

# Department of Natural Resources

## Programs Selected For Fiscal Year 1995 Statewide Audit

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February 1996

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Financial Audit Division  
Office of the Legislative Auditor  
State of Minnesota

96-4





STATE OF MINNESOTA

**OFFICE OF THE LEGISLATIVE AUDITOR**

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JAMES R. NOBLES, LEGISLATIVE AUDITOR

Representative Ann H. Rest, Chair  
Legislative Audit Commission

Members of the Legislative Audit Commission


Mr. Rodney W. Sando, Commissioner  
Department of Natural Resources


We have audited selected areas of the Department of Natural Resources for the fiscal year ended June 30, 1995, as further explained in Chapter 1. The work conducted in the department is part of our Statewide Audit of the State of Minnesota's fiscal year 1995 financial statements. The Comprehensive Annual Financial Report for the year ended June 30, 1995 includes our report, issued thereon dated December 1, 1995. The following Summary highlights the audit objectives and conclusions. We discuss our concerns more fully in the individual chapters of this report.

We conducted our audit in accordance with generally accepted government standards. Those standards require that we obtain an understanding of management controls relevant to the audit. The standards require that we design the audit to provide reasonable assurance that the Department of Natural Resources complied with provisions of laws, regulations, contracts, and grants that are significant to the audit. The management of the Department of Natural Resources is responsible for establishing and maintaining the internal control structure and complying with applicable laws, regulations, contracts, and grants.

In accordance with Minn. Stat. Section 3.975, this report will be referred to the Attorney General. Finding 2 discusses the department's potential noncompliance with Minn. Stat. Section 16A.15, Subd. 3, relating to its flood mitigation grants. Without explicit language in the flood mitigation appropriation laws, we question the department's ability to use the appropriations to finance prior commitments. The Attorney General must determine the legality of reimbursements the department made to counties for previous flood mitigation expenditures. Minn. Stat. Section 3.975 requires us to report such issues to the Attorney General and the Legislative Audit Commission.

This report is intended for the information of the Legislative Audit Commission and the management of the Department of Natural Resources. This restriction is not intended to limit the distribution of the report, which was released as a public document on February 2, 1996.

  
James R. Nobles  
Legislative Auditor

  
John Asmussen, CPA  
Deputy Legislative Auditor

End of Fieldwork: December 1, 1995

Report Signed On: January 25, 1996



# SUMMARY

State of Minnesota

Office of the Legislative Auditor

Centennial Office Building • St. Paul, MN 55155

612/296-4708

## Department of Natural Resources

### Programs Selected For Fiscal Year 1995 Statewide Audit

Public Release Date: February 2, 1996

No. 96-4

### Agency Background

The Department of Natural Resources (DNR) is responsible for managing public waters, lands, parks, forests, and minerals, as well as insuring compliance with a broad range of regulations that affect natural resources. The department consists of seven divisions, departmental field operations, and support services. DNR operates six regions throughout the state. Each region has supervisors representing the department's various divisions, as well as a regional administrator who provides overall coordination and support for the region. Rodney W. Sando is the commissioner of the department.

### Selected Audit Areas and Conclusions

Our scope was limited to those areas material to the State of Minnesota's Comprehensive Annual Financial Report for the year ended June 30, 1995. We audited Permanent School Fund timber sales revenues and transfers to the General Fund, Capital Projects Fund flood mitigation grants, and regional parks grants.

We found that DNR accurately recorded the timber sales revenues and General Fund transfers in the Permanent School Fund. However, we found that DNR does not deposit timber sales receipts collected by the area offices timely.

We found that DNR grants for flood mitigation and regional parks were correct and accurately recorded on the statewide accounting system. However, in two cases, DNR reimbursed local governmental units for costs incurred prior to the effective date of the flood mitigation appropriation. We have referred this issue to the Attorney General's Office to determine whether DNR had the authority to expend appropriation for prior commitments. Payments made for costs incurred prior to the appropriation may not be in compliance with Minn. Stat. Section 16A.15, Subd. 3.

Contact the Financial Audit Division for additional information.

296-1235



## **Department of Natural Resources**

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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
Jeanine Leifeld, CPA	Audit Manager
Jack Hirschfeld, CPA	Auditor-In-Charge
Leah Tetzlaff	Auditor

### **Exit Conference**

We discussed the findings and recommendations found in Chapters 2 and 3 with the following staff of the Department of Natural Resources on October 5, 1995:

John Heintz	Financial Management Bureau Administrator
John Bouthilet	Accounting Manager
Joe Gibson	Supervisor, Environmental Review, Planning and Coordination
Kent Lokkesmoe	Waters Division Director





# Department of Natural Resources

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## Chapter 1. Introduction

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The Department of Natural Resources (DNR) is responsible for managing public waters, lands, parks, forests, and minerals, as well as ensuring compliance with a broad range of regulations that affect natural resources. The department consists of seven divisions, departmental field operations, and support services. DNR operates six regions throughout the state. Each region has supervisors representing the department's various divisions, as well as a regional administrator who provides overall coordination and support for the region. Rodney W. Sando is the commissioner of the department.

Our audit scope focused on the fiscal year 1995 expenditures included in Table 1-1. These financial activities were material to the state's financial statements for the year.

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**Table 1-1: Audited Financial Activities**  
**Year Ended June 30, 1995**

<u>Revenue Program</u>	
Permanent School Fund timber sale revenues	\$4,415,272
<u>Expenditure Programs</u>	
Capital Projects Fund flood mitigation grants	\$1,794,115
Capital Projects Fund regional park grants	\$2,400,000
Permanent School Fund transfers to the General Fund	\$3,423,643

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Source: Auditor analysis of financial activity recorded in the statewide accounting system.

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The primary objective of the Statewide Audit is to render an opinion on the State of Minnesota's financial statements included in its Comprehensive Annual Financial Report for fiscal year 1995. This includes determining whether the financial statements of the state fairly present its financial position, results of operations, and change in cash flows in conformity with generally accepted accounting principles. As part of our work, we are required to gain an understanding of the internal control structure and ascertain whether the state complied with laws and regulations that may have a material effect on its financial statements.

To address this objective, we interviewed key department employees, reviewed applicable policies and procedures, and tested representative samples of financial transactions.

Our work in the Department of Natural Resources was completed as part of our audit to express an opinion on the state's fiscal year 1995 financial statements. The Comprehensive Annual Financial Report for the year ended June 30, 1995 includes our report, issued thereon dated December 1, 1995. The Minnesota Financial and Compliance Report on Federally Assisted Programs for the year ended June 30, 1995 will include our reports on the supplementary information schedule, internal control structure, and compliance with laws and regulations. We anticipate issuing this report in June 1996.

We concluded that the amounts shown on Table 1-1 were fairly presented on the state's Comprehensive Annual Financial Report. We discuss, in detail, any internal control issues and other concerns in Chapters 2 and 3 of this report.

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## Chapter 2. Timber Sales

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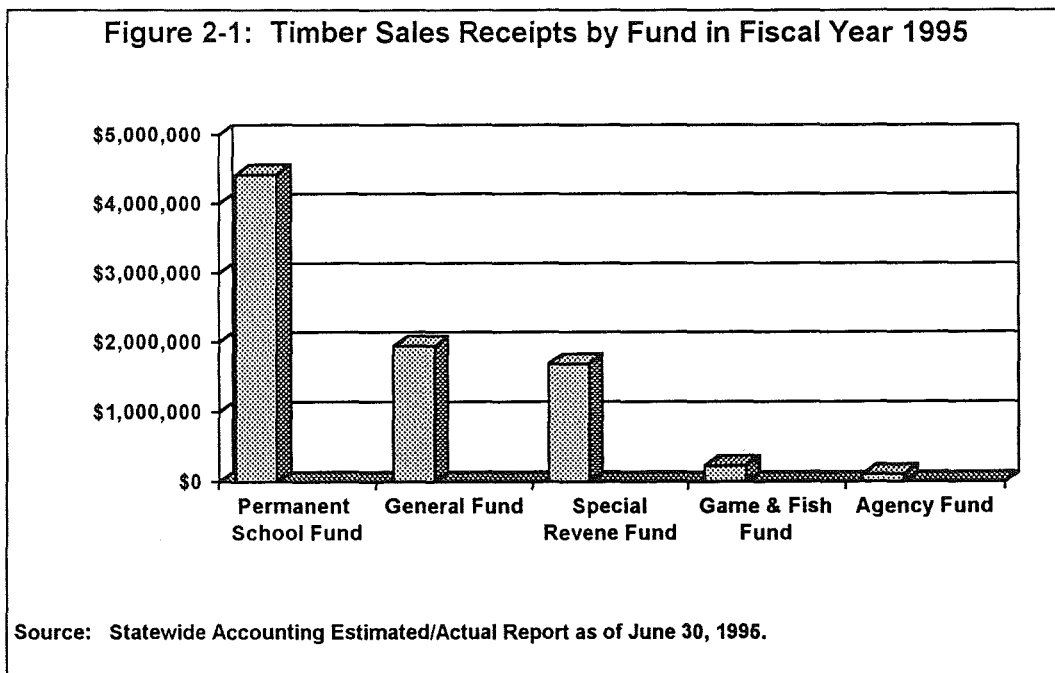
### *Chapter Conclusions*

*The Forestry Division accurately recorded the timber sales revenues in the Permanent School Fund. However, we found that DNR does not deposit timely receipts collected by the area offices.*

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Minn. Stat. Chapter 90 assigns the responsibility for conducting timber sales to DNR. The DNR Forestry Division has developed specific policies and procedures relating to timber sales. Area offices conduct timber sales in accordance with these regulations and internal procedures.

Total timber sales revenues amounted to \$8,411,000 in fiscal year 1995. DNR credited these revenues to individual funds, depending on the land on which the timber sales tracts were located. The chart below shows the timber sales revenues for each fund during fiscal year 1995. We limited our audit scope only to timber sales revenues for the Permanent School Fund. Permanent School Fund timber sales revenues amounted to \$4,415,272 in fiscal year 1995.



DNR has established 40 area offices throughout the state. DNR area field personnel appraise the value of timber designated for sale on specific tracts of land. Area offices conduct two types of timber sales based upon the appraised value of the tracts: auction sales and informal sales. DNR conducts auction sales for tracts appraised over \$3,000. DNR uses informal sales for sales of timber on tracts appraised at equal to or less than \$3,000. Area offices collect the advance

## Department of Natural Resources

payment of 25 percent of the appraised value from auction sales and the full appraised value of tracts sold through informal sales. The central office bills and collects the remaining amount due on auction sales.

We determined that the department correctly recorded timber sales receipts to the Permanent School Fund within the statewide accounting system. However, we found that DNR does not deposit certain timber sales receipts promptly.

### **1. Area offices are not depositing the advance payments from auction sales and informal sales of timber timely.**

DNR area offices do not deposit receipts from advance payments and informal sales of timber directly. Based upon Forestry Division Policies and Procedures, area offices mail the checks to the central office in Saint Paul for deposit. We estimate that during fiscal year 1995, the area offices sent approximately \$2.3 million to the central office for deposit. Current policies require the area offices to mail the auction sale advance and informal sales receipts to the central office for deposit. In both instances, the department is not depositing these receipts timely. Minn. Stat. Section 16A.275 requires state agencies to deposit receipts totaling \$250 or more daily.

Mailing the incoming receipts to the central office delays the deposit of these funds by several days. Also, the current procedures increases the likelihood of the checks being lost or stolen. DNR should work with the Department of Finance to establish or use existing local bank depositories where cost effective.

### *Recommendation*

- *The Forestry Division should reevaluate its policies and procedures for timber sales to ensure that cash collections at the area offices are promptly deposited.*

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## Chapter 3. Flood Mitigation Program

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### *Chapter Conclusions*

*The Department of Natural Resources (DNR) makes grant payments to local governmental units under the Flood Mitigation Program. The payment amounts were correct and accurately recorded on the statewide accounting system. However, in two cases, DNR reimbursed local governmental units for costs incurred prior to the effective date of the flood mitigation appropriation, potentially in noncompliance with Minn. Stat. Section 16A.15, Subd. 3.*

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The Flood Hazard Mitigation Program provides assistance to local governmental units for capital improvements to prevent or alleviate flood damage to public lands, facilities, or capital improvements. The Flood Mitigation Program provides matching funds equal to 50 percent of the local governmental unit's project cost. DNR establishes grant agreements with the governmental units allowing for reimbursement of the project costs. Grant recipients submit reimbursement requests documenting the amount of expenditures. Minn. Stat. Section 103F.161 specifies what local activities and costs are eligible under this program.

The department submits specific projects and funding recommendations to the Legislature as part of the budgetary process. The Legislature ultimately approves specific projects and the related funding. The 1994 appropriation of \$2,600,000 funded expenditures for four projects during fiscal year 1995. Of this amount, DNR made grant payments of \$1,794,114 from the Capital Projects Fund during fiscal year 1995. Below is a table showing the approved grant amount and the payments during fiscal year 1995 charged to the 1994 appropriation.

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**Table 3-1**  
**Costs Charged to the Flood Mitigation Program**  
**Fiscal Year 1995**

<u>Projects</u>	<u>Approved Project Grants(1)</u>	<u>Payments During Fiscal Year 1995</u>	<u>Remaining Funding</u>
Red River Watershed	\$ 350,000	\$ 350,000	\$ 0
Renville County	50,000	11,287	38,713
City of Chaska	1,300,000	1,300,000	0
City of Winona	<u>900,000</u>	<u>132,827</u>	<u>767,173</u>
Total	<u>\$2,600,000</u>	<u>\$1,794,114</u>	<u>\$805,886</u>

- (1) These grants may represent only partial project funding. For instance, in the Agency Capital Budget Request for fiscal years 1994-1999, DNR requested \$1.3 million in state reimbursements for the city of Chaska project. The entire project was estimated at \$2,006,000. The remaining costs were reimbursed from previous appropriations.

Source: Statewide accounting records as of June 30, 1995.

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Local governmental units submit reimbursement requests equal to half of the costs it has incurred. DNR reviews the costs for appropriateness and accuracy prior to approving the payment.

We found that the payments amounts charged to the Capital Projects Fund were correct, and that the accounting records were accurate. However, in reviewing the payments, we noted that the department reimbursed local governmental units for expenditures that occurred prior to the effective date of the 1994 appropriation.

### **2. The Department of Natural Resources reimbursed local governmental units for costs incurred prior to the effective date of the flood mitigation appropriation.**

DNR made two payments under the Flood Mitigation Program to local governmental units for costs partially incurred prior to the effective date of the 1994 flood mitigation appropriation, which was May 16, 1994:

Renville County	\$7,121 paid for costs incurred from July 16, 1993 through October 17, 1994.
Red Lake Watershed	\$262,459 paid for costs incurred from May 31, 1993 through May 31, 1994.

These payments conflict with Minn. Stat. Section 16A.15, Subd. 3. This statute states that an obligation may not be incurred until an encumbrance is established, and an encumbrance cannot be established without a sufficient appropriation balance.

DNR staff believe that, because these grants are on a project basis, the specific appropriation period is irrelevant. For example, they stated that the \$50,000 given to Renville County was intended for "preliminary engineering". However, since Renville had already incurred much of its preliminary engineering costs in response to a 1993 flood, DNR believes that the Legislature intended to reimburse the county for costs already incurred. Therefore, DNR included in the grant agreement with Renville County a statement that the "in-kind services dating back to May 1993 shall be eligible for all or part of the cost sharing requirements of the grant."

We believe that DNR should not have reimbursed the county for prior costs. The intention of these grants is to prevent or reduce the damage of future floods. In the absence of explicit appropriation language, DNR does not have the authority to extend appropriation funding to prior commitments. By doing so, the state allowed the county to free up resources for other purposes.

We have reported this issue to the Attorney General. We are requesting an interpretation of the appropriation laws. We are also requesting the Attorney General to determine if DNR should seek reimbursement from the counties for the two payments identified above.

### *Recommendation*

- *DNR should discontinue retroactive funding of flood mitigation requests, unless it obtains explicit appropriation authority to pay prior commitments.*



# Minnesota Department of Natural Resources

## OFFICE OF THE COMMISSIONER

500 Lafayette Road  
St. Paul, Minnesota 55155-4037

January 18, 1996

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

Dear Mr. Nobles:

Thank you for the opportunity to respond in writing to the findings contained in your audit of the Department of Natural Resources (DNR) as part of the Statewide Audit for F.Y. 1995.

**Finding #1: Area offices are not depositing the advance payments from auction sales and informal sales of timber timely. The audit recommends we reevaluate our procedures and set up and utilize local depositories, if cost-effective.**

In our experience, the risk due to lost or stolen checks is insignificant. The checks are mailed by the area foresters to the central office where they are immediately processed. The Division of Forestry maintains centralized accounts receivable records. Any lost or stolen checks would be detected and recovered in the normal course of business. (We have never had an instance of this and the audit does not cite any.)

We believe that the potential cash flow would not justify using depositories. For example, in F.Y. 1995 there were 52 sales conducted through 28 area offices for a total appraised value of \$1,976,200. On average, each area held two auctions resulting in only two deposits of \$36,076 each. This would yield a total of about \$2,500 in interest for all 28 locations. In the past, the Department of Finance has been reluctant to establish depositories for low volumes.

In our procedures, both the checks and the documentation (Appraisal Report and Notice of Sales) are sent directly to the central office and are immediately processed and deposited. The amounts are posted to the Forestry accounts receivable records. In processing, the documentation and checks are stamped with a unique validation number. The information from the source documents, including the validation number, is input into the DNR Revenue Processing System. This validation number ties a transaction together and provides an audit trail for tracking receipts. Sending the checks to a local bank and the documentation to the central office and then somehow reconciling them would be difficult. We are not clear how to do it in practice.

Finally, we have recognized for several years that our revenue accounting computer system is outdated; it does not adapt to decentralized receipts processing and accounts receivable postings. Accordingly, we



Mr. James R. Nobles  
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requested and received an appropriation from the 1995 Session to begin design and development of a totally new accounts receivable and revenue processing system. When implemented, it will enable decentralized deposit and posting to accounts receivable records and much more.

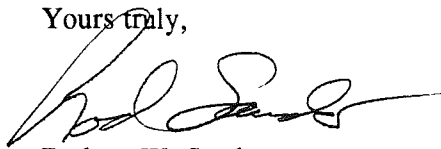
At this time, the Department of Finance has indicated that it does not appear cost-effective to set up depositories for our area locations. We will include this issue within the scope of our revenue processing system redesign and make every effort to address your concerns in the redesigned system.

**Finding #2: The DNR reimbursed local governmental units for costs incurred prior to the effective date of the flood mitigation appropriation. The audit recommends that we discontinue retroactive funding, unless there is explicit appropriation authority.**

We agree, that as a matter of policy, it would be a better business practice not to reimburse for costs incurred prior to the appropriation date. Accordingly, we will not make these kinds of payments in the future.

We respectfully disagree with your statement that the payments to Renville County and the Red Lake Watershed are a violation of M.S. 16A.15, Subd. 3. The DNR incurred no obligation until the contract was established--after the appropriation date. Similarly, we did not "extend appropriation funding to prior commitments." Again, there was no commitment made until the appropriation and contract were in effect.

Yours truly,



Rodney W. Sando  
Commissioner

cc: Jeanine Leifeld, CPA, Audit Manager, OLA  
Ronald Nargang, Deputy Commissioner, DNR  
Eugene Gere, Assistant Commissioner for Administration, DNR  
Raymond Hitchcock, Assistant Commissioner for Operations, DNR  
Gerald Rose, Director, DNR Forestry Division  
Kent Lokkesmoe, Director, DNR Waters Division  
John Heintz, Administrator, DNR Financial Management Bureau