Department of Finance

Financial Audit
For the Year Ended June 30, 1994

June 1995

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Financial Audit Division
Office of the Legislative Auditor
State of Minnesota

95-31

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Department of Finance

Financial Audit
For the Year Ended June 30, 1994

Public Release Date: June 28, 1995 No. 95-31

Objectives:

- Review Internal Control Structure: bond sales, debt service transfers, master lease draws and repayments, school energy loans, statewide indirect costs, and University of Minnesota grants.

- Test compliance with certain finance-related legal provisions.

Conclusions:

We found one area where the department's financial reporting process needed improvement:

- The state's financial statements contained a departure from generally accepted accounting principles because of difficulties in implementing a new standard.

We found no departures from finance-related legal provisions.

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

STATE OF MINNESOTA
OFFICE OF THE LEGISLATIVE AUDITOR
CENTENNIAL BUILDING, ST. PAUL, MN 55155 • 612/296-4708
JAMES R. NOBLES, LEGISLATIVE AUDITOR

Members of the Legislative Audit Commission

Ms. Laura King, Commissioner
Department of Finance

Audit Scope

We have completed a financial audit of the Department of Finance as of and for the year ended June 30, 1994. Our audit was limited to only that portion of the state of Minnesota's financial activities attributable to the transactions of the Department of Finance as outlined below and as further discussed in the Introduction Section.

We conducted our audit in accordance with generally accepted government auditing standards. Those standards require that we consider the internal control structure in order to plan our audit, and that we perform tests of the department's compliance with certain material provisions of laws, regulations, contracts, and grants. However, our objective was not to provide an opinion on the internal control structure or on overall compliance with finance-related legal provisions.

Internal Control Structure

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

- bond sales;
- debt service transfers;
- master lease draws and repayments;
- school energy loans;
- statewide indirect costs; and
- University of Minnesota transfers.

For the internal control structure categories 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.

In addition, the Department of Finance, along with other state agencies, provides centralized statewide controls in the following areas:

- statewide accounting system;
- budgets and appropriations;
- cash receipts and disbursements;
- payroll transaction processing;
- investment transaction accounting and investment income allocation; and
- general obligation bonded debt.

As a part of our audit, we reviewed selected controls for the areas listed above.

Management Responsibilities

The management of the Department of Finance is responsible for establishing and maintaining an internal control structure. This responsibility includes compliance with applicable laws and regulations. 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.

Because of 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.

Conclusions

The results of our tests indicated that, with respect to the items tested, the Department of Finance 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 Department of Finance had not complied, in all material respects, with those provisions.

Finding 1 discusses improvements needed in the Department of Finance's financial reporting process.

We also noted certain other matters involving the internal control structure and its operations that we reported to management of the Department of Finance at an exit conference held on June 2, 1995.

This report is intended for the information of the Legislative Audit Commission and management of the Department of Finance. This restriction is not intended to limit the distribution of this report, which was released as a public document on June 28, 1995.

We thank the Department of Finance's staff for their cooperation during this audit.

James R. Nobles
Legislative Auditor

John Asmussen, CPA
Deputy Legislative Auditor

End of Fieldwork: February 10, 1995

Report Signed On: June 20, 1995

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Audit Participation

The following members of the Office of the Legislative Auditor prepared this report:

John Asmussen, CPA	Deputy Legislative Auditor
Claudia Gudvangen, CPA	Audit Manager
Cecile Ferkul, CPA	Auditor-in-Charge
Gail Thurmer, CISA	Staff Auditor
Karen Klein, CPA	Staff Auditor
Rhonda Regnier, CPA	Staff Auditor
Christina Weiss	Staff Auditor
Laura Puig-White	Staff Auditor
Marina Mirman	Staff Auditor
Steve Johnson	Intern

Exit Conference

We discussed the results of our audit with the following officials of the Department of Finance at an exit conference held on June 2, 1995:

Laura M. King	Commissioner
Rosalie Greeman	Assistant Commissioner
Margaret Jenniges	Director of Financial Reporting

Introduction

The Department of Finance manages the accounting, budgetary, and debt management activities of the state. It establishes policies and procedures for state agencies to follow to ensure consistent and reliable financial data and compliance with statutory provisions. The department maintains the state's accounting system and monitors controls to prevent unauthorized transactions.

The Commissioner of Finance, appointed by the Governor, directs the operations of the department. Following John Gunyou's resignation in October 1994, Laura King was appointed commissioner. The department primarily receives General Fund appropriations to finance its operations. For fiscal year 1994, departmental administrative expenditures totaled $18,815,278, which included $10,012,918 for the Statewide Systems Project, discussed below.

Major functions of the Department of Finance during fiscal year 1994 included the following:

- The financial reporting unit coordinates preparation of the State's Comprehensive Annual Financial Report, the Comparison of Budget and Actual Revenue, Expenditures and Changes in Funds Balance, and the reports required by the Single Audit Act relating to the receipt and expenditure of federal funds.

- The budget services division coordinates preparation of the governor's biennial budget. The budget outlines past spending on a program basis, and proposes the future roles and responsibilities of state government.

- The department, in conjunction with the Departments of Administration and Employee Relations, has coordinated the replacement of the state's computerized accounting, payroll, personnel, procurement, and information access systems. The legislature appropriated $17,100,000 for fiscal years 1992 through 1994, with an additional $14,600,000 appropriated for fiscal year 1995. The Department of Finance also obtained $537,633 in fiscal year 1993 and $650,000 in 1995 through interagency agreements with seven state agencies, and transferred $359,876 from its own departmental appropriations for the project. Thus, funds available for the systems project totaled $33,247,509 as of December 31, 1994. The accounting and procurement components of the new system (MAPS) began functioning for budgetary and contracting purposes on April 3, 1995. MAPS will be fully operational on July 1, 1995. The payroll and human resource components (SEMA4) will be phased in after that date.

Department of Finance

- The cash and debt management division coordinates the sale of state general obligation bonds, used mainly to finance state building construction and repair. In fiscal year 1994, the Department of Finance issued bonds totaling $483,555,000, including $273,555,000 to refinance outstanding bonds originally issued at higher interest rates. The division also calculates constitutionally and statutorally required transfers to the Debt Service Fund to accumulate funds for repayment of the general obligation bonds. Transfers, and related deposits, totaled $268,537,000 in fiscal year 1994.

- The cash and debt management division also consolidates lease purchases under the master lease program. Master lease draw downs in fiscal year 1994 were $15,127,222. The Department of Administration uses the master lease program mainly to purchase computer equipment and motor pool vehicles.

- The accounting services division transfers appropriated funds to the University of Minnesota. General Fund transfers to the University for fiscal year 1994 totaled $444,966,000. In addition, the University received $12,552,260 during fiscal year 1994 from bond proceeds for various capital construction projects. There were also some transfers for other smaller projects and programs.

- The budget services division also allocates and collects statewide indirect costs. This helps ensure that a program's expenditure base includes all operating costs and, where possible, allows for recovery of those costs from the federal government or through user fees. In fiscal year 1994, agencies reimbursed $9,701,891 to the General Fund.

Current Finding and Recommendation

1. The state's financial statements contained a departure from generally accepted accounting principles because of difficulties in implementing a new standard.

The Department of Finance received a qualified audit opinion on its financial statements for the year ended June 30, 1994, because the statements for the Workers' Compensation Assigned Risk Plan were not prepared in accordance with generally accepted accounting principles (GAAP). The plan is reported as a component unit of the state and is audited by a certified public accounting firm.

There was a significant change in the established accounting principles in fiscal year 1994. Statement No. 14, The Financial Reporting Entity, promulgated by the Governmental Accounting Standards Board, was first effective for this year. This statement changed the definition of financial activities to be included in a governmental entity's financial statements. As a result of the changing principles, the State of Minnesota was required to include financial information for several new component units. This required coordination with the individual entities and their external auditors.

At the same time that additional work was necessary to implement the new accounting principles, the financial reporting division was undergoing staffing changes. The department hired a new director in July 1994, after a vacancy of several months. In addition, two senior staff members went on mobility assignments to the Statewide Systems Project. This left a heavy workload for the remaining experienced staff and new employees. As a result, the department did not begin working to resolve all financial reporting issues with the component units in a timely manner. The Workers' Compensation Assigned Risk Plan, which prepares its financial statements in accordance with regulatory guidelines, could not provide GAAP based statements as requested.

Recommendation

- *The Department of Finance should work with the Workers' Compensation Assigned Risk Plan to ensure it has GAAP based financial statements.*

State of Minnesota
Department of Finance

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June 13, 1995

James R. Nobles
Legislative Auditor
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Dear Jim:

The purpose of this letter is to respond to the finding in your report on the audit of the Department of Finance for the year ended June 30, 1994.

Current Finding

The state's financial statements contained a departure from generally accepted accounting principles because of difficulties in implementing a new standard.

Recommendation

The Department of Finance should work with the Workers' Compensations Assigned Risk Plan to ensure it has GAAP based financial statements.

Response

Financial Reporting staff have been working with the Workers' Compensations Assigned Risk Plan and the CPA firm retained to audit their financial statements. The plan administrator has agreed to provide audited GAAP financial statements for their fiscal year ending December 31, 1994. The financial report is scheduled to be available in July 1995.

As we mentioned in the exit conference, we have reorganized most of the Accounting Division. As a part of that effort, we have provided additional resources for the financial reporting section. This will enable us to develop the expertise necessary to more effectively implement new accounting and reporting standards.

Warmest regards,

Laura M. King
Commissioner