



FINANCIAL AUDIT DIVISION REPORT

**Legacy Funds: Outdoor Heritage,
Clean Water, and Parks and Trails**

Internal Controls and Legal Compliance Audit

July 1, 2009, through January 31, 2011

November 30, 2011

Report 11-27

FINANCIAL AUDIT DIVISION

Centennial Building – Suite 140

658 Cedar Street – Saint Paul, MN 55155

Telephone: 651-296-4708 • Fax: 651-296-4712

E-mail: auditor@state.mn.us • Web site: <http://www.auditor.leg.state.mn.us>

Through Minnesota Relay: 1-800-627-3529 or 7-1-1



OFFICE OF THE LEGISLATIVE AUDITOR

State of Minnesota • James Nobles, Legislative Auditor

November 30, 2011

Representative Michael Beard, Chair
Legislative Audit Commission

Members of the Legislative Audit Commission

Mr. Thomas Landwehr, Commissioner
Department of Natural Resources

Mr. Paul Aasen, Commissioner
Pollution Control Agency

Mr. John Jaschke, Executive Director
Board of Water and Soil Resources

This report presents the results of our selected scope internal controls and compliance audit of expenditures from three Legacy funds (Outdoor Heritage, Clean Water, and Parks and Trails) administered by the Department of Natural Resources, Pollution Control Agency, Board of Water and Soil Resources, and several nonstate organizations for the period July 1, 2009, through January 31, 2011.

We discussed the results of the audit with the staff at the respective state agencies and nonstate organizations in October and November 2011. This audit was conducted by Brad White, CPA, CISA, CFE (Audit Manager) and Scott Tjomsland, CPA, CISA (Auditor-in-Charge), assisted by Tyler Billig, CPA; Melanie Greufe, CPA, CFE; David Minch; Carissa Moritz; Kevin Schoenrock; Blake Schwagel; Lindsay Tietze, CPA; Emily Wiant; and Zach Yzermans, CPA.

This report is intended for the information and use of the Legislative Audit Commission and the management of the Department of Natural Resources, Pollution Control Agency, and Board of Water and Soil Resources. This restriction is not intended to limit the distribution of this report, which was released as a public document on November 30, 2011.

We received the full cooperation of staff from the state agencies and nonstate organizations while performing this audit.

James R. Nobles
Legislative Auditor

Cecile M. Ferkul, CPA, CISA
Deputy Legislative Auditor

Table of Contents

| | <u>Page</u> |
|--|-------------|
| Report Summary | 1 |
| Legacy Funds Overview | 3 |
| Scope, Objective, and Methodology | 4 |
| Conclusion | 7 |
| Findings and Recommendations | 9 |
| 1. The Department of Natural Resources, Pollution Control Agency, and Board of Water and Soil Resources did not ensure that certain costs paid with money appropriated from Legacy funds complied with the restricted uses of those funds | 9 |
| 2. The Pollution Control Agency and Board of Water and Soil Resources made unauthorized advances of Legacy money to grantees | 13 |
| 3. The Department of Natural Resources, Pollution Control Agency, and Board of Water and Soil Resources paid some grantees for costs without ensuring that the costs complied with the restrictions applicable to the uses of Legacy funds | 14 |
| 4. The Department of Natural Resources did not accurately pay some reimbursement requests for grants from the Outdoor Heritage Fund | 16 |
| 5. The Pollution Control Agency did not sufficiently monitor whether a grantee complied with statutory match requirements | 17 |
| 6. The Department of Natural Resources did not adequately safeguard state warrants held by employees for land acquisition closings | 18 |
| Appendix A – Selected Nonprofit and Local Government Organizations Receiving Legacy Grants | 19 |
| Agency Responses | 21 |
| Department of Natural Resources | 21 |
| Pollution Control Agency | 25 |
| Board of Water and Soil Resources | 29 |

Report Summary

Conclusion

The selected internal controls at the organizations we reviewed were generally adequate to ensure that the organizations used money appropriated from Legacy funds for the purposes authorized in the Legacy Amendment and applicable state laws; safeguarded financial resources; accurately paid employees, vendors, and grantees in accordance with managements' authorizations; complied with finance-related legal provisions; and created reliable financial data. For the items tested, the organizations generally complied with significant finance-related legal requirements.

However, the state agencies¹ we reviewed had some internal control weaknesses and instances of noncompliance, as discussed in the report's findings.

Key Findings

- The Department of Natural Resources, Pollution Control Agency, and Board of Water and Soil Resources did not ensure that certain costs paid with money appropriated from Legacy funds complied with the restricted uses of those funds. ([Finding 1, page 9](#))
- The Pollution Control Agency and Board of Water and Soil Resources made unauthorized advances of Legacy money to grantees. ([Finding 2, page 13](#))
- The Department of Natural Resources, Pollution Control Agency, and Board of Water and Soil Resources paid some grantees for costs without ensuring that the costs complied with the restrictions applicable to the uses of Legacy funds. ([Finding 3, page 14](#))

Audit Objectives and Scope

Objectives

- Internal Controls
- Legal Compliance

Period Audited

July 1, 2009, through January 31, 2011

Legacy Funds Included

- Outdoor Heritage Fund
- Clean Water Fund

- Parks and Trails Fund

Financial Areas Audited

- Payroll Expenditures
- Operating and Administrative Expenditures

- Land Acquisitions and Easements
- Grants

¹ The Department of Natural Resources, Pollution Control Agency, and Board of Water and Soil Resources.

Legacy Funds Overview

In 2008, Minnesota voters approved the Outdoor Heritage, Clean Water, Parks and Trails, and Arts and Cultural Heritage Amendment to the Minnesota Constitution, commonly called the “Legacy Amendment.” The amendment increased the state sales tax by three-eighths of 1 percent for a 25-year period beginning in July 2009 and distributed the taxes among four funds, which we collectively refer to as the Legacy funds. The Legacy Amendment outlines the share of the revenue each fund receives and its allowable uses as follows:²

- **Outdoor Heritage Fund:** This fund receives 33 percent of the dedicated sales tax revenue. Revenue must be used to restore, protect, and enhance wetlands, prairies, forests, and habitat for fish, game, and wildlife.
- **Clean Water Fund:** This fund receives 33 percent of the dedicated sales tax revenue. Revenue must be used to protect, enhance, and restore water quality in lakes, rivers, and streams and to protect groundwater from degradation. Five percent must be spent to protect drinking water sources.
- **Parks and Trails Fund:** This fund receives 14¼ percent of the dedicated sales tax revenue. Revenue must be used to support parks and trails of regional or statewide significance.
- **Arts and Cultural Heritage Fund:** This fund receives 19¾ percent of the dedicated sales tax revenue. Revenue must be used for arts, arts education, and arts access and to preserve Minnesota’s history and cultural heritage.³

The Lessard-Sams Outdoor Heritage Council recommends appropriations from the Outdoor Heritage Fund and provides oversight for projects supported by the fund. The Clean Water Council recommends appropriations from the Clean Water Fund, but unlike the Lessard-Sams Outdoor Heritage Council, the Clean Water Council is not significantly involved in oversight. Oversight for programs and projects supported with money from the Clean Water Fund, Parks and Trails Fund, and Outdoor Heritage Fund is provided by legislative committees and the state agencies that receive, spend, and grant Legacy money.

Table 1 summarizes the total appropriations and expenditures from the Outdoor Heritage, Clean Water, Parks and Trails, and Arts and Cultural Heritage funds from July 1, 2009, through June 30, 2011.

² *Minnesota Constitution*, art. XI, sec. 15.

³ We did not include the Arts and Cultural Heritage Fund in the scope of this audit. In August 2010, we issued a report, *Minnesota State Arts Board*, which included a finding related to the use of money appropriated from the Arts and Cultural Heritage Fund.

Table 1
Total Legacy Fund Appropriations and Expenditures
July 1, 2009, through June 30, 2011

| <u>Legacy Fund:</u> | Fiscal Years 2010-2011 <u>Appropriations</u> | Fiscal Years 2010-2011 <u>Expenditures</u> |
|---------------------------------|--|--|
| Outdoor Heritage Fund | \$ 146,471,000 | \$ 83,446,837 |
| Clean Water Fund | 152,245,000 | 85,562,117 |
| Parks and Trails Fund | 65,097,000 | 48,041,854 |
| Arts and Cultural Heritage Fund | <u>93,220,000</u> | <u>84,777,718</u> |
| Total | <u>\$457,033,000</u> | <u>\$301,828,226</u> |

Source: Minnesota Accounting and Procurement System.

The Legislature has tried to limit the use of Legacy money for administrative costs.⁴ When the Legislature first appropriated money from each Legacy fund in *Laws of Minnesota* 2009, Chapter 172 and *Laws of Minnesota* 2010, Chapter 361, it put percentage caps on some appropriations to limit the amount that could be used for administrative costs. In the 2010 appropriations from the Outdoor Heritage Fund, the Legislature specified that appropriated money could only be used for costs “directly related to and necessary for a specific appropriation and included in the project’s accomplishment plan;” it also specifically prohibited funding “indirect costs or other institutional overhead.”⁵ The 2011 appropriations law allowed money from all four funds to be used only for costs that were “directly related to and necessary for” a specific appropriation of Legacy money.⁶ Legislators took this approach to allow more discretion in using Legacy money for administrative costs. Organizations that receive Legacy money must be able to show that all costs – including administrative costs – charged to a Legacy appropriation are “directly related to and necessary for” the specific appropriation they received.⁷

⁴ We use the term “administrative costs” to include all support costs, including costs that are referred to as “indirect,” “overhead,” or “institutional” costs.

⁵ *Laws of Minnesota* 2010, chapter 361, art. 1, sec. 2, subd. 7.

⁶ *Laws of Minnesota* 2011, First Special Session, chapter 6, art. 1, sec. 2, subd. 7 (Outdoor Heritage Fund appropriations); *Laws of Minnesota* 2011, First Special Session, chapter 6, art. 2, sec. 2, subd. 2 (Clean Water Fund appropriations); *Laws of Minnesota* 2011, First Special Session, chapter 6, art. 3, sec. 2, subd. 2 (Parks and Trails Fund appropriations); and *Laws of Minnesota* 2011, First Special Session, chapter 6, art. 4, sec. 2, subd. 2 (Arts and Cultural Heritage Fund appropriations).

⁷ In its report, *The Legacy Amendment*, (issued on November 30, 2011), the Program Evaluation Division of the Office of the Legislative Auditor identified as an “ongoing concern” questions about how to appropriately and effectively limit the use of Legacy money for administrative costs.

Scope, Objective, and Methodology

We limited the scope of our audit to a review of the expenditures from the Outdoor Heritage, Clean Water, and Parks and Trails funds during the period from July 1, 2009, through January 31, 2011. We will examine expenditures from the Arts and Cultural Heritage Fund in 2012.

We analyzed the funds' expenditures and further narrowed the scope of our review to expenditures made by the Department of Natural Resources, Pollution Control Agency, and Board of Water and Soil Resources, which were nearly 90 percent of the funds' total expenditures during the period from July 2009 through January 2011.⁸ Table 2 summarizes the expenditures from the Legacy funds for the Department of Natural Resources, Pollution Control Agency, and Board of Water and Soil Resources from July 1, 2009, through January 31, 2011.

Table 2
Expenditures from the Legacy Funds for the
Department of Natural Resources, Pollution Control Agency, and
Board of Water and Soil Resources
July 1, 2009, through January 31, 2011¹

| <u>Agency / Legacy Fund:</u> | <u>Land Purchases & Easements</u> | <u>Grants²</u> | <u>Payroll</u> | <u>Nonpayroll³</u> | <u>Total Expenditures</u> |
|----------------------------------|---------------------------------------|---------------------------|--------------------|-------------------------------|---------------------------|
| Natural Resources: | | | | | |
| Outdoor Heritage Fund | \$43,961,839 | \$19,603,897 | \$ 228,050 | \$ 1,434,248 | \$65,228,034 |
| Parks and Trails Fund | 0 | 1,767,384 | 3,469,506 | 9,116,385 | 14,353,275 |
| Clean Water Fund | 0 | 75,000 | 3,134,186 | 2,577,717 | 5,786,903 |
| Total | <u>\$43,961,839</u> | <u>\$21,446,281</u> | <u>\$6,831,742</u> | <u>\$13,128,350</u> | <u>\$85,368,212</u> |
| Pollution Control: | | | | | |
| Clean Water Fund | \$ 0 | \$ 1,467,849 | \$7,897,497 | \$10,668,099 | \$20,033,445 |
| Total | <u>\$ 0</u> | <u>\$ 1,467,849</u> | <u>\$7,897,497</u> | <u>\$10,668,099</u> | <u>\$20,033,445</u> |
| Water and Soil Resources: | | | | | |
| Outdoor Heritage Fund | \$ 897,504 | \$ 136,000 | \$ 206,284 | \$ 3,969 | \$ 1,243,757 |
| Clean Water Fund | <u>2,380,728</u> | <u>15,469,892</u> | <u>924,973</u> | <u>112,249</u> | <u>18,887,842</u> |
| Total | <u>\$ 3,278,232</u> | <u>\$15,605,892</u> | <u>\$1,131,257</u> | <u>\$116,218</u> | <u>\$20,131,599</u> |

¹ Expenditures included fiscal years 2010 and 2011, through January 31, 2011.

² Grant expenditures included payments to the nonstate organizations shown in Table 2.

³ This category of expenditures included nonpayroll costs directly charged to the appropriations and costs allocated to appropriations for administrative services, such as accounting, human resources, and information technology, and facility costs (rent, utilities, etc.).

Source: Minnesota Accounting and Procurement System.

⁸ We did not examine five other agencies receiving appropriations from these three funds.

We also analyzed the grants of Legacy funds made by the Department of Natural Resources, Pollution Control Agency, and Board of Water and Soil Resources to local governments and nonprofit organizations, some of which were specifically identified in the appropriation laws and others which were determined through competitive grant programs. We selected for our testing ten nonstate organizations receiving the largest grants through each Legacy fund, as shown in Table 3. The table lists the organizations we examined, the source of the Legacy money they received, and total grants the state agencies awarded and paid through January 31, 2011.

Table 3
Selected Legacy Fund Grants to
Nonstate Organizations
July 1, 2009 through January 31, 2011

| <u>Grantee</u> | <u>Amounts Awarded</u> | <u>Amounts Paid</u> |
|--------------------------------------|------------------------|---------------------|
| <u>Outdoor Heritage Fund:</u> | | |
| Pheasants Forever, Inc. | \$17,008,737 | \$8,098,629 |
| Anoka County | 3,800,000 | 3,800,000 |
| Trust for Public Land | 1,850,000 | 1,850,000 |
| Ducks Unlimited | 8,020,000 | 1,720,055 |
| The Nature Conservancy | 6,101,279 | 1,387,009 |
| Southwest Initiative Foundation | 1,617,000 | 1,279,970 |
| Minnesota Land Trust | 2,154,000 | 440,807 |
| Trout Unlimited | 2,050,000 | 439,621 |
| <u>Clean Water Fund:</u> | | |
| St. Croix River Association | \$500,000 | \$466,820 |
| <u>Parks and Trails Fund:</u> | | |
| City of Nisswa | \$500,000 | \$500,000 |

Note: Appendix A identifies the specific legislative appropriations law authorizing grant funding to these organizations.

Sources: *Laws of Minnesota* 2009, chapter 172, *Laws of Minnesota* 2010, chapter 361, and the Minnesota Accounting and Procurement System.

The objective for our selected-scope audit of the expenditures of the Outdoor Heritage, Clean Water, and Parks and Trails funds made by the Department of Natural Resources, Pollution Control Agency, Board of Water and Soil Resources, and selected nonstate organizations was to answer the following questions:

- Did organizations have adequate internal controls to ensure they used money appropriated from Legacy funds only for purposes authorized in the Legacy Amendment and applicable state laws; safeguarded those financial resources; accurately paid employees, vendors, and grantees in accordance with managements' authorizations; complied with finance-related legal provisions; and created reliable financial data?

- Did each organization comply with significant finance-related legal requirements?

To answer these questions, we gained an understanding of each organization's financial policies and procedures; considered the risk of errors in the accounting records and potential noncompliance with relevant legal requirements; analyzed accounting data to identify unusual trends or uses of funds; examined a sample of Legacy grant appropriations; and reviewed evidence supporting financial transactions to test whether each organization's controls were effective and if the transactions complied with laws, regulations, policies, grant agreements and contract 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 various criteria to evaluate internal controls and compliance. We used, as our criteria to evaluate agency controls, the guidance contained in the *Internal Control-Integrated Framework*, published by the Committee of Sponsoring Organizations of the Treadway Commission.⁹ We used state laws, regulations, grant agreements and contracts, as well as policies and procedures established by the departments of Management and Budget and Administration and each organization's internal policies and procedures as criteria to assess compliance.

Conclusion

The selected internal controls at the organizations we reviewed were generally adequate to ensure that the organizations used money appropriated from the Legacy funds for the purposes authorized in the Legacy Amendment and state laws; safeguarded financial resources; accurately paid employees, vendors, and grantees in accordance with managements' authorizations; complied with finance-related legal provisions; and created reliable financial data. For the items tested, the organizations generally complied with significant finance-related legal requirements.

However, the state agencies¹⁰ we reviewed had certain internal control weaknesses and instances of noncompliance, as discussed in the following *Findings and Recommendations* section.

⁹ 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.

¹⁰ The Department of Natural Resources, Pollution Control Agency, and Board of Water and Soil Resources.

Findings and Recommendations

The Department of Natural Resources, Pollution Control Agency, and Board of Water and Soil Resources did not ensure that certain costs paid with money appropriated from Legacy funds complied with the restricted uses of those funds.

Finding 1

Money appropriated from Legacy funds may only be used for purposes specified in the Legacy Amendment and applicable state laws. The Department of Natural Resources, Pollution Control Agency, and Board of Water and Soil Resources could not demonstrate that certain costs they allocated to or paid from specific appropriations of Legacy money complied with the legal restrictions on the use of money appropriated from those funds.

PAYROLL COSTS

The state agencies we examined allocated some employees' payroll costs to appropriations from the Legacy funds based on estimates of the employees' assignments to projects or tasks, but they did not periodically assess how well those allocations corresponded to actual work those employees performed for the purposes of the specific appropriations. As a result, some payroll costs allocated to the Legacy funds may have been for work that did not comply with the purposes of specific Legacy appropriations.

To address that risk, we expanded our testing. We discussed with a sample of employees paid with Legacy funds the actual work they performed. While we did not find any obvious discrepancies (such as instances where employees paid with Legacy funds were unable to explain their general or specific contributions to Legacy-related activities), our approach was not sufficient to reach the conclusion that all payroll costs charged to the funds related to work that complied with the purposes of specific Legacy appropriations.

Without periodic validation by the state agencies that an allocation process resulted in costs that complied with the purpose of specific requirements of a funding source, there is an increased risk that a funding source, such as the Legacy funds, may pay for costs that do not contribute to specific programs, projects, and activities. The federal government protects itself against this risk by requiring grant recipients, including the State of Minnesota, to conduct quarterly time studies to validate the accuracy of payroll allocations,¹¹ and to obtain annual

¹¹ In a federal quarterly time study, employees track, over a period of a few weeks, how much time they actually spend performing services for specific federal programs, and management compares those actual hours to the allocations they had set up for those employees. Where the time studies show a discrepancy, management adjusts the allocation to better correspond to the actual hours worked.

certification from each employee paid entirely from a single federal grant that the grant's activities were the employee's sole scope of work duties. Neither the Department of Management and Budget nor the agencies had cost allocation policies that required agencies to periodically verify that payroll costs allocated to Legacy funds corresponded to actual work those employees performed for the purposes of the specific appropriations.

The agencies had the following additional weaknesses in other payroll cost allocations:

Payroll Adjustments - The Department of Natural Resources did not document, as required by state policy, the basis for any of the 14 Legacy-related payroll adjustments we tested.¹² Without documentation of the reason for the adjustment and calculations to support the adjustment amount, the department could not show how the adjustment resulted in an allocation that complied with the purposes of the specific appropriations. Based on discussions with the department's staff about the intent of the adjustments, we recalculated the adjustment amounts and identified approximately \$9,500 that had been allocated in error between the Legacy funds and other funds.

Other Payroll - Neither the Department of Management and Budget nor the agencies we reviewed in this audit had policies that addressed how to allocate other types of payroll costs, such as employee holiday, vacation, and sick leave; retroactive pay adjustments; separation payments; and unemployment benefits. Often, agencies allocated these types of costs based on the payroll allocation in place at the time of the transaction. This did not always result in allocations that ensured the costs complied with the purposes of the specific appropriations, as shown in the following examples:

- For 13 of 28 employees tested from the Department of Natural Resources and 10 of 24 employees tested from the Pollution Control Agency, employees did not allocate their leave hours (including vacation, sick, and holiday leave) to Legacy funds consistent with the allocation of hours they worked. For example, from August 2010 through January 2011, one Department of Natural Resources' employee allocated about 43 percent of his working hours to the Clean Water Fund, but allocated 100 percent of his leave hours to the Legacy funds. If the employee had allocated his leave in the same proportion he allocated the work he performed each pay period (which would be one way to do the allocation) he would have allocated about 97 hours, or about \$3,400, to non-Legacy funds.
- The Pollution Control Agency and Board of Water and Soil Resources allocated to the Clean Water Fund \$2,357 and \$400, respectively, certain

¹² Department of Management and Budget's SEMA4 Operating Policy & Procedures - PAY0029, requires that, "Agencies must document the rationale for any expense transfers that are processed."

retroactive pay adjustments that related to time periods when the employees had not worked on Clean Water Fund activities.

- The Department of Natural Resources allocated separation payments¹³ between funds based on the employees' payroll cost allocations at the time of separation. For example, the department allocated about \$2,400 of an employee's \$21,700 separation payment to the Parks and Trails Fund because the employee attributed about 9 hours of his time in his last pay period before retirement to Parks and Trails Fund activities; the employee had never otherwise identified any work hours as being related to Parks and Trails Fund activities. In total, we estimate that the department used \$4,175 of the Clean Water Fund's money and \$11,028 of the Parks and Trails Fund's money for separation payments that did not correspond to the hours the employees worked on those funds' activities. (Neither the Pollution Control Agency nor Board of Water and Soil Resources allocated any significant amount of employees' separation payments to Legacy funds.)
- The Department of Natural Resources paid unemployment costs of \$4,105 from the Clean Water Fund even though the unemployment costs were determined based on an employment period when the employee was entirely funded from the Game and Fish Fund.

OTHER COSTS

Some agencies allocated other costs, including administrative costs, to Legacy funds without documenting how those costs complied with the purposes of the specific appropriations of money from Legacy funds. For example:

- Through January 31, 2011, the Pollution Control Agency allocated about \$6.6 million¹⁴ of its costs to its appropriations of Clean Water Fund money without documenting that the costs complied with the purposes authorized by the laws that appropriated the money. The agency based its allocations on a general cost allocation rate the agency used to recover costs associated with its operations, including costs for accounting, human resources, and information technology support services; rent; and general office supplies and equipment. For example, the agency applied its fiscal year 2010 and 2011 cost allocation rates to a \$4,669,000 appropriation from the Clean Water Fund, which was for grants to help local governments identify ways to beneficially reuse municipal wastewater. The use of the cost allocation rates resulted in the agency allocating almost

¹³ Upon termination of employment from state service, employees are paid the balance of vacation hours accrued up to a maximum level and a percentage of their accrued sick leave hours.

¹⁴ Through June 30, 2011, the Pollution Control Agency had allocated costs totaling about \$8.7 million to its Clean Water Fund appropriations.

\$890,000 of its costs to the appropriation without documenting how those costs complied with the purposes of the appropriation.

- The Board of Water and Soil Resources could not show how \$4,256 it charged to a fiscal year 2011 Outdoor Heritage Fund appropriation for vehicle rentals, cell phone services, and employee expense reimbursements were directly related to and necessary for the purposes of the specific appropriation, as required by the 2010 appropriations law. In addition, the board could not show how \$20,000 of estimated vehicle rental costs and \$50,000 of other costs it charged to the Clean Water Fund complied with the purposes of the specific appropriations.
- The Department of Natural Resources could not show how expenditures totaling \$27,684 complied with the purposes of the specific appropriation from the Clean Water Fund and Parks and Trails Fund. The department did not have purchase orders to show authorization for the purchases, documents to show that the department received the goods, and invoices to show the accuracy of the payments. *Minnesota Statutes* require all officers and agencies of the state to maintain records necessary to provide full and accurate documentation of official activities.¹⁵
- The Pollution Control Agency had no assurance that an administrative cost rate used by a grantee only included costs that complied with the purposes of the specific appropriation and grant agreement. The grantee did not support how the administrative services it provided at \$100 per hour related to the actual costs incurred to administer the grant. The rate was not designated in the grant agreement with the agency; however, the grant budget limited the grantee's total reimbursement for administrative costs to \$50,000.

The Legacy Amendment and state laws allow Legacy funds only to be used for the purposes of the specific appropriation. Without policies and procedures on the allocation of payroll and other costs to Legacy funds, the state cannot ensure that agencies have complied with provisions in the Legacy Amendment and state laws that prescribe how Legacy money may be used.

Recommendations

- *The Department of Natural Resources, Pollution Control Agency, and Board of Water and Soil Resources should work with the Department of Management and Budget to develop policies to ensure that allocations of payroll and other costs comply with the purposes of the specific appropriation of the Legacy funds.*

¹⁵ *Minnesota Statutes* 2010, 15.17, subd. 1 and subd. 2.

- *The Department of Natural Resources, Pollution Control Agency, and Board of Water and Soil Resources should review and correct, as needed, allocation issues discussed in this finding.*
- *The Department of Natural Resources, Pollution Control Agency, and Board of Water and Soil Resources should review, correct, and document other similar payroll and cost allocations to ensure they comply with the purposes of the specific appropriation of money from Legacy funds.*

The Pollution Control Agency and Board of Water and Soil Resources made unauthorized advances of Legacy money to grantees.

Finding 2

The Pollution Control Agency and Board of Water and Soil Resources advanced Legacy funds to some grantees without sufficient authorization or in violation of state grant policies and grant agreements. The appropriation laws for the Outdoor Heritage Fund allowed grant advances only if approved as part of the required accomplishment plans.¹⁶ State policy¹⁷ states that reimbursement is the preferred way to make grant payments.¹⁸ The policy requires an agency that advances grant funds to include in the grant agreement the grant payment terms and to reconcile all advance payments within 12 months after beginning of the grant period.¹⁹

The entities had the following instances of noncompliance:

- The Board of Water and Soil Resources advanced \$136,000 in Outdoor Heritage Fund grants to 19 soil and water conservation districts. The accomplishment plans for these grants did not include approval for advance payments, as required by the appropriation laws.²⁰
- Although the Pollution Control Agency's grant agreement with a grantee limited payment to reimbursement based on invoices for services actually performed, the agency advanced \$450,000 to the grantee in August 2010. Based on our review of the grantee's financial records, it had spent only

¹⁶ *Laws of Minnesota* 2009, chapter 172, art. 1, sec. 2, subd. 11, and *Laws of Minnesota* 2010, chapter 361, art. 1, sec. 2, subd. 10.

¹⁷ Department of Administration, Office of Grants Management Policy 08-08.

¹⁸ Paying grants on a reimbursement basis allows the agency to better assess whether the grantee is using the funds efficiently and effectively to achieve the purposes of the grant in compliance with the grant agreement.

¹⁹ Department of Administration, Office of Grants Management Policy 08-08 was revised in August 2011 to require that all advance payments on grants be reconciled within 12 months of issuance or within 60 days of the end of the grant period, whichever comes first.

²⁰ *Laws of Minnesota* 2009, chapter 172, art. 1, sec. 2, subd. 11, and *Laws of Minnesota* 2010, chapter 361, art. 1, sec. 2, subd. 10.

about \$61,000 of the advance by April 2011 and invested the remaining \$389,000 in its money market account. In addition, the agency had not performed a financial reconciliation of the advance by August 2011, as required by state policy.

- As of May 2011, the Board of Water and Soil Resources had not reconciled advance payments to actual costs grantees incurred for several Clean Water Fund grants. State grants policy required reconciliations of all advances within 12 months of the beginning of the grant period,²¹ but the board had only reconciled one of the five we tested that had reached that deadline.

Recommendations

- *The Board of Water and Soil Resources should not advance grants from the Outdoor Heritage Fund unless specifically approved in each grant's accomplishment plan.*
- *The Pollution Control Agency should pay its grantees in accordance with the terms it establishes in its grant agreements.*
- *The Pollution Control Agency and Board of Water and Soil Resources should perform financial reconciliations of the grant funds they advanced and recover any unspent funds.*

Finding 3

The Department of Natural Resources, Pollution Control Agency, and Board of Water and Soil Resources paid some grantees for costs without ensuring that the costs complied with the restrictions applicable to the uses of Legacy funds.

The agencies paid some grantees for costs without ensuring that the costs complied with the restrictions applicable to the uses of Legacy funds, as explained in the bullets below:

- The Department of Natural Resources reimbursed a grantee \$21,702 for services a subcontractor performed before the services were an allowable cost of the grant. The executive director of the Lessard-Sams Outdoor

²¹ Effective March 2011, the Board of Water and Soil Resources obtained from the Department of Administration a waiver from the state policy requirement that it perform a reconciliation of advance grant payments within 12 months of the start of the grant period. The exemption required the board to limit initial advances to 50 percent of the grant amounts and to not pay additional grant funds until grantees had spent those initial advances and the board had performed the financial reconciliations. However, this waiver stated that it did not apply to grants the board funded prior to March 2011.

Heritage Council approved a revised accomplishment plan that added the subcontractor services to the grant. According to the executive director, the revised plan was intended to authorize payment for services the subcontractor provided after the revised plan was approved.²²

- The Pollution Control Agency paid reimbursement requests for six of the seven Clean Water Fund grantees we tested without receiving adequate supporting documentation to substantiate the costs. The department paid one grantee about \$111,000 for reimbursement requests without supporting evidence, such as contracts, invoices, or receipts. Other grantees requested reimbursements for payroll costs without identifying the specific employees, dates and hours worked, or the employees' pay rates; and mileage costs without identifying trip details, such as purpose, locations, or actual miles driven. Without sufficient detail to support specific expenses, the agency cannot determine if costs were reasonable or eligible for grant reimbursement.
- The Board of Water and Soil Resources did not clearly specify match requirements in some grant agreements for Clean Water Fund grants. Although the work plans incorporated into the grant agreements indicated matching amounts, the match requirements were not specified. The Clean Water Fund appropriation law required a local match of grant money from nonstate sources for certain types of grants. The state's grant policy requires agencies to use written grant agreements that include, in part, the grantee's duties and responsibilities in carrying out the grant.²³ Because the board did not include the match requirement in the grant agreements, the grantee may inadvertently not obtain the required matching funds. The board may also not adequately monitor for compliance with the specific appropriations if it did not include those requirements in the grant agreements.

Recommendations

- *The Department of Natural Resources should determine whether to seek recovery of amounts reimbursed to a grantee for unauthorized costs paid to the subcontractor.*
- *The Pollution Control Agency should require Clean Water Fund grantees to provide detailed, supporting documentation for expenses as a basis for reimbursement from grant funds.*
- *The Board of Water and Soil Resources should include in its grant agreements information sufficient for the grantee to clearly understand its matching requirements.*

²² *Laws of Minnesota* 2009, chapter 172, art. 1, sec. 2, subd. 9, required accomplishment plans approved by the Lessard-Sams Outdoor Heritage Council for all appropriations from the Outdoor Heritage Fund.

²³ Department of Administration, Office of Grants Management Policy 08-04.

Finding 4

The Department of Natural Resources did not accurately pay some reimbursement requests for grants from the Outdoor Heritage Fund.

The Department of Natural Resources' internal controls did not prevent or detect a significant duplicate payment and some minor payment errors. In addition, the department sometimes paid different amounts on grantee reimbursement requests without a documented explanation for the difference. The department had the following errors in its grant reimbursements to nonprofit organizations from the Outdoor Heritage Fund:

- Duplicate Payment - The Department of Natural Resources made a duplicate reimbursement to a grantee. The department paid the initial \$473,600 reimbursement in January 2010 and then paid it again in February 2010. The grantee notified the department about the duplicate payment; however, instead of requiring repayment, department staff allowed the grantee to offset the overpayment against subsequent reimbursement requests. It took almost five months for that offset to occur.
 - Ineligible Costs - The Department of Natural Resources reimbursed a grantee for \$4,000 of costs incurred before the grant agreement was executed. The department eventually detected the mistake and offset the overpayment against a subsequent grant reimbursement request.
 - Incorrect Accounts - The Department of Natural Resources paid \$2,100 for land appraisals to a grantee from the wrong account in the accounting system. The grantee had received several grants from the Outdoor Heritage Fund, and the department mistakenly paid the appraisal cost from the wrong grant. As a result, the accounting system did not reflect accurate costs for the grants involved.
 - Reimbursement Errors – The Department of Natural Resources' grant reimbursements to three grantees included small inaccuracies in the amounts paid. First, the department did not reimburse one grantee for \$2,625 of eligible land appraisal and survey costs included in a \$125,000 reimbursement request, and the department's records did not have a documented explanation for not paying that amount. Second, the department did not identify that another grantee included the same costs totaling \$298 in two different reimbursement requests. Third, the department did not pay the correct amount to another grantee for 4 of the 13 reimbursement requests we tested. Although these errors were minor, in the aggregate, they indicate a lack of controls over the department's grant reimbursements.
-

Without adequate controls to ensure the accuracy of grant payments, the department has an increased risk of errors occurring without detection.

Recommendation

- *The Department of Natural Resources should review the nature of payment errors and improve controls over its grant reimbursement procedures to reduce mistakes.*

The Pollution Control Agency did not sufficiently monitor whether a grantee complied with statutory match requirements.

Finding 5

The Pollution Control Agency did not have evidence that it assessed the propriety or adequacy of matching resources designated by a grantee before the deadline set in the appropriation law. The law required that the grant appropriation be matched by nonstate resources, and that money not matched by November 15, 2010, was no longer available for the grant purpose.²⁴

In addition, the Pollution Control Agency did not adequately monitor the costs a grantee used to match the \$50,000 designated in the grant for administrative services. For example, on one payment request, the agency allowed the grantee to include in its match around \$7,000 of costs for the production and mailing of the grantee's newsletter; these costs may not have complied with the purpose of the grant. On a subsequent payment request, the agency did not question the grantee's basis for increasing the hourly rate for some in-kind services from \$50 to \$200. In addition, the grantee told us they had estimated the hours used as a basis for the match and had insufficient documentation to show that those services had been provided to the grant.

Recommendations

- *The Pollution Control Agency should document its assurance that the grantee had established sufficient matching resources before the November 15, 2010 deadline.*
- *The Pollution Control Agency should review costs submitted as part of a grantee's match to ensure the costs contribute to the purposes of the grant and represent actual costs incurred or services provided.*

²⁴ *Laws of Minnesota* 2009, chapter 172, art. 2, sec. 4 (j).

Finding 6 **The Department of Natural Resources did not adequately safeguard state warrants held by employees for land acquisition closings.**

The Department of Natural Resources did not have a policy to protect warrants needed for land acquisition closings.²⁵ Normally, the employee obtained the warrants shortly before the date of the land acquisition closing; however, sometimes, due to unanticipated events, a closing was postponed. For example, an employee held a \$716,400 warrant in a locked desk for five and a half months before the land closing eventually occurred. Another employee held a \$6,694 warrant for four months before re-depositing it back into the state's bank account; when the warrant was reissued, the employee held it for two additional months before the closing finally occurred. Holding warrants for extended periods increases the risk of loss or theft.

Recommendation

- *The Department of Natural Resources should establish a policy for protecting warrants held by employees for land acquisition closings.*

²⁵ A warrant is similar to a check, with the state treasury acting as the bank.

Appendix A
Selected Nonprofit and Local Government Organizations
Receiving Legacy Grants
Fiscal Years 2010 through 2011 (through January 31, 2011)

| <u>Grantee</u> | <u>Legislative Session Law</u> | <u>Award</u> | <u>Expended</u> |
|--------------------------------------|---|---------------------|--------------------|
| <u>Outdoor Heritage Fund:</u> | | | |
| Pheasants Forever, Inc. | 2009, chapter 172, art. 1, sec. 2, subd. 2(c) | \$ 3,000,000 | \$2,877,234 |
| Pheasants Forever, Inc. | 2009, chapter 172, art. 1, sec. 2, subd. 4(c) | 5,600,000 | 3,034,186 |
| Pheasants Forever, Inc. | 2009, chapter 172, art. 1, sec. 2, subd. 5(a) | 125,000 | 5,183 |
| Pheasants Forever, Inc. | 2009, chapter 172, art. 1, sec. 2, subd. 5(a) | 159,000 | 155,050 |
| Pheasants Forever, Inc. | 2009, chapter 172, art. 1, sec. 2, subd. 5(a) | 45,737 | 22,284 |
| Pheasants Forever, Inc. | 2010, chapter 361, art. 1, sec. 2, subd. 2(c) | 3,015,000 | 828,697 |
| Pheasants Forever, Inc. | 2010, chapter 361, art. 1, sec. 2, subd. 3(e) | 1,559,000 | 10,995 |
| Pheasants Forever, Inc. | 2010, chapter 361, art. 1, sec. 2, subd. 4(b) | <u>3,505,000</u> | <u>1,165,000</u> |
| | | <u>\$17,008,737</u> | <u>\$8,098,629</u> |
| Anoka County | 2009, chapter 172, art. 1, sec. 2, subd. 2(g) | \$ 1,900,000 | \$1,900,000 |
| Anoka County | 2010, chapter 361, art. 1, sec. 2, subd. 2(e) | <u>1,900,000</u> | <u>1,900,000</u> |
| | | <u>\$ 3,800,000</u> | <u>\$3,800,000</u> |
| Trust for Public Land | 2009, chapter 172, art. 1, sec. 2, subd. 5(a) | 350,000 | \$ 350,000 |
| Trust for Public Land | 2010, chapter 361, art. 1, sec. 2, subd. 5(a) | <u>1,500,000</u> | <u>1,500,000</u> |
| | | <u>\$ 1,850,000</u> | <u>\$1,850,000</u> |
| Ducks Unlimited | 2009, chapter 172, art. 1, sec. 2, subd. 4(b) | \$ 2,528,000 | \$1,704,942 |
| Ducks Unlimited | 2009, chapter 172, art. 1, sec. 2, subd. 4(e) | 450,000 | 15,113 |
| Ducks Unlimited | 2010, chapter 361, art. 1, sec. 2, subd. 4(a) | <u>5,042,000</u> | <u>0</u> |
| | | <u>\$ 8,020,000</u> | <u>\$1,720,055</u> |
| The Nature Conservancy | 2009, chapter 172, art. 1, sec. 2, subd. 5(a) | \$ 157,279 | \$ 150,903 |
| The Nature Conservancy | 2009, chapter 172, art. 1, sec. 2, subd. 5(a) | 250,000 | 61,957 |
| The Nature Conservancy | 2010, chapter 361, art. 1, sec. 2, subd. 2(d) | 2,041,000 | 1,385 |
| The Nature Conservancy | 2010, chapter 361, art. 1, sec. 2, subd. 2(f) | <u>3,653,000</u> | <u>1,172,764</u> |
| | | <u>\$ 6,101,279</u> | <u>\$1,387,009</u> |
| Southwest Initiative Foundation | 2009, chapter 172, art. 1, sec. 2, subd. 2(b) | <u>\$ 1,617,000</u> | <u>\$1,279,970</u> |
| Minnesota Land Trust | 2009, chapter 172, art. 1, sec. 2, subd. 2(f) | \$ 500,000 | \$ 41,511 |
| Minnesota Land Trust | 2010, chapter 361, art. 1, sec. 2, subd. 3(a) | 816,000 | 7,670 |
| Minnesota Land Trust | 2010, chapter 361, art. 1, sec. 2, subd. 5(e) | <u>838,000</u> | <u>391,626</u> |
| | | <u>\$ 2,154,000</u> | <u>\$ 440,807</u> |
| Trout Unlimited | 2009, chapter 172, art. 1, sec. 2, subd. 5(c) | <u>\$ 2,050,000</u> | <u>\$ 439,621</u> |
| <u>Clean Water Fund:</u> | | | |
| St. Croix River Association | 2009, chapter 172, art. 2, sec. 4 (j) | <u>\$ 500,000</u> | <u>\$ 466,820</u> |
| <u>Parks and Trails Fund:</u> | | | |
| City of Nisswa | 2009, chapter 172, art. 3, sec. 2 (d) | <u>\$ 500,000</u> | <u>\$ 500,000</u> |

Source: Auditor created using *Laws of Minnesota* and the Minnesota Accounting and Procurement System.

Minnesota Department of Natural Resources

Office of the Commissioner
500 Lafayette Road • St. Paul, MN • 55155



November 17, 2011

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

Dear Mr. Nobles:

Thank you for the opportunity to respond to the draft report on Legacy Fund expenditures. We concur with the findings and recommendations, and offer the following specific comments regarding the findings applicable to the Department of Natural Resources (DNR) in your report:

Audit Finding #1: The Department of Natural Resources, Pollution Control Agency, and Board of Water and Soil Resources did not ensure that certain costs paid with money appropriated from Legacy funds complied with the restricted uses of those funds.

Audit Recommendations:

- *The Department of Natural Resources, the Pollution Control Agency, and the Board of Water and Soil Resources should work with the Department of Management and Budget to develop policies to ensure that allocations of payroll and other costs comply with the purposes of the specific appropriation of the Legacy funds.*
- *The Department of Natural Resources, the Pollution Control Agency, and the Board of Water and Soil Resources should review and correct, as needed, allocation issues discussed in this finding.*
- *The Department of Natural Resources, the Pollution Control Agency, and the Board of Water and Soil Resources should review, correct, and document other similar payroll and cost allocations to ensure they comply with the purposes of the specific appropriation of money from Legacy funds.*

DNR Response: Partially Resolved - The department is currently involved in a project with MMB that will address the concerns identified in the recommendation. The status of that project as it pertains to each bulleted recommendation above is as follows:

- The Laws of 2011, 1st Special Session (Chapter 6, Article 5, Section 9) directed MMB to provide Legacy accounting and technical assistance to state agencies as follows: “No later than January 1, 2012, the commissioner of management and budget shall finalize guidance and best practices to assist state agencies in uniformly accounting for their expenditure of legacy funds.” DNR will continue to work with MMB on this joint project, and will document its current allocation policies.
 - Person responsible for resolution: Jerry Hampel
 - Estimated date of completion: January 1, 2012
- Based on an internal audit, DNR completed the necessary transfers to correct the \$9,500 of payroll adjustment errors prior to the exit conference meeting.
 - Person responsible for resolution: Jerry Hampel
 - Estimated date of completion: Implemented
- DNR will review, correct and document resolution of other similar payroll and cost allocation errors as noted in the report if possible. Going forward, additional emphasis will be placed on documenting the rationale for allocations or adjustments as necessary to comply with current policies.
 - Person responsible for resolution: Jerry Hampel
 - Estimated date of completion: January 1, 2012

Audit Finding #3: The Department of Natural Resources, the Pollution Control Agency, and the Board of Water and Soil Resources paid some grantees for costs without ensuring that the costs complied with the restrictions applicable to the uses of Legacy funds.

Audit Recommendation: The Department of Natural Resources should determine whether to seek recovery of amounts reimbursed to the grantee for unauthorized costs paid to the subcontractor.

DNR Response: Resolved - On November 7, 2011, DNR sent a certified letter to the grantee requesting repayment by November 30, 2011. The grantee stated that the executive director of the Lessard-Sams Outdoor Heritage Council has indicated he will make a proposal to the council to amend the work plans to provide for retroactive funding of the overpayment noted in the report.

- Person responsible for resolution: Denise Anderson
- Estimated date of completion: Implemented

Audit Finding #4: The Department of Natural Resources did not accurately pay some reimbursement requests for grants from the Outdoor Heritage Fund.

Audit Recommendation: The Department of Natural Resources should review the nature of payment errors and improve controls over its grant reimbursement procedures to reduce mistakes.

DNR Response: Partially Resolved - DNR agrees with the errors identified and completed adjustments to correct the accounts prior to the exit conference meeting. In addition, DNR restructured the pass-thru grants operations within OMBS in October 2011 to provide additional supervisory review and oversight to the grant specialist(s). Redesign of controls in the accounts payable unit will also be considered to provide further improvements over grant reimbursements.

- Person responsible for resolution: Jerry Hampel
- Estimated date of completion: January 1, 2012

Audit Finding #6: The Department of Natural Resources did not adequately safeguard state warrants held by employees for land acquisition closings.

Audit Recommendation: The Department of Natural Resources should establish a policy for protecting warrants held by employees for land acquisition closings.

DNR Response: Partially Resolved - The Division of Land and Minerals revised its procedures to implement additional safeguards over warrants returned when land acquisition closing dates are rescheduled or cancelled. The department will also revise its administrative policies for this and other similar situations in non-land acquisition areas that may result in a returned warrant.

- Person responsible for resolution: Jerry Hampel
- Estimated date of completion: January 1, 2012

Again, thank you for the opportunity to respond to the draft report. It has been a tremendous challenge to implement the Legacy programs within the short timeframe since the Legacy Amendment was authorized. We are committed to implementing in a transparent and accountable manner.

Sincerely,



Tom Landwehr
Commissioner



Minnesota Pollution Control Agency

520 Lafayette Road North | St. Paul, Minnesota 55155-4194 | 651-296-6300

800-657-3864 | 651-282-5332 TTY | www.pca.state.mn.us | Equal Opportunity Employer

November 23, 2011

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

Dear Mr. Nobles:

Thank you for the opportunity to review and respond to the Office of Legislative Auditor's (OLA) findings and recommendations resulting from a recent audit of the Legacy funds for the State of Minnesota, of which the Minnesota Pollution Control Agency (MPCA) was a recipient. The MPCA is committed to sound fiscal and program management, and the use of Legacy funds to meet the requirements of the Federal Clean Water Act, the State Clean Water Legacy Act, and other legislative directives.

Further, the MPCA appreciates the professional review conducted by OLA staff. The MPCA has written a response to each audit finding and recommendation.

Finding #1: The Department of Natural Resources, Pollution Control Agency, and Board of Water and Soil Resources did not ensure that certain costs paid with money appropriated from Legacy funds complied with the restricted uses of those funds.

OLA Recommendation:

- *The Department of Natural Resources, the Pollution Control Agency, and the Board of Water and Soil Resources should work with the Department of Management and Budget to develop policies to ensure that allocations of payroll and other costs comply with the purposes of the specific appropriation of the Legacy funds.*
- *The Department of Natural Resources, the Pollution Control Agency, and the Board of Water and Soil Resources should review and correct, as needed, allocation issues discussed in this finding.*
- *The Department of Natural Resources, the Pollution Control Agency, and the Board of Water and Soil Resources should review, correct, and document other similar payroll and cost allocations to ensure they comply with the purposes of the specific appropriation of money from Legacy funds.*

Agency response: The MPCA generally agrees with the OLA's recommendations.

The MPCA corrected payroll where staff work hours were found to be inconsistent with the predicted time allocation during the audit. The MPCA is also refining procedures to improve its reconciliation of work plans to the actual hours worked on a project or program. These procedures will describe the required documentation and the reconciliation schedule. The MPCA further commits to work with Minnesota Management and Budget (MMB) to improve the electronic self-entry payroll system, so that it supports the Agency's use of multiple funding sources to implement its programs, including an accurate allocation of leave time.

However, the MPCA disagrees with the OLA's conclusion on page 11 on how retroactive pay should be charged. In FY2008-2009, Clean Water Legacy staff were funded from the General Fund. The Clean Water Legacy Act appropriations from the General Fund were appropriated as a one-time funding mechanism. Agencies cannot charge payroll expenditures to the previous fiscal year after mid-July. After that time, adjustments must be charged to the current fiscal year. The MPCA believes it appropriately paid retroactive payroll adjustments from the Clean Water Fund since the adjustments were for staff performing the same work, just under the new funding source. The MPCA believes it would have been inappropriate to charge another funding source for these payroll adjustments.

The MPCA commits to work with MMB to complete risk assessments of Agency operations, ensure the strength of internal controls, and document its efforts to monitor these critical components. The MPCA also will continue to refine the agency cost allocation plan and all expenditures are documented to show compliance with the purposes of the appropriation. The MPCA will also review its policies in determining the reasonableness of costs used by its grantees, and where necessary to provide training, guidance documents and monitoring.

Implementation Date: June 30, 2012

Responsible Manager: Myrna Halbach, Assistant Chief Financial Officer

Finding #2: The Pollution Control Agency and the Board of Water and Soil Resources made unauthorized advances of Legacy money to grantees.

OLA Recommendation:

- *The Board of Water and Soil Resources should not advance grants from the Outdoor Heritage Fund unless specifically approved in each grant's accomplishment plan.*
- *The Pollution Control Agency should pay its grantees in accordance with the terms it establishes in its grant agreements.*
- *The Pollution Control Agency and the Board of Water and Soil Resources should perform financial reconciliations of the grant funds they advanced and recover any unspent funds.*

Agency response: The MPCA agrees with the OLA's recommendations. The Agency commits to improved training for its grants managers regarding grant terms and requirements. The MPCA's Assistant CFO and Contract Unit supervisor will develop and conduct the training.

Implementation Date: December 31, 2011

Responsible Manager: Myrna Halbach, Assistant Chief Financial Officer

Finding #3: The Department of Natural Resources, the Pollution Control Agency, and the Board of Water and Soil Resources paid some grantees for costs without ensuring that the costs complied with the restrictions applicable to the uses of Legacy funds.

OLA Recommendation:

- *The Department of Natural Resources should determine whether to seek recovery of amounts reimbursed to a grantee for unauthorized costs paid to the subcontractor.*
- *The Pollution Control Agency should require Clean Water Fund grantees to provide detailed, supporting documentation for expenses as a basis for reimbursement from grant funds.*

- *The Board of Water and Soil Resources should include in its grant agreements information sufficient for the grantee to clearly understand its matching requirements.*

Agency response: The MPCA agrees with the recommendation. The Agency commits to updating its policy and training on the level of supporting documentation required for reimbursement of grant funds.

Implementation Date: December 31, 2011

Responsible Manager: Myrna Halbach, Assistant Chief Financial Officer

Finding #5: The Pollution Control Agency did not sufficiently monitor whether a grantee complied with statutory match requirements.

OLA Recommendation:

- *The Pollution Control Agency should document its assurance that the grantee had established sufficient matching resources before the November 15, 2010 deadline.*
- *The Pollution Control Agency should review costs submitted as part of a grantee's match to ensure the costs contribute to the purposes of the grant and represent actual costs incurred or services provided.*

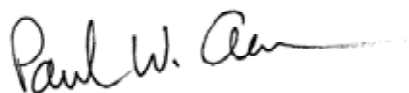
Agency response: The MPCA agrees with the OLA's recommendation above. The MPCA has initiated a review of the process used to determine whether matching resources exist, and the reasonableness of costs under the grant provisions for reimbursement.

Implementation Date: December 31, 2011

Responsible Manager: Myrna Halbach, Assistant Chief Financial Officer

Thank you again for the opportunity to respond. If you have any questions, please feel free to contact Assistant Chief Financial Officer Myrna Halbach at 651-757-2403, Myrna.Halbach@state.mn.us, or Finance Manager Lyle Mueller at 651-757-2591, Lyle.Mueller@state.mn.us.

Sincerely,



Paul W. Aasen
Commissioner



November 22, 2011

James R. Nobles, Legislative Auditor
Room 140 Centennial Building
658 Cedar Street
Saint Paul, Minnesota 55155

Dear Mr. Nobles:

Thank you for the opportunity to respond to the findings and recommendations included in the draft audit report of the Legacy Fund expenditures conducted by your office for the period July 1, 2009 through January 31, 2011.

For each recommendation we have noted the response, persons responsible for resolving the finding, and the estimated completion date of the action planned.

Finding 1: The Department of Natural Resources, Pollution Control Agency, and Board of Water and Soil Resources did not ensure that certain costs paid with money appropriated from Legacy funds complied with the restricted uses of those funds.

Recommendation: The Department of Natural Resources, the Pollution Control Agency, and the Board of Water and Soil Resources should work with the Department of Management and Budget to develop policies to ensure that allocations of payroll and other costs comply with the purposes of the specific appropriation of Legacy funds.

Recommendation: The Department of Natural Resources, the Pollution Control Agency, and the Board of Water and Soil Resources should review and correct, as needed allocation issues discussed in these findings.

Recommendation: The Department of Natural Resources, the Pollution Control Agency, and the Board of Water and Soil Resources should review, correct, and document other similar payroll and cost allocations to ensure they comply with the purposes of the specific appropriation of money from Legacy funds.

Response: We agree with the recommendations. BWSR has already developed Clean Water Fund spending plans for fiscal year 2012 and submitted them to MMB. We are planning an upgraded system for tracking staff hours and currently are researching several options. We have implemented a periodic review and adjustment of actual time spent vs. planned time on all Legacy Funds. During the audit and in the period directly after it we reviewed and made adjustments to entries for those items where we agreed with the audit findings.

Persons Responsible: Julie Blackburn, Assistant Director, and William Eisele, Admin. Serv. Dir.

Estimated Completion Date: July 2012.

Finding 2: The Pollution Control Agency and the Board of Water and Soil Resources made unauthorized advances of Legacy money to grantees.

Recommendation: The Board of Water and Soil Resources should not advance grants from the Outdoor Heritage Fund unless specifically approved in each grant's accomplishment plan.

Response: We agree that the Board of Water and Soil Resources should not advance Outdoor Heritage Funds via grants or contracts unless specifically approved in the accomplishment plan. BWSR will seek in-advance authorization from the Lessard-Sams Outdoor Heritage Council via accomplishment plan amendments and forthcoming approvals.

Persons Responsible: Kevin Lines, Easement Section Manager, and David Weirens, Land and Water Section Manager.

Estimated Completion Date: June 30, 2012.

Recommendation: The Pollution Control Agency and the Board of Water and Soil Resources should perform financial reconciliations of the grant funds they advanced and recover any unspent funds.

Response: We agree with the recommendation and believed it was addressed through the receipt of two exception requests from the Office of Grants Management (OGM) and the adoption of a Board policy¹. The Board is carrying out the grant management functions identified in the recommendation and is committed to reconciling grants and recovering any unspent funds consistent with policies of the OGM. The Board will develop means to carry out reconciliation of grants that are subject to three different versions of OGM policy 08-08.

Person Responsible: David Weirens, Land and Water Section Manager.

Estimated Completion Date: Underway, with completion in July 2012.

¹ The Board established policies and procedures to comply with OGM Policies 08-08 and 08-10 beginning in May 2010. On December 7, 2010 the Board submitted two exception requests to the OGM, specifically regarding the requirement to reconcile grants within 12 months of the beginning of the grant period. Both requests were granted, one on March 10, 2011 and the other on July 26, 2011. The Board adopted a policy on June 22, 2011 regarding the establishment of grant monitoring and verification procedures consistent with these exceptions. Receipt of the approved exception requests, adoption of the revised Board policy followed by staff implementation brought BWSR into compliance with policies 08-08 and 08-10. OGM policy 08-08 was subsequently revised on August 31, 2011 and the Board will again take steps to align the latest OGM policy and Board policy.

Finding 3: The Department of Natural Resources, the Pollution Control Agency, and the Board of Water and Soil Resources paid some grantees for costs without ensuring that the costs complied with the restrictions applicable to the uses of Legacy funds.

Recommendation: The Board of Water and Soil Resources should include in its grant agreements information sufficient for the grantee to clearly understand its matching requirements.

Response: We will enact the recommendation. The match amount is currently specified in the work plan which is the custom tailored portion of the grant agreement. In addition, the required match is prescribed and communicated with grantees in several ways, including:

1. Board policy resolutions,
2. Request for Proposals,
3. eligibility criteria,
4. the workplan portion of the grant agreement²,
5. local government resolutions authorizing grant applications and grant acceptance, and
6. grant monitoring and match verification protocols.

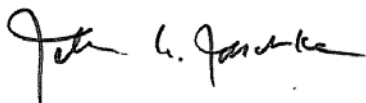
In the past ten years BWSR has had no disputes with grantees related to the match amount required.

Person Responsible: David Weirens, Land and Water Section Manager.

Estimated Completion Date: Completed.

This concludes the agency response. We value the professional work by the OLA staff to evaluate our programs and process and will address all findings, and ideas from other sources, as we go forward with the Legacy aspects of our mission. Please let me know if you have any questions.

Sincerely,



John G. Jaschke, Executive Director

cc: Brian Napstad, BWSR Board Chair

² The grant to the Conservation Corps of Minnesota and Iowa (formerly Minnesota Conservation Corps) did not include a specific grant match amount as the grant – assembled from three separate appropriations to meet legislative intent – was to provide labor services to other Clean Water Fund grant projects that were already approved and met or exceeded the match requirement. For these unique grants, BWSR established a project-by-project review and staff approval process for each activity conducted by the grantee in the workplan portion of the grant agreement.