



FINANCIAL AUDIT DIVISION REPORT

Office of MN.IT Services

Billings for Agency-Based Information Technology Services

Internal Controls and Compliance Audit

July 2014 through March 2016

December 8, 2016

Report 16-17

FINANCIAL AUDIT DIVISION
Centennial Building – Suite 140
658 Cedar Street – Saint Paul, MN 55155
Telephone: 651-296-4708 • Fax: 651-296-4712
Email: legislative.auditor@state.mn.us
Website: <http://www.auditor.leg.state.mn.us>
Through Minnesota Relay: 1-800-627-3529 or 7-1-1

Financial Audit Division

The Financial Audit Division annually audits the state's financial statements and, on a rotating schedule, audits agencies in the executive and judicial branches of state government, three metropolitan agencies, and several "semi-state" organizations. The division has a staff of about 30 auditors, most of whom are CPAs. The division conducts audits in accordance with standards established by the American Institute of Certified Public Accountants and the Comptroller General of the United States.

The Office of the Legislative Auditor (OLA) also has a Program Evaluation Division, which evaluates topics periodically selected by the Legislative Audit Commission.

Reports issued by both OLA divisions are solely the responsibility of OLA and may not reflect the views of the Legislative Audit Commission, its individual members, or other members of the Minnesota Legislature. For more information about OLA reports, go to:

<http://www.auditor.leg.state.mn.us>

To obtain reports in electronic ASCII text, Braille, large print, or audio, call 651-296-4708. People with hearing or speech disabilities may call through Minnesota Relay by dialing 7-1-1 or 1-800-627-3529.

To offer comments about our work or suggest an audit, investigation, or evaluation, call 651-296-4708 or e-mail legislative.auditor@state.mn.us.

Conclusion on Internal Controls

The Financial Audit Division bases its conclusion about an organization's internal controls on the number and nature of the control weaknesses we found in the audit. The three possible conclusions are as follows:

Conclusion	Characteristics
Adequate	The organization designed and implemented internal controls that effectively managed the risks related to its financial operations.
Generally Adequate	With some exceptions, the organization designed and implemented internal controls that effectively managed the risks related to its financial operations.
Not Adequate	The organization had significant weaknesses in the design and/or implementation of its internal controls and, as a result, the organization was unable to effectively manage the risks related to its financial operations.



December 8, 2016

Representative Sondra Erickson, Chair
Legislative Audit Commission

Members of the Legislative Audit Commission

Thomas A. Baden, Jr., Commissioner and Chief Information Officer
Office of MN.IT Services

This report presents the results of our internal controls and compliance audit of the Office of MN.IT Services for the period July 2014 through March 2016. The objectives of this audit were to determine whether the Office of MN.IT Services had adequate internal controls to ensure that it accurately billed state agencies for agency-based information technology services and whether MN.IT complied with the legal requirements we tested.

This audit was conducted by Tracia Polden, Senior Auditor. We received the full cooperation of the Office of MN.IT Services' 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

Table of Contents

	<u>Page</u>
Report Summary	1
Agency Overview	3
Objectives, Scope, and Methodology	5
Conclusion	6
Office of MN.IT Services' Response.....	7

Report Summary

The Office of MN.IT Services (MN.IT) is an executive branch agency that provides information technology services to other state agencies.¹ State law requires state agencies to reimburse MN.IT for the cost of those services. To meet agencies' unique information technology needs, the office provides some services through staff physically located in executive branch agencies.² In fiscal year 2016, MN.IT billed state agencies approximately \$155.6 million for these agency-based information technology services.

Over the past few years, MN.IT has changed the way it bills state agencies for agency-based services. In phases, MN.IT shifted from billings using predetermined billing rates to billings using the actual payroll costs of staff providing agency-based services. The first agencies MN.IT phased in had simple funding structures, such as primarily operating with money from the state's General Fund. The agencies MN.IT phased in later had more complex funding structures, such as numerous federal grant programs, and MN.IT needed to tie its billings for agency-based services to specific programs. Starting in fiscal year 2016, MN.IT billed most agencies for the actual payroll costs of its employees providing agency-based services.³

Audit Scope

We conducted this audit to see whether MN.IT had adequate internal controls over payroll processes for its employees who provided agency-based information technology services and whether it accurately billed agencies for these services. We examined MN.IT billings for agency-based services for the period from July 2014 through March 2016, to the extent that MN.IT used actual payroll costs to bill the agencies for those services.⁴

¹ While the Office of MN.IT Services primarily serves other state agencies, it also provides some services to Minnesota county and local governments, K-12 schools, higher education, and some Minnesota nonprofits.

² The office also centrally manages services shared by numerous entities, such as email and voice communication tools, mainframe computing, managed hosting of applications and websites, and data center facilities operations. OLA previously audited MN.IT's billings for these shared services. See Office of the Legislative Auditor, Financial Audit Division Report 15-01, *Office of MN.IT Services - Billings for Shared Information Technology Services*, issued January 22, 2015.

³ Exceptions were the departments of Employment and Economic Development, Natural Resources, and Public Safety. These departments continued to pay for agency-based services directly through the state's payroll system rather than through MN.IT's billing process. MN.IT phased these agencies into its billing process in fiscal year 2017.

⁴ The scope of our audit did not include billings for agency-based services using predetermined billing rates.

In addition to analyzing payroll expenditures for agency-based services and MN.IT's processes to prepare and disseminate its bills, we specifically tested internal controls over payroll processes for MN.IT staff providing agency-based services at three executive branch agencies – the departments of Health, Human Services, and Transportation.

Conclusion

The Office of MN.IT Services had adequate internal controls to ensure it accurately billed other state agencies for payroll costs related to agency-based information technology services. The office also paid those employees in accordance with management's authorizations, bargaining agreements, and other personnel and payroll related legal requirements we tested.

Agency Overview

Office of MN.IT Services

The Office of MN.IT Services (MN.IT) is an executive branch agency that provides information technology services to other state agencies.⁵ MN.IT's commissioner, Thomas Baden, appointed by Governor Mark Dayton in 2015, is also the state's chief information officer. The commissioner oversees the work of nearly 2,100 information technology staff.⁶ To meet the unique information technology needs of executive branch agencies, most of these employees are physically located in the agencies; we refer to services provided by these employees as "agency-based" services.⁷ State law requires state agencies to reimburse MN.IT for the cost of those services.⁸

Over the past few years, MN.IT has changed the way it bills state agencies for agency-based services.⁹ In phases, MN.IT shifted from billings using predetermined billing rates to billings using the actual payroll costs of staff providing agency-based services. The first agencies MN.IT phased in had simple funding structures, such as primarily operating with money from the state's General Fund. The agencies MN.IT phased in later had more complex funding structures, such as numerous federal grant programs, and MN.IT needed to tie its billings for agency-based services to specific programs. Starting in fiscal year 2016, MN.IT billed most agencies for the actual payroll costs of its employees providing agency-based services.¹⁰

⁵ While the Office of MN.IT Services primarily serves other state agencies, it also provides some services to Minnesota's county and local governments, K-12 schools, higher education, and some Minnesota nonprofits.

⁶ Many of these employees were employed by various state agencies prior to the consolidation of the state's information technology services required by *Laws of Minnesota* 2011, First Special Session, chapter 10, art. 4.

⁷ The office also centrally manages services shared by numerous entities, such as email and voice communication tools, mainframe computing, managed hosting of applications and websites, and data center facilities operations. OLA previously audited MN.IT's billings for these shared services. See Office of the Legislative Auditor, Financial Audit Division Report 15-01, *Office of MN.IT Services, Billings for Shared Information Technology Services*, issued January 22, 2015.

⁸ *Minnesota Statutes* 2015, 16E.14, subd. 3.

⁹ In addition to billing agencies for payroll costs related to agency-based information technology services, MN.IT also bills for various hardware and software purchases for agency-based networks and applications. The scope of our audit did not include billings for these nonpayroll agency-based costs.

¹⁰ Exceptions were the departments of Employment and Economic Development, Natural Resources, and Public Safety. These departments continued to pay for agency-based services directly through the state's payroll system rather than through MN.IT's billing process. MN.IT phased these agencies into its billing process in fiscal year 2017.

As shown in Table 1, MN.IT billed state agencies approximately \$155.6 million in fiscal year 2016 for its employees providing agency-based information technology services.

Table 1
Office of MN.IT Services
Billings for Agency-Based Information Technology Services

<u>State Agency</u>	<u>Fiscal Years¹</u>	
	<u>2015</u>	<u>2016</u>
Human Services ²		\$ 71,342,350
Revenue ³	\$13,340,805	12,893,338
Transportation ²		20,439,190
Management and Budget ³	7,434,921	7,150,642
Corrections ³	6,518,017	6,657,927
Health ²		12,204,345
Pollution Control Agency ²		7,387,986
Other State Agencies ⁴	<u>10,965,617</u>	<u>17,556,164</u>
Total	<u>\$38,259,360</u>	<u>\$155,631,942</u>

¹ The state's fiscal year is July 1 through June 30.

² Until fiscal year 2016, these agencies paid directly for agency-based services through the state's payroll system rather than to MN.IT through its billings process.

³ Until fiscal year 2016, MN.IT billed these agencies for agency-based services using predetermined billing rates.

⁴ During fiscal year 2015, MN.IT billed about \$9.2 million to some of these Other State Agencies using predetermined billing rates, and billed about \$1.7 million using actual payroll costs.

Source: The state's accounting system.

MN.IT used payroll data from the state's accounting system to prepare its monthly bills for agency-based services. Each monthly bill included actual payroll costs on a bi-weekly payroll period basis for MN.IT employees assigned to provide agency-based services to other departments. MN.IT billed for the biweekly payroll periods with the most days worked in a calendar month and generated the bill after the state had made the related payments to the employees.¹¹

State agencies determined the funding used to reimburse MN.IT for agency-based services. The funding could be from a variety of sources, including federal and state money legally restricted for specific program purposes. We did not test whether agencies paid for agency-based services with funding that corresponded to the services provided.

¹¹ For example, MN.IT included in its July 2015 bills for agency-based services paycheck dates July 24 and August 7, which reflect services for biweekly pay periods from July 1 through July 14 and July 15 through July 28. MN.IT billed for these July services after August 7, when the state paid employees for their work through July 28.

Objectives, Scope, and Methodology

For the period from July 2014 through March 2016, our audit of the Office of MN.IT Services' billings for agency-based information technology services focused on answering the following questions:

- Did the Office of MN.IT Services have adequate internal controls to ensure that it accurately billed state agencies for agency-based information technology services?
- Did the Office of MN.IT Services comply with the legal requirements we tested?

To meet the audit objectives, we gained an understanding of the Office of MN.IT Services' financial policies and procedures. We interviewed Office of MN.IT Services' management and staff to understand the differences among the different types of services MN.IT provides to state agencies. We gained an understanding of the processes MN.IT used to identify, summarize, and bill for payroll costs related to agency-based information technology services. We analyzed accounting data to identify unusual trends. We considered the risk of errors in the accounting records and potential noncompliance with relevant legal requirements.

We analyzed MN.IT's billing practices and tested the accuracy of MN.IT's bills. We examined payroll transactions on a sample basis and reviewed supporting documentation to test whether MN.IT's internal controls were effective and if the transactions complied with laws, regulations, and policies. In addition, we performed the following tests:

- **Security Access Test:** We tested whether MN.IT had appropriately limited its employees' access to the state's time reporting and payroll functions to the access needed for the employees' job duties. We also tested whether MN.IT had avoided assigning employees with incompatible security roles (roles that would allow an employee to initiate, authorize, and execute a payroll or human resources transaction without the involvement of others).
 - **Time Entry Test:** For the departments of Health, Human Services, and Transportation, we tested how MN.IT used the state's self service time entry system for employees providing agency-based services. We tested how MN.IT grouped employees and assigned primary and backup approvers for automated biweekly time reporting. We also tested how effectively MN.IT used self service time entry error reports to identify and follow-up on instances when time entry did not comply with the state's internal control expectations.
 - **Billing Accuracy Test:** For the departments of Health, Human Services, and Transportation, we tested whether MN.IT's billings corresponded to
-

the underlying actual payroll data for employees providing agency-based services.

We conducted the audit in accordance with generally accepted government auditing standards.¹² Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our conclusions based on our audit objectives.

We used various criteria to evaluate internal control and compliance. We used, as our criteria to evaluate MN.IT's controls, the guidance contained in the most recent edition of the internal control standards published by the U.S. Government Accountability Office.¹³ We used state laws, along with the policies and procedures established by the departments of Management and Budget and Administration and MN.IT's internal policies and procedures as evaluation criteria over compliance.

Conclusion

The Office of MN.IT Services had adequate internal controls to ensure it accurately billed other state agencies for payroll costs related to agency-based information technology services. The office also paid those employees in accordance with management's authorizations, bargaining agreements, and other personnel and payroll related legal requirements we tested.

¹² Comptroller General of the United States, Government Accountability Office, *Government Auditing Standards, 2011 Revision* (Washington D.C., December 2011).

¹³ Comptroller General of the United States, Government Accountability Office, *Standards for Internal Control in the Federal Government*, (Washington D.C., September 2014). In September 2014, the State of Minnesota adopted these standards as the internal control framework for the executive branch.



658 Cedar Street
St. Paul, MN 55155

December 5, 2016

Mr. James Nobles, Legislative Auditor
Minnesota Office of the Legislative Auditor
1st Floor, Centennial Building
658 Cedar Street
St. Paul, Minnesota 55155

Dear Mr. Nobles,

I would like to thank you and your staff for the work done on the audit of *Billings for Agency-Based Information Technology Services*. We appreciate the professionalism of your staff and the effort that they put forth on this engagement.

I am incredibly proud to receive an audit report with no findings or recommendations. It is important that customers of Minnesota IT Services feel confident in the billings for services that are delivered locally in their agencies, the subject of this report.

We also would like to emphasize our commitment to fully resolving other issues with rate-based services, brought to our attention during your January 2015 audit of *Billings for Shared Information Technology Services*. With our newly adopted two year rate package, we are happy to report that Minnesota IT Services now has a complete set of balanced rates that will accurately recover costs without any over or under recoveries.

Thank you once again for your office's commitment to improving state government.

Sincerely,

/s/ Thomas Baden

Thomas Baden
Commissioner and Chief Information Officer