs are accurately charged to federal programs.*

The Department of Commerce has not yet recovered disallowed expenditures totaling \$426,523 for the Weatherization Assistance for Low-Income Persons Program reimbursed to a local service provider that it suspended.

Finding 3

In November 2009, the Department of Commerce suspended payments to a local service provider (Tri Valley Opportunity Council, Inc., located in Crookston, Minnesota) from the federal Weatherization Assistance for Low Income Persons

Program (CFDA #81.042⁷ and 81.042 ARRA⁸). Following the suspension, the department allowed the local service provider several opportunities to remedy the missing documentation and to justify the disallowed costs. However, on April 11, 2011, based on guidance it received from the federal Department of Energy and after investigating the provider's lack of accountability and widespread problems with missing documentation, the department notified the service provider that it was terminating the grant agreement. Before the suspension, the department had paid the local service provider \$432,279 for weatherization assistance costs. The department is seeking recovery of \$426,523 for the undocumented or unallowable costs.

Recommendation

- *The department should seek recovery of the \$426,523 of weatherization assistance expenditures that did not comply with the federal program requirements.*

Finding 4

The Department of Commerce did not adequately track equipment inventory purchased by local service providers with funds from the federal Weatherization Assistance for Low-Income Persons Program.

The department did not update its equipment records with specific information for vehicles and other weatherization equipment purchased by local service providers with funds from the federal Weatherization Assistance for Low-Income Persons Program (CFDA #81.042⁹ and 81.042 ARRA¹⁰) for fiscal year 2010. When the federal government approved the purchase of program vehicles or equipment, the department identified the service provider and type of equipment on its inventory system; however, the department did not update inventory records with the actual date of purchase, vehicle identification numbers or equipment serial numbers, and the final purchase price as called for in federal regulations.¹¹ Without this key information, the department is unable to identify and track the specific equipment items purchased with federal funding and cannot periodically verify that the local service provider is still in possession of the specific weatherization equipment.

Recommendation

- *The department should improve controls to ensure that it updates its equipment inventory records with specific identification of weatherization vehicles and equipment acquired with federal program funds.*

⁷ Federal Grant Award #DE-EE0000653.

⁸ Federal Grant Award #DE-EE0000103.

⁹ Federal Grant Award #DE-EE0000653.

¹⁰ Federal Grant Award #DE-EE0000103.

¹¹ 10 CFR 600.232 (2010).



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April 18, 2011

James R. Nobles
Legislative Auditor
Office of the Legislative Auditor
Centennial Office Building, Room 140
658 Cedar Street
St. Paul, MN 55155-1603

Dear Mr. Nobles:

I would like to thank the Office of the Legislative Auditor and your financial audit team for their work reviewing the Minnesota Department of Commerce's administration in fiscal year 2010 of the Low Income Home Energy Assistance Program and the Weatherization Assistance for Low-Income Persons Program. Your team provided a professional review of the Department's general compliance requirements related to federal assistance, including the Department's cash management practices and provided valuable recommendations based on that review. I welcome the opportunity to take positive action on those recommendations. We agree with the overall findings of the audit.

In my role as a new Commissioner at the Commerce Department, I am committed to effective internal controls. This audit will assist the Department's efforts to strengthen its program and financial management.

Specific responses to the audit findings follow.

Finding 1: The Department of Commerce did not adequately perform certain monitoring procedures designed to ensure that local service providers complied with federal requirements of the Weatherization Assistance for Low-Income Persons Program.

Recommendations:

- The department should obtain written direction from appropriate federal officials on how to resolve the federal funds used for weatherization improvements that did not achieve an energy savings.*

- *The department should improve monitoring of local service providers to ensure compliance with federal Davis Bacon requirements and provider monitoring required in its state plan for the Weatherization Assistance for Low-Income Persons Program.*

Response: The Department agrees with the finding and will work with U.S. Department of Energy staff to resolve ambiguities in the Weatherization Assistance Program state plan regarding how and when the decision is made to install energy measures. Processes have been improved to ensure that monitoring is conducted in accordance with federal requirements. Stronger systems are now in place to ensure compliance with the federal Davis Bacon requirements. Commerce's State Energy Office manager (Janet Streff) and Weatherization Assistance Program supervisor (Marilou Cheple) will be primarily responsible for these efforts. These efforts will be completed by June 30, 2011.

Finding 2: The Department of Commerce overcharged \$117,324 of agency indirect costs to federal programs for the fourth quarter ending June 30, 2010.

Recommendations:

- *The department should correct the indirect cost overcharges of \$117,324 and improve internal controls to ensure that indirect costs are accurately charged to federal programs.*

Response: The Department agrees. The Department concurs with this finding and has corrected the overcharge. Indirect cost charges will now be reviewed by the accounting director prior to processing. Commerce's Financial Management Director (Tim Jahnke) has already corrected the overcharge.

Finding 3: The Department of Commerce has not yet recovered disallowed expenditures totaling \$426,523 for the Weatherization Assistance for Low-Income Persons Program reimbursed to a local service provider that it suspended.

Recommendations:

- *The department should seek recovery of the \$426,523 of weatherization assistance expenditures that did not comply with the federal program requirements.*

James R. Nobles
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Response: The Department concurs and is implementing the steps necessary to recover the funds. Commerce's State Energy Office manager (Janet Streff) will be primarily responsible for this effort. The expected time frame to recover funds is by approximately September 30, 2011.

Finding 4: The Department of Commerce did not adequately track equipment inventory purchased by local service providers with funds from the federal Weatherization Assistance for Low-Income Persons Program.

Recommendations:

- The department should improve controls to ensure that it updates its equipment inventory records with specific identification of weatherization vehicles and equipment acquired with federal program funds.*

Response: The Department agrees with this finding. Commerce's Weatherization Assistance Program supervisor (Marilou Cheple) has already improved controls to ensure that its equipment inventory records are updated on a regular basis so that vehicles and equipment acquired with federal program funds are tracked appropriately.

I appreciate the work of your agency to identify areas within Commerce that need improvement. We are committed to taking appropriate action to further strengthen our program.

Sincerely,



Mike Rothman
Commissioner