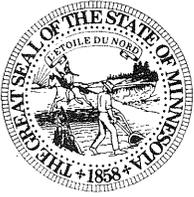

**STATEWIDE AUDIT
DEPARTMENT OF ENERGY AND
ECONOMIC DEVELOPMENT
MANAGEMENT LETTER
YEAR ENDED JUNE 30, 1985**

MARCH 1986

**Financial Audit Division
Office of the Legislative Auditor
State of Minnesota**



STATE OF MINNESOTA

OFFICE OF THE LEGISLATIVE AUDITOR

VETERANS SERVICE BUILDING, ST. PAUL, MN 55155 • 612/296-4708

JAMES R. NOBLES, LEGISLATIVE AUDITOR

Mr. Mark Dayton, Commissioner
Department of Energy and Economic Development
900 American Center Building
150 East Kellogg Blvd.
St. Paul, Minnesota 55101

Dear Commissioner Dayton:

We have reviewed certain accounting procedures and controls for your department as part of our statewide audit of the State of Minnesota's fiscal year 1985 financial statements and federal programs. The scope of our work has been limited to:

- those aspects of your department which have material impact on any of the state's various funds and account groups shown on the financial statements;
- the federal programs included in the Single Audit scope, specifically the Community Development Block Grant Program (CFDA #14.228) and the Energy Conservation-Institutional Buildings Program (CFDA #81.052); and
- the status of prior audit recommendations.

We emphasize that this has not been a complete financial and compliance audit of all programs within your department. However, we are in the process of completing a financial and compliance audit of your department and we will issue a report on that audit work in April 1986.

The Single Audit coverage satisfies the federal government's financial and compliance audit requirements for all federal programs administered by your department in fiscal year 1985. The federal government is ultimately responsible for determining resolution of Single Audit recommendations and the appropriate federal program agency will contact your agency to review your efforts toward corrective actions for 1985 and prior years. They will also notify you of their final resolution.

This management letter contains both the recommendations developed during this audit and a reiteration of a prior recommendation which has not yet been fully implemented. Attached to your management letter is a summary of the progress on all audit recommendations developed during our 1984 statewide audit.

The recommendations included in this letter are presented to assist you in improving accounting procedures and controls. Progress on implementing these recommendations will be reviewed during our audit next year.

The administration of subgrants awarded under the Community Development Block Grant Program (CFDA #14.228) should be improved.

DEED awards subgrants from the Community Development Block Grant (CDBG) Program to local units of government in the state. The funds are to be used to enhance local communities by providing decent housing, a suitable living environment, and expanding economic opportunities, principally for persons of low and moderate income. Our review of this program disclosed several areas of weakness, as follows:

- quarterly reports from subrecipients are not being received, properly reviewed, and maintained in the grant files;
- documentation for monitoring subrecipient performance is insufficient;
- DEED has not developed a system to require and monitor audits of subrecipients to ensure compliance with grant requirements; and
- DEED's refund procedures do not ensure compliance with cash management guidelines.

The grant agreements between the State of Minnesota and the local units of government require each subgrantee to submit quarterly reports to DEED within 25 days of the end of the quarter. Eleven of the 69 subgrants tested were missing at least one of the required quarterly reports. DEED began logging in subrecipient reports in 1985. However, procedures were not developed to prevent payments to subrecipients delinquent in reporting requirements. Additionally, documentation was not available to indicate that reports were reviewed as received. A monitoring system to withhold payments to subrecipients delinquent in reporting requirements and to ensure that quarterly reports are reviewed for reasonableness should be developed.

DEED is required to complete reviews and require audits of the local units of government as may be necessary or appropriate to determine whether subgrantees have satisfied the applicable performance criteria. DEED does complete several types of reviews to satisfy this requirement, such as technical assistance visits, desk reviews and on-sight monitoring. However, a systematic method of identifying the grants scheduled for the various types of review has not been developed. We also found inconsistent documentation for the visits completed. Proper documentation should include a schedule of visits, a description of what was reviewed, any problems noted, and how the problems will be resolved.

DEED is responsible for ensuring that required audits of subrecipients are completed. In addition, they are responsible to resolve any procedural findings or questioned costs identified in the various subrecipient audit reports. The specific audit requirements have changed in recent years. Following passage of the Single Audit Act of 1984 (P.L. 98-502), subrecipients who receive total direct and indirect federal assistance of \$100,000 or more per year are required to obtain an annual financial and compliance

audit made in accordance with the Act and with Office of Management and Budget (OMB) Circular A-128. Subrecipients who receive between \$25,000 and \$100,000 per year are required to obtain either an audit made in accordance with the Single Audit guidelines or a financial and compliance audit of all federal funds. DEED has not notified all subrecipients of these audit requirements.

Prior to the passage of the Single Audit Act, CDBG subgrantees were required to have an audit at least once every two years, as specified in the Minnesota Small Cities Development Program Manual. The two-year period began with the grant period start date stated in the grant agreement and the audit reports were to be submitted to DEED within 120 days of the two-year period. We found that 18 of the 30 tested grants, with start dates prior to or on July 1, 1983, did not have an audit report on file as of November 19, 1985. Furthermore, we found no plan to monitor the submission of audit reports.

Occasionally subrecipients will return federal funds to DEED. Rather than returning the monies to the U. S. Department of Housing and Urban Development (HUD), DEED reduces its subsequent requests for federal funds by the amount of any refunds received. Normally, refunds are less than DEED's next federal drawdown of funds. On December 26, 1984, a subrecipient returned \$123,906 of federal monies to DEED. On February 21, 1985, \$9,138 of the refund remained on hand. U.S. Treasury Circular 1075 establishes guidelines for requesting federal funds. The circular does not specifically indicate how refunds are to be treated. However, it does provide that the amount of cash on hand should be limited to immediate cash needs. In many cases it will be administratively easier and more efficient for DEED to retain the refunded monies and reduce future drawdowns. However, if many larger refunds are received, it may be more appropriate to return the funds to HUD. DEED should work with HUD to establish formal procedures for handling refunds to ensure compliance with U.S. Treasury Circular 1075.

In September 1985, the HUD Minneapolis-St. Paul Regional Office issued a report on problems found during their review of the State's CDBG program. They also found that DEED had inadequate documentation for monitoring reviews completed, had no organized or systematic method to select recipients for review, conducted an insufficient number of monitoring visits, and had no audit management system.

In October 1985 DEED began working on the development of compliance monitoring forms, correspondence procedures, and a monitoring plan. These will be incorporated into a procedures handbook covering all aspects of the program. When completed, these items should help to reduce the problems cited in our review of subgrants for fiscal year 1985.

RECOMMENDATIONS:

1. *DEED should develop procedures to ensure timely submission and review of quarterly reports and should withhold payments to subrecipients who do not comply with reporting requirements.*

Mr. Mark Dayton, Commissioner

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2. DEED should continue to develop procedures to ensure that adequate documentation is maintained for all reviews or monitoring visits completed.
3. DEED should inform all subrecipients of the requirements of the Single Audit Act of 1984 and should develop a system to monitor compliance with these requirements and to resolve any audit findings.
4. DEED should work with the U.S. Department of Housing and Urban Development to develop appropriate procedures for processing subrecipient refunds.

Ineligible insurance costs were paid from the Energy Conservation Institutional Buildings grant funds.

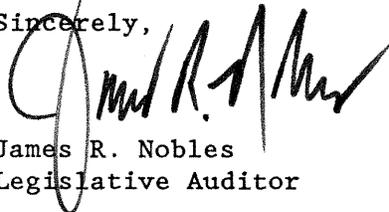
DEED receives an administrative grant from the U.S. Department of Energy to administer the Energy Conservation Institutional Buildings Grant Program (CFDA #81.052). DEED processes applications, makes recommendations and monitors grantee compliance. The department occasionally hires emergency employees (who may be appointed for up to 60 days) to meet processing requirements during peak work periods in the grant program. Although emergency employees are not eligible for insurance benefits, during fiscal year 1985, an insurance payment of \$39.88 was made with federal funds for one of these employees.

RECOMMENDATION:

5. DEED should work with the Department of Finance to recover the inappropriate insurance payment.

Thank you for the cooperation extended our staff during this audit.

Sincerely,


James R. Nobles
Legislative Auditor


John Asmussen, CPA
Deputy Legislative Auditor

Attachment

February 24, 1986

DEPARTMENT OF ENERGY AND ECONOMIC DEVELOPMENT

Attachment

STATUS OF PRIOR AUDIT RECOMMENDATIONS
AND

PROGRESS TOWARD IMPLEMENTATION

The indirect cost rate applied to the Community Development Block Grant was not based on total departmental costs.

1. DEED should work with the U.S. Department of Housing and Urban Development to determine whether the recovery of \$33,601 for fiscal year 1984 indirect costs were appropriate.

Recommendation Implemented. In August 1985, HUD reviewed the 1985 Indirect Cost Plan and concluded that all necessary adjustments had been made concerning the questioned costs.

Quarterly progress reports from recipients of Community Block Grant subgrants are not being received, properly recorded, and maintained in the grant files.

2. DEED personnel should continue to develop procedures to ensure the timely submission of quarterly reports.

RECOMMENDATION NOT IMPLEMENTED. See current recommendation #1.

Payments to subgrantees are being made before environmental clearance has been given.

3. DEED should not authorize subgrant payments until the environmental clearance has been granted, unless the costs have been documented to be exempt.

Recommendation Implemented. Current year testing concluded that all payments made prior to environmental clearance were for exempt costs. The U. S. Department of Housing and Urban Development in October 1985 identified this issue as resolved.

Questioned costs have not been resolved for certain Land and Water Conservation (LAWCON) subgrants.

4. DEED should recover any excess state match amount which might arise from the resolution of the federal questioned costs.

Recommendation Implemented. The department contacted all subrecipients with questioned costs and either received additional documentation for the items questioned or requested the appropriate refund. This implementation has not received final acceptance by the appropriate federal agency.

DEPARTMENT OF ENERGY AND ECONOMIC DEVELOPMENT

Attachment

Page 2

The Statewide Accounting System (SWA) general ledger has not been updated for the DEED Rural Rehabilitation and Minnesota Energy and Economic Development Authority (MEEDA) loans receivable.

5. DEED should work with the Department of Finance to properly update the SWA general ledger for activity in the Rural Rehabilitation and Minnesota Energy and Economic Development Authority (MEEDA) loan programs.

Recommendation Implemented.



MINNESOTA Department of Energy and Economic Development

Office of the Commissioner
(612) 296-6424

900 American Center
150 East Kellogg Boulevard
St. Paul, Minnesota 55101

February 24, 1986

Mr. James R. Nobles
Legislative Auditor
Office of the Legislative Auditor
Veteran's Service Building
St. Paul, MN 55155

**RE: Response to Draft OLA Audit Letter for the Community Development Block
Grant Program Administration**

Dear Mr. Nobles:

The purpose of this letter is to provide you with a response to your recent draft letter regarding DEED's administration of the Community Development Block Grant Program. Specifically, your letter provided four recommendations for improving program administration. For your convenience, I will respond to your recommendations in the order in which they were given.

1. DEED should develop procedures to ensure timely submission and review of quarterly reports from subrecipients.

DEED is currently contracting with SMR Computer consulting firm to develop a grants management software package. One of the vital components of the workplan is to develop a computerized procedure for tracking a variety of monitoring requirements, including quarterly reports. Specifically, the quarterly report component will work as follows: upon grant approval, specific quarterly report dates will be entered into the computer for each grant. Prior to the quarterly report receipt dates, the computer will automatically generate a letter to the grantees, reminding them of their quarterly report responsibilities. If, by the quarterly report due date, the computer does not show an entry that indicates a quarterly report has been received and reviewed, it will automatically generate an exception report, which will identify delinquent reporting and report review. This will provide DEED management with two things. First, we will know which grantees are not complying with quarterly report requirements. Secondly, we will know which CD reps have fallen behind in quarterly report reviews. Thus, the system should provide DEED management with the necessary information to ensure that we meet quarterly reporting requirements.

2. DEED should continue to develop procedures to ensure that adequate documentation is maintained for all reviews or monitoring visits completed.

There are two techniques which DEED is initiating to assure the maintenance

AN EQUAL OPPORTUNITY EMPLOYER



of adequate review or monitoring documentation. First, in regard to monitoring, DEED has developed a draft monitoring plan which staff intends to implement immediately. The plan addresses the method of selection of projects to be monitored and the necessary forms, checklists, and reports to document monitoring visits. Findings resulting from monitoring visits will be entered into the computer system being developed by SMR and will be tracked in much the same manner as quarterly reports. Secondly, DEED staff has previously been in the habit of maintaining "desk" project files and "master" project files. This system has occasionally resulted in the placement of vital documents in desk files, rather than the master file. The concept of two project files for each project has been officially eliminated. All appropriate documents will be placed in the central file area (formerly the "master file"). Duplicative desk files are being discouraged. In addition, individual CD reps are now responsible for the contents of all the grant files in their assigned areas of the State. Thus, the combination of a specific monitoring system and improved internal file maintenance should substantially reduce any documentation deficiencies.

3. **DEED should inform all subrecipients of the requirements of the Single Audit Act of 1984 and should develop a system to review the Single Audit reports and resolve any audit findings.**

OLA staff orally reviewed this matter with DEED staff. Since those discussions, DEED has mailed (2-6-86) a copy of OMB Circular A-128 to each FY'83 and '84 grantee. DEED distributed A-128 to each FY'85 grant recipient at the grant management workshop. Consequently, every SCDP recipient now has a copy of OMB Circular A-128. In addition, audit report review and finding resolution procedures will be incorporated in the financial management section of the draft monitoring plan and into the computer grants management software.

4. **DEED should work with the U.S. Department of Housing and Urban Development to develop appropriate procedures for processing subrecipient refunds.**

DEED staff has made initial contact with HUD staff on this issue. If possible, a formal, written procedure will be developed, implemented, and forwarded to you upon completion.

DEED has attempted to sincerely address each of your recommendations. In some instances, we began addressing your recommendations before they arrived in written form. I have not appended attachments to this letter; but, if you wish, we could provide additional copies of:

1. The Draft Monitoring Plan
2. Draft computer grants management software package (when completed)
3. The February 6, 1986 letter from Louis F. Jambois to all SCDP grant recipients, enclosing OMB Circular A-128 requirements.
4. The mailing list used to send A-128.

February 24, 1986

Of course, we have developed a file which includes all of the material identified above, as well as your draft management letter.

We would be happy to show you the progress we've made. We intend to continue to improve SCDP management. If you have any questions or need additional information, please contact Mr. Robert F. Benner, Deputy Commissioner, Community Development Division, at (612) 297-2515.

With best regards.

Sincerely,

A handwritten signature in black ink, appearing to read "Mark B. Dayton". The signature is written in a cursive, somewhat stylized font. It starts with a large, sweeping "M" and ends with a long, horizontal flourish.

Mark B. Dayton
Commissioner

/pb
III/91-1