

# **Department of Commerce**

## **Selected Scope Financial Audit**

**For the Period July 1, 1995, through June 30, 1997**

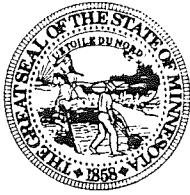
**September 1997**

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

**97-50**





STATE OF MINNESOTA

**OFFICE OF THE LEGISLATIVE AUDITOR**

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JAMES R. NOBLES, LEGISLATIVE AUDITOR

Senator Deanna Wiener, Chair  
Legislative Audit Commission

Members of the Legislative Audit Commission

Mr. David Gruenes, Commissioner  
Department of Commerce

We have audited the Financial Examinations Division, Registration and Insurance Division, and the Administrative Services Division of the Department of Commerce for the period July 1, 1995, through June 30, 1997, as further explained in Chapter 1. Our audit scope included material revenues and expenditure cycles within these divisions. Our audit did not include the Enforcement and Licensing Division and did not include department payroll. Therefore, we emphasize that this has not been a complete audit of all of the financial activities of the Department of Commerce. The following Summary highlights the audit objectives and conclusions. We discuss these issues more fully in the individual chapters of this report.

We conducted our audit in accordance with generally accepted auditing standards and *Government Auditing Standards*, as issued by the Comptroller General of the United States. Those standards require that we obtain an understanding of internal controls relevant to the audit. The standards also require that we design the audit to provide reasonable assurance that the department complied with provisions of laws, regulations, contracts, and grants that are significant to the audit. Management of the department is responsible for establishing and maintaining the internal control structure and for compliance with applicable laws and regulations.

This report is intended for the information of the Legislative Audit Commission and management of the Department of Commerce. This restriction is not intended to limit the distribution of this report, which was released as a public document on September 10, 1997.

James R. Nobles  
Legislative Auditor

John Asmussen, CPA  
Deputy Legislative Auditor

End of Fieldwork: August 20, 1997

Report Signed On: August 28, 1997



# SUMMARY

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## Department of Commerce

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### Background Information

The mission of the Department of Commerce is to enforce state laws, safeguard consumer rights, and regulate financial industries. James Ulland served as commissioner from September 1993 until December 1995. David Gruenes became commissioner of the department in December 1995.

The department is organized into the following divisions: the Administrative Services Division, the Financial Examinations Division, the Enforcement and Licensing Division, and the Insurance and Registration Division.

### Audit Scope and Objectives

The focus of our audit was the revenue and expenditures of the Financial Examinations Division, the Registration and Insurance Division, and the Administrative Services Division for the two years ended June 30, 1997.

### Conclusions

The Department of Commerce provided reasonable assurance that license and regulatory fees of the Insurance and Registration Division and the Financial Examinations Division were properly collected, adequately safeguarded, and correctly recorded in the accounting system. The department complied with applicable regulations in the collection of licenses and regulatory fees for the items tested.

The Department of Commerce provided reasonable assurance that expenditures were authorized within the legal provisions of the appropriation and administered in accordance with applicable finance related legal provisions. For the transactions tested, expenditures were made for goods and services received and were made for a proper purpose based on the mission of the department.



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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
Jim Riebe, CPA	Audit Manager
Charlie Gill	Auditor-in-Charge
Susan O'Connell	Auditor
Dale Ogren, CPA	Auditor





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## Chapter 1. Introduction

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The Minnesota Legislature established the Department of Commerce in 1983. At that time, the Banking, Insurance, and Securities and Real Estate Departments were organized into a single agency to better coordinate regulatory functions. The mission of the Department of Commerce is to enforce state laws, safeguard consumers rights, and regulate financial industries. James Ulland served as commissioner from September 1993 until December 1995. David Gruenes became commissioner of the department in December 1995. The commissioner of the Department of Commerce is the appointing authority for a number of boards, committees, and special task forces that either the Legislature or the commissioner created.

The Department of Commerce is organized into the following divisions: the Administrative Services Division, the Financial Examinations Division, the Enforcement and Licensing Division, and the Insurance and Registration Division. The department received an appropriation to finance its operations. Commerce collected numerous types of fees associated with licensing, examinations, and regulatory services provided by the department. Most fees are deposited into the General Fund. Many fees are set in statute; the department set other fees to recover the costs of providing certain services such as bank and insurance company examinations.

The focus of our audit was the revenue and expenditures of the Financial Examinations, Registration and Insurance, and the Administrative Services divisions. Our previous audit of the department for the three year period ending June 30, 1995, included department payroll and Enforcement and Licensing Division revenues and expenditures.

- The Financial Examinations Division was responsible for regulating commercial state banks, state credit unions, trust companies, investment certificate companies, state savings and loans, industrial loan and thrifts, consumer small loan lenders, and finance companies.
- The Registration and Insurance Division examined the financial condition of companies licensed to sell insurance and other insurance products in Minnesota. The division reviewed registration applications for market investments. The division also provided staff assistance to the Petroleum Tank Release Compensation Board. The board administered compensation claims from the Petroleum Tank Release Cleanup Fund for cleanup of leaks and spills from petroleum storage tanks. Petroleum Tank Release Cleanup Fund expenditures account for more than 60 percent of total department expenditures. We audit Petroleum Tank Release Cleanup Fund expenditures during our annual Statewide audit; therefore, those expenditures were not included as part of the scope of this audit.
- The Administrative Services Division provided support services to the whole department. These services included depositing receipts, processing payroll, procuring goods and

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services, and disbursing funds. Additional services provided by the division included information systems and human resources.

During fiscal years 1996 and 1997 respectively, the Financial Examinations Division had revenues of approximately \$4.3 million and \$3.7 million, and the Registration and Insurance Division had revenues of about \$19.8 million and \$24.9 million. Total department revenues were about \$50 million in fiscal year 1996 and \$59 million in fiscal year 1997.

We audited administrative expenditures (excluding payroll) of the Financial Examinations Division, the Registration and Insurance Division, and the Administrative Services Division that totaled approximately \$2 million and \$2.6 million during fiscal years 1996 and 1997 respectively. Total department expenditures during fiscal years 1996 and 1997 were approximately \$44.7 million and \$48.5 million.

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## Chapter 2. Revenues

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### *Chapter Conclusions*

*The Department of Commerce provided reasonable assurance that license and regulatory fees of the Insurance and Registration Division and the Financial Examinations Division were properly collected, adequately safeguarded, and correctly recorded in the accounting system. The department complied with applicable regulations in the collection of licenses and regulatory fees for the items tested.*

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The Insurance and Registration Division and the Financial Examinations Division collected numerous types of fees as discussed in the following sections. Most fees for the Department of Commerce are set in statute.

### **The Insurance and Registration Division**

The Insurance and Registration Division regulated insurance companies doing business in Minnesota and collected revenue for the annual licensing of those companies and insurance agents. The division also billed fees for the time department insurance analysts spent reviewing required financial information for insurance companies. Table 2-1 shows the revenues for the two years ended June 30, 1997.

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**Table 2-1**  
**Insurance and Registration Division Revenues**

	<u>Year Ended June 30</u>	
	<u>1996</u>	<u>1997</u>
Insurance Company License	\$ 757,275	\$ 756,200
Insurance Company Desk Audits	1,292,150	1,231,748
Securities Agent License	825,850	968,500
Securities Agent License Renewal	2,444,400	2,766,250
Redeemable Securities Registration	<u>14,430,863</u>	<u>19,182,114</u>
Total	<u>\$19,750,638</u>	<u>\$24,904,812</u>

Source: MAPS accounting records.

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### **Insurance Company Desk Audits**

Insurance companies doing business in Minnesota are required by Minn. Stat. 60A.13 to file an annual statement with the Department of Commerce. Department of Commerce analysts audited insurance companies to determine the business conditions and to verify that required information

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was filed appropriately, as required by the National Association of Insurance Commissioners. The hourly rate for desk audit billing was \$62.45 per hour for fiscal years 1996 and 1997.

### **Insurance Company Licenses**

Insurance companies were issued annual licenses on June 1 of each year. The license was issued after determining that the appropriate annual statements had been filed and subsequently approved by the commissioner. The fee for each company's annual certificate of authority was \$575. The department issued approximately 1,400 renewal licenses in June 1997.

### **Redeemable Securities Registration**

Companies filed registration statements relating to redeemable securities issued by open end management companies or unit investment companies, as defined in the Investment Company Act of 1940, and paid a filing fee of \$100 plus an additional fee as specified in statute based on the offering price. The Department of Commerce securities analysts determined the appropriateness of the documentation prior to obtaining the commissioner's approval.

### **Securities Agent and Broker/Dealer Licenses and Renewals**

The National Association of Securities Dealers (NASD) issued annual licenses for securities agents and broker/dealers. The annual fees ranged from \$50 to \$200 depending on the type of license. Securities agents who terminated employment with one broker-dealer and changed to a different broker-dealer paid a \$25 license transfer fee. The NASD collected the fees and remitted them to the Department of Commerce by electronic bank transfer. The NASD issued the license and sent the department a list of the names associated with the fees collected. The license renewal period is in January of each year. As of May 1997, there were approximately 1,200 broker-dealers, 800 investment advisers, and 63,000 securities agents with active licenses.

### **The Financial Examinations Division**

The Financial Examinations Division was responsible for regulating commercial state banks, state credit unions, state savings and loans, and other finance companies. The division chartered and licensed over 700 financial services organizations and licensees doing business at over 1,135 locations in Minnesota. The division performed on-site examinations and investigations, and licensed qualified individuals, corporations, and members to conduct regulated activities. The division also collected and analyzed financial data and reports submitted by financial institutions and licensees doing business in the state. Table 2-2 shows the revenues for the two years ended June 30, 1997.

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**Table 2-2**  
**Financial Examinations Division Revenues**

	<u>Year Ended June 30</u>	
	<u>1996</u>	<u>1997</u>
Bank and Trust Company Assessment	\$1,750,632	\$1,426,936
Bank and Trust Examination Fee	1,793,110	1,514,842
Other	<u>778,808</u>	<u>743,896</u>
Total	<u>\$4,322,550</u>	<u>\$3,685,674</u>

Source: MAPS accounting records.

Department of Commerce staff attributed the decrease in Financial Examinations Division revenues from fiscal year 1996 to fiscal year 1997 to downsizing in the division's operations and efficiencies resulting from automating aspects of the examinations process.

### **Bank and Trust Company Assessments and Examination Fees**

The bank and trust company assessment was one of two ways the Department of Commerce charged the banking industry for services provided. The formula was based on the division's budget, salaries, indirect costs, and Attorney General's fees. Commerce billed the regulated industries based on a ratio of 103 percent of the industries' assets. The bank and trust examination fee represented the cost of the services of division examiners. Companies were billed the actual number of hours for on-site work and preparation. The fee was based on three years of data. For example, the fee for fiscal year 1997 was calculated in mid-1996 and included 1995 actual data, 1996 data projected for the end of the year, and 1997 budgeted amounts.

### **Audit Scope and Objectives**

We focused our review of Insurance and Registration Division and Financial Examination Division revenue collection on the following objectives:

- Did the Department of Commerce design internal controls to provide reasonable assurance that revenues for licenses and regulatory fees were properly collected, adequately safeguarded, and correctly recorded in the accounting system?
- Did the Department of Commerce comply with applicable regulations in the collection of licenses and regulatory fees?

The methodology we used to audit revenues included interviews with key departmental staff to obtain an understanding of the controls in place over revenues. We tested receipts for material revenues included in our audit scope. We verified that the fees collected were appropriate and that the cashiers deposited the revenue promptly and accurately into the accounting records in accordance with Department of Finance requirements.

The Department of Commerce provided reasonable assurance that revenues for licenses and regulatory fees were properly collected, adequately safeguarded, and correctly recorded in the accounting system. The department complied with applicable regulations in the collection of licenses and regulatory fees for items tested.

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## Chapter 3. Administrative Expenditures

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### *Chapter Conclusions*

*The Department of Commerce provided reasonable assurance that expenditures were authorized within the legal provisions of the appropriation and in accordance with applicable finance related legal provisions. For the transactions tested, expenditures were made for goods and services received and for a proper purpose based on the mission of the department.*

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The Department of Commerce received an appropriation to fund its operations. Total appropriations for fiscal years 1996 and 1997 were approximately \$15 million each year. The Administrative Services Division processes payroll and other disbursements centrally. The department employs approximately 250 staff.

Our audit scope was limited to administrative expenditures (excluding payroll) for the Financial Examinations, Registration and Insurance, and Administrative Services Divisions in fiscal years 1996 and 1997. Expenditures of the Enforcement and Licensing Division and payroll for the entire department were not included in the scope of this audit, but were included in our last audit of the department for the three years ended June 30, 1995.

Table 3-1 summarizes fiscal year 1996 and 1997 expenditures included in our audit scope.

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**Table 3-1**  
**Administrative Expenditures**

	Fiscal Year	
	1996	1997
Non-State Rent	\$ 691,470	\$ 779,600
Supplies and Equipment	417,603	535,844
Travel	288,854	385,438
Other	612,124	898,866
Total Expenditures	<u>\$2,010,051</u>	<u>\$2,599,749</u>

Source: MAPS accounting records as of 6/30/97.

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### **Audit Scope and Objectives**

We focused on the following objectives for administrative expenditures included in our audit scope:

- Did the Department of Commerce provide reasonable assurance that expenditures were authorized within the legal provisions of the appropriation and in accordance with applicable finance related legal provisions?

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- Were expenditures made for goods and services received and for a proper purpose based on the mission of the department?

The methodology we used to evaluate these audit objectives included analytical reviews, tests of transaction details and balances, and tests of compliance. We reviewed the support for accounting data and substantiated account balances.

## **Conclusions**

The Department of Commerce provided reasonable assurance that expenditures were authorized within the legal provisions of the appropriation and in accordance with applicable finance related legal provisions. For the items tested, expenditures were made for goods and services received and for a proper purpose based on the mission of the department.