

**DEPARTMENT OF EDUCATION
FINANCIAL AUDIT
FOR THE YEAR ENDED JUNE 30, 1991**

APRIL 1992

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

SUMMARY

State of Minnesota
Office of the Legislative Auditor
Centennial Office Building • St. Paul, MN 55155
612/296-4708

DEPARTMENT OF EDUCATION

FINANCIAL AUDIT FOR THE YEAR ENDED JUNE 30, 1991

Public Release Date: April 3, 1992

No. 92-21

OBJECTIVES:

- EVALUATE INTERNAL CONTROL STRUCTURE: Policies and procedures for the distribution of various state and federal grants.
- TEST COMPLIANCE WITH CERTAIN FINANCE-RELATED LEGAL PROVISIONS.

CONCLUSIONS:

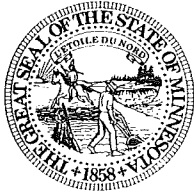
We found two areas where the internal control structure needed improvement:

- The department does not keep the original media supporting the bank transfer of funds to the local schools for state aids.
- The department needs to improve the monitoring system of school district single audit reports to ensure proper resolution of federal audit findings.

We found two areas where the department had not complied with finance-related legal provisions:

- The department does not properly calculate special education reimbursements to school districts for contracted services.
- The department has not filed financial status reports timely for its federal programs.

Contact the Financial Audit Division for additional information.
(612) 296-1730



STATE OF MINNESOTA

OFFICE OF THE LEGISLATIVE AUDITOR

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

JAMES R. NOBLES, LEGISLATIVE AUDITOR

Representative Ann Rest, Chair
Legislative Audit Commission

Members of the Legislative Audit Commission

Mr. Tom Lindquist, Chair
State Board of Education

Mr. Eugene Mammenga, Commissioner
Department of Education

Audit Scope

We have conducted a financial related audit of the Minnesota Department of Education as of and for the fiscal year ended June 30, 1991. Our audit was limited to only that portion of the State of Minnesota financial activities attributable to the transactions of the Minnesota Department of Education. We have also made a study and evaluation of the internal control structure of the Minnesota Department of Education in effect at June 30, 1991.

We conducted our audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial activities attributable to the transactions of the Minnesota Department of Education are free of material misstatements.

As part of our study and evaluation of the internal control structure, we performed tests of the Minnesota Department of Education's compliance with certain provisions of laws, regulations, and grants. However, our objective was not to provide an opinion on overall compliance with such provisions.

Management Responsibilities

The management of the Minnesota Department of Education is responsible for establishing and maintaining an internal control structure. This responsibility includes compliance with applicable laws, regulations, contracts, and grants. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control structure policies and procedures. The objectives of an internal control structure are to provide management with reasonable, but not absolute, assurance that:

- assets are safeguarded against loss from unauthorized use or disposition;
- transactions are executed in accordance with applicable legal and regulatory provisions, as well as management's authorization; and
- transactions are recorded properly on the statewide accounting system in accordance with Department of Finance policies and procedures.

Due to inherent limitations in any internal control structure, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of the structure to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

Internal Control Structure

For purposes of this report, we have classified the significant internal control structure policies and procedures in the following categories:

State Programs:

- General Education Aid
- Capital Expenditures Facilities Aid
- Disparity Reduction Aid
- Homestead and Agriculture Aid
- School Endowment Fund Apportionment Aid
- Special Education Aid - Regular
- Transportation Aid - Regular

Federal Programs:

- Food Distribution (CFDA #10.550)
- National School Lunch Program (CFDA #10.555)
- Child Care Food Program (CFDA #10.558)
- Educationally Deprived Children (CFDA #84.010)
- Handicapped State Grants (CFDA #84.027)
- Educational Improvement Partnerships (CFDA #84.151)

For all of the internal control structure categories and programs listed above, we obtained an understanding of the design of relevant policies and procedures and whether they have been placed in operation, and we assessed control risk.

Representative Ann Rest, Chair
Members of the Legislative Audit Commission
Mr. Tom Lindquist, Chair
Mr. Eugene Mammenga, Commissioner
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Conclusions

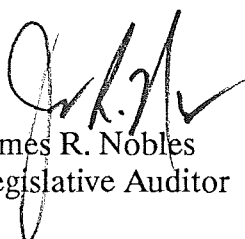
Our study and evaluation disclosed the conditions discussed in findings 1 and 2 involving the internal control structure of the Minnesota Department of Education. We consider this condition to be a reportable condition under standards established by the American Institute of Certified Public Accountants. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control structure that, in our judgment, could adversely affect the entity's ability to record, process, summarize, and report financial data.

A material weakness is a reportable condition in which the design or operation of the specific internal control structure elements does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to the financial activities being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We do not believe the reportable conditions described above are material weaknesses.

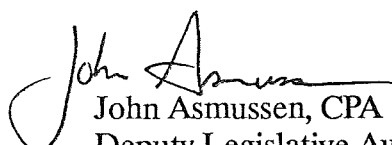
The results of our tests indicate that, with respect to the items tested, except for findings 2 to 4, the Minnesota Department of Education complied, in all material respects, with the provisions referred to in the audit scope paragraphs. With respect to items not tested, nothing came to our attention that caused us to believe that the Minnesota Department of Education had not complied, in all material respects, with those provisions.

This report is intended for the information of the Legislative Audit Commission and management of the Minnesota Department of Education. This restriction is not intended to limit the distribution of this report, which was released as a public document on April 3, 1992.

We thank the Department of Education staff for their cooperation during this audit.



James R. Nobles
Legislative Auditor



John Asmussen, CPA
Deputy Legislative Auditor

End of Fieldwork: January 10, 1992

Report Signed On: March 27, 1992

Department of Education

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Audit Participation

The following staff from the Office of the Legislative Auditor prepared the report:

John Asmussen, CPA	Deputy Legislative Auditor
Renee Redmer, LPA	Audit Manager
Cecile Ferkul, CPA	Audit Supervisor
Sonya Hill	Audit Staff
Rhonda Regnier, CPA	Audit Staff
Karen Klein	Audit Staff
Rubin Perelman	Intern

Exit Conference

The findings and recommendations in this report were discussed with the following staff of the Department of Education on February 4, 1992:

Eugene Mammenga	Commissioner
Joyce Krupey	Assistant Commissioner
Wayne Erickson	Manager, Special Education
Ed Wilkins	Director, Fiscal Services
Gary Farland	Director, Education Finance and Analysis
Margaret Drey	Director, Child Nutrition
Don Pfiffner	Supervisor, Education Budgeting and Payments
Bob Fischer	Supervisor, Special Education
Audrey Bomstad	Specialist, IDEAS Payments and Reporting
Steve Sandberg	UFARS, Reporting and Auditing

Department of Education

Introduction

The mission of the Minnesota Department of Education is to provide leadership, service, and regulation to maintain and improve an equitable, accessible, and quality system of public education for all learners. The department's functions include:

- developing, modifying, initiating, and recommending educational policies;
- improving the management of educational programs and services at state, regional, and local levels; and
- assisting local school districts in assessing educational needs, planning and restructuring programs and services, and evaluating the effectiveness of programs.

The Commissioner, Mr. Eugene Mammenga, is the administrative head of the Department of Education. The 1991 Legislature cut the department's operating budget by 20 percent for the 1992-93 biennium. The cut will eliminate 80 jobs, nearly one-third of the department's employees.

Departmental activities are financed mainly by General Fund appropriations and federal grants. The department also administers the Maximum Effort School Loan Fund which had loans receivable at June 30, 1991 totalling \$42,332,000 as shown in Minnesota's Comprehensive Annual Financial Report. Fiscal year 1991 expenditures categorized by state and federal programs are shown below. Major federal financial assistance programs, including state matching expenditures, are shown by Catalog of Federal Domestic Assistance Number (CFDA). The amount shown for Food Distribution (CFDA 10.550) is the value of commodities distributed to local schools.

Department of Education

State Programs:(1)

General Education Aid	\$1,562,980,071
Capital Expenditures Facilities Aid	67,636,541
Disparity Reduction Aid	13,782,911
Homestead and Agriculture Credit Aid	191,254,526
School Endowment Fund Apportionment Aid	31,179,045
Special Education Aid - Regular	154,319,639
Transportation Aid - Regular	114,848,598
Other State Programs	163,425,165

Federal Programs:(2)

Food Distribution (CFDA #10.550)	14,298,601
National School Lunch Program (CFDA #10.555)	49,951,336
Child Care Food Program (CFDA #10.558)	43,544,149
Educationally Deprived Children (CFDA #84.010)	51,453,751
Handicapped State Grants (CFDA #84.027)	38,915,742
Educational Improvement Partnerships (CFDA #84.151)	5,284,807
Nonmajor Federal Programs	<u>32,460,594</u>

Total Departmental Expenditures	<u>\$2,535,335,476</u>
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Sources: (1) The state program amounts are budgetary basis expenditures recorded on the Statewide Accounting System as of August 31, 1991.

(2) The federal programs are from Minnesota's Financial and Compliance Report on Federally Assisted Programs.

Current Findings and Recommendations

1. The Department of Education does not retain detailed records supporting state aid payments made to local school accounts via bank transfers.

The Department of Education does not keep the original media supporting the bank transfer of funds to the local schools for state aids. After the bank transfers the funds to the local school accounts, the department reuses the tapes and destroys the original record of the bank transactions. It is important that the department maintain the original media supporting the transfer of funds to resolve any questions or discrepancies that may arise. The department also does not list the computer magnetic tapes that support payments to the schools on its records retention plan.

In April 1991, the department began to pay state aids to local schools by using the automated clearing house (ACH) process. This process makes transfers to school accounts through the federal reserve system. The department generates the transfer data semi-monthly on a computer magnetic tape. A local bank uses the tapes to process the state aid payments to the schools. The information is summarized and recorded in the statewide accounting system. After the bank processes the transfer of funds to the respective school bank accounts, the tapes are returned to the department. The tapes are the only detailed record of the actual bank transactions. The computer magnetic tapes supporting the bank transfers provide an audit trail of aid payments made to the schools. The tapes also provide a means for the department to detect and investigate discrepancies in aid payments to the schools. The department should maintain the magnetic tapes or transfer the data to another storage media.

The department does not have the authority to destroy records without the approval of the state's record disposition panel. Minn. Stat. Section 138.17 provides for the retention and disposal of all government records regardless of storage media. This statute requires approval by the record disposition panel prior to the disposal of records. The Department of Education should include record retention procedures for the magnetic tapes, or propose another storage media and obtain approval from the state's record retention panel.

Recommendations

- *The Department of Education should retain the magnetic bank transaction tapes supporting aid payments to schools, or transfer the data to another storage media.*
- *The department should include the computer magnetic tapes for the ACH process and other storage media on its record retention plan.*

Department of Education

2. The department needs to improve the monitoring system of school district single audit reports to ensure proper resolution of federal audit findings.

The Education Finance and Analysis Unit does not properly monitor the resolution of school district single audit issues. Other department program officials resolve questioned costs and other subrecipient findings. The Education Finance and Analysis Unit is mainly responsible to resolve cross-cutting findings in school district audit reports. However, the unit does not ensure that corrective actions are taken by the school districts within six months after receipt of the audit reports. Therefore, the department is not in compliance with the provisions of the Single Audit Act governing the resolution of subrecipient audit findings.

The Education Finance and Analysis Unit has not determined resolution of some cross-cutting findings in school district reports for the year ended June 30, 1990. For 1990, the unit sent an initial letter to the respective schools highlighting the issues as identified in the single audit reports. However, after the initial correspondence, the unit did not follow-up with the school districts to ensure that the proper corrective actions were taken to resolve the cross-cutting audit issues.

Our review of the unit's monitoring system showed that the system was incomplete and that audit issues are not resolved on a timely basis. Of eight school district reports reviewed for 1990 with audit issues, the unit began correspondence with five school districts after the six months allowed to resolve issues. For two of the eight districts reviewed, we found no documentation showing that the districts corrected the issues. In addition, for the eight districts, no evidence exists of the unit's conclusion on whether the corrective action taken by the districts was appropriate.

The U. S. Office of Management and Budget Circular A-128 requires each state to review the subrecipients' audit reports and identify report issues pertaining to federal financial assistance passed through to the subrecipients. Part 9(c) of the Circular requires that states verify that corrective action is taken on instances of material noncompliance with applicable laws and regulations within six months after receipt of the audit report. Without a proper and timely monitoring system, the department cannot ensure proper use of federal funds subgranted to the school districts.

Recommendations

- *The department should improve the subrecipient monitoring system to ensure that school district cross-cutting audit issues are resolved.*
- *The department should ensure and document that proper corrective actions are taken by the schools within six months after receiving the audit reports.*

Department of Education

3. The department does not properly calculate reimbursements to school districts for contracted services.

The Special Education Information Technology and Aids Unit reimburses some school districts a larger share of contracted services than allowed by statute. Minn. Stat. Section 124.32, Subd. 1(d), states that:

“for special instruction and services provided to any pupil by contracting for services with public, private, or voluntary agencies other than school districts, the state shall pay each district 52 percent of the difference between the amount of the contract and the basic revenue of the district for that pupil for the amount of time the pupil receives services under the contract.”

In many cases the unit properly reimburses schools for contract services. However, when the students receive the services on school premises or in addition to their regular school program, the unit does not deduct the amount of basic revenue. Nine of 15 school districts reviewed had contracts for special services in fiscal year 1990-1991 which the unit reimbursed at 52 percent. For example, the unit paid the Minneapolis school district \$188,804 for contract services without a general revenue reduction. Because of many variables involved, we could not calculate the exact amount overpaid to the Minneapolis district.

The department acknowledges that it calculates contractual service reimbursements differently than authorized by statute. However, the department believes its calculation is a more equitable approach than provided by the existing law. As a result, it intends to seek a statutory change to the reimbursement formula.

Recommendation

- *The department should comply with Minn. Stat. Section 124.32, Subd. 1(d) or obtain a statutory amendment to the reimbursement formula.*

4. The department has not filed financial status reports timely for its federal programs.

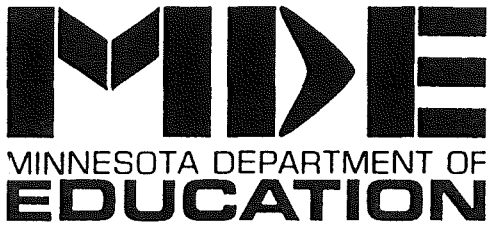
The department has not filed many of the required financial status reports for its federal programs for the years ended June 30, 1989, 1990 and 1991. The program staff rely on the Fiscal Services Unit to prepare these federal reports. However, in many cases, the reports have not been prepared. In other cases, the reports have been filed late. 34 CFR, Subtitle A, Part 74, Subpart I, 74.70 states that, “the financial status report is due 90 days after the grant year and final reports are due 90 days after expiration or termination of grant support.”

Department of Education

The Fiscal Services Unit has not filed final reports for five of 26 required programs for fiscal year 1989. Preliminary reports were filed for these programs; however, final reports with actual data have not been filed. For fiscal year 1990 only preliminary reports were filed for 21 programs. The unit has not submitted the final reports for these programs. The unit has not filed either preliminary or final financial status reports for its programs for the 1991 fiscal year.

Recommendation

- *The department should file the financial status reports with the federal government within the proper timeframes.*



Capitol Square 550 Cedar Street
Saint Paul, Minnesota 55101 612/296-6104

March 24, 1992


Mr. James R. Nobles, Legislative Auditor
Centennial Building
St. Paul, MN 55155

Dear Mr. Nobles:

Enclosed are responses to the four findings and recommendations from the Fiscal Year 1990-91 statewide financial audit. We are in basic agreement with findings numbered 1, 2, and 4 and as we have indicated in our response sheets, changes to bring us into full compliance should occur no later than September 30, 1992. Finding number 3 dealing with reimbursement for certain Special Education contracted services needs a statutory amendment which we expect to receive in the 1993 session.

If there are questions or items needing clarification, please contact Ed Wilkins in our Fiscal Services Section or other staff members identified in our response who are responsible for implementation.

Sincerely,


Gene Mammenga
Commissioner of Education

GM/EW:mpb

Enclosures



March 11, 1992

DEPARTMENT OF EDUCATION
Draft Audit Report, Period Ending June 30, 1991

Finding: 1. The Department of Education does not retain detailed records supporting state aid payments made to local school accounts via bank transfers.

Recommendation:

- The Department of Education should retain the magnetic bank transaction tapes supporting aid payments to schools, or transfer the data to another storage media.
- The department should include the computer magnetic tapes for the ACH process and other storage media on its record retention plan.

DEPARTMENT OF EDUCATION RESPONSE

Department Agrees/Disagrees with Finding: Agrees

Person Responsible for Implementation: Audrey Bomstad

Projected Completion Date: July 1992

Department Comments/Corrective Action:

Beginning in April 1991, we have generated a computer report of the detailed payment data by school district from the magnetic transaction tape used to process state aid payments to districts. These reports were intended to satisfy the need for resolving issues, providing an audit trail, and retaining records. The audit finding is that the generated computer report does not meet the standards for retaining the original record of payments processed.

For fiscal year 1992, we will retain the magnetic tapes that are available. An alternative method of data storage will be used beginning with the fiscal year beginning July 1, 1992. The method will likely be to transfer the payment transaction data, from the same computerized payment system data file that is the basis for the magnetic tape, to a computer diskette. This will have the advantage of providing the capability for duplicate storage at more than one site.

We also will proceed to adjust our records retention plan for the use of the computer diskette storage method within the criteria and other requirements for records retention.

March 11, 1992

DEPARTMENT OF EDUCATION
Draft Audit Report, Period Ending June 30, 1991

Finding: 2. The department needs to improve the monitoring system of school district single audit reports to ensure proper resolution of federal audit findings.

Recommendation:

- The department should improve the subrecipient monitoring system to ensure that school district cross-cutting audit issues are resolved.
- The department should ensure and document that proper corrective actions are taken by the schools within six months after receiving the audit reports.

DEPARTMENT OF EDUCATION RESPONSE

Department Agrees/Disagrees with Finding: Agrees

Person Responsible for Implementation: Steve Sandberg

Projected Completion Date: June 30, 1992 and each June 30 thereafter

Department Comments/Corrective Action:

Additional clerical support staff time will be used to improve the efficiency and effectiveness of the monitoring procedures and of the professional staff person assigned the responsibility for monitoring the resolution of school district single audit issues. The support person will maintain a database for audit findings and responses, and assist with follow-up activities.

For unresolved issues relating to the year ended June 30, 1990, a follow-up procedure will occur resulting in a) documentation that the districts have corrected the issues and b) evidence from our review that the corrective action taken is appropriate. This will occur as soon as possible with a target date of June 30, 1992 for completion.

For the monitoring process to be used for the year ended June 30, 1991 and thereafter, the improved clerical and monitoring procedures will be in place beginning April 1, 1992. The intended result is for resolution of all single audit issues to occur within six months of the December 31 statutory date for submission of the audit reports, i.e., by June 30, 1992 and each June 30 thereafter.

March 11, 1992

DEPARTMENT OF EDUCATION
Draft Audit Report, Period Ending June 30, 1991

Finding: 3. The department does not properly calculate reimbursements to school districts for contracted services.

Recommendation:

- *The department should comply with Minn. Stat. Section 124.32, Subd. 1(d) or obtain a statutory amendment to the reimbursement formula.*

DEPARTMENT OF EDUCATION RESPONSE

Department Agrees/Disagrees with Finding: Disagrees

Person Responsible for Implementation: Robert H. Fischer

Projected Completion Date: July 1, 1993, based on action of the legislature

Department Comments/Corrective Action:

The legislative auditors recommended the department seek an attorney general's opinion in regard to the issues regarding calculation of contracted services aid in special education. Initially, we understood that the legislative auditor would abide by the attorney general's opinion. Apparently, the auditors still feel the statute is sufficiently ambiguous to require a change in language.


The department proposes that aids be calculated as they have for the past 15 years for 1991-92 and 1992-93. The department will seek a legislative change to clarify the language in this area in the 1993 legislative session. The department agrees the contracted services area needs definition clarification.

We would ask the legislative auditors' office to not require we change established practice, based on the attorney's opinion, until the department has an opportunity to seek legislative clarification in 1993.

MINNESOTA ATTORNEY GENERAL - Education

M E M O R A N D U M

TO : Robert Fischer
Special Education Information,
Technology and Aids Units
Minnesota Department of Education

FROM : Steven B. Liss 
Special Assistant
Attorney General

DATE : January 31, 1992

PHONE : 296-3304

SUBJECT : Special Education - Legislative Auditor

I am writing in response to your questions concerning several issues raised by the Legislative Auditor. As I understand, the Auditor has not yet issued the Audit Report.

1. Contract for Special Education Services.

Minnesota Statutes, section 124.32, subd. 1d., provides:

Subd. 1d. Contract services. For special instruction and services provided to any pupil by contracting with public, private, or voluntary agencies other than school districts, the state shall pay each district 52 percent of the difference between the amount of the contract and the basic revenue of the district for that pupil for the amount of time the pupil receives services under the contract.

As you have described the situation, there are instances when MDE pays the full 52 percent of cost without subtracting the basic revenue received by the district. This would occur where the

Robert Fischer
January 31, 1992
Page 2

district is providing the full educational program to the student, but contracts for additional services, such as an assessment or therapy after school. The auditor questioned whether the Department has the authority to avoid subtracting the basic revenue before reimbursing the district.

The language of the statute is ambiguous when applied to the instances you describe and, therefore, does not clearly answer the question. Thus, a definitive answer cannot be provided. It appears, however, that the Department's interpretation of the statute to permit payment of the full 52 percent for services that are provided outside of the school day is a reasonable one.

The statute provides that the Department shall subtract the basic revenue "for the amount of time the pupil received services under the contract." The school district, however, receives no basic revenue for time spent outside of the school day. Therefore, there is nothing to deduct in calculating the payment for services.

Section 124.32, subd. 1d. is arguably intended to prevent a school district from receiving double payment for the same period of time during the school day. Limiting the deduction to services performed during the school day would be consistent with this purpose. The Department's position is a long-standing departmental interpretation of the statute it administers. That interpretation is a reasonable one and entitled to some deference. There appears to be no reason that this policy cannot continue.

March 11, 1992

DEPARTMENT OF EDUCATION
Draft Audit Report, Period Ending June 30, 1991

Finding: 4. The department has not filed financial status reports timely for its federal programs.

Recommendation:

- The department should file the financial status reports with the federal government within the proper timeframes.

DEPARTMENT OF EDUCATION RESPONSE

Department Agrees/Disagrees with Finding: Agrees

Person Responsible for Implementation: Don Johnson

Projected Completion Date: September 30, 1992

Department Comments/Corrective Action:

The department's Fiscal Services Section has experienced difficulty completing financial status reports for the past year for many of the major federal programs. Availability of staff for this assignment has been a problem. In addition, there has been an increase in the number of internal and external reports required to provide cash management and necessary management reports.

A part-time accounting officer is being hired under an existing federal complement to complete the reporting responsibilities and other related duties. It is anticipated many of the reports will be completed in a matter of weeks and all reports will be current with the Fiscal Year 1992 reporting cycle.