Department of Children, Families & Learning

Selected Programs
Fiscal Year 1997 Statewide Audit

March 1998

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Financial Audit Division
Office of the Legislative Auditor
State of Minnesota

98-12

Centennial Office Building, Saint Paul, MN 55155 • 612/296-1727

STATE OF MINNESOTA

OFFICE OF THE LEGISLATIVE AUDITOR

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Legislative Audit Commission

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Ms. Jeanne Kling, Acting Board President
Minnesota State Board of Education

Mr. Robert Wedl, Commissioner
Department of Children, Families & Learning

We have audited selected programs of the Department of Children, Families & Learning for the fiscal year ended June 30, 1997, 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 1997 financial statements and Single Audit. The Comprehensive Annual Financial Report for the year ended June 30, 1997, includes our report, issued thereon dated December 8, 1997. The Minnesota Financial and Compliance Report on Federally Assisted Programs for the year ended June 30, 1997, will include our reports on the supplementary information schedule, internal control structure, compliance with laws and regulations, and a summary of prior audit findings. We anticipate issuing this report in March 1998. Therefore, we emphasize that this has not been a complete audit of all financial activities of the Department of Children, Families & Learning. 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 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 management controls relevant to the audit. The standards require that we design the audit to provide reasonable assurance that the Department of Children, Families & Learning complied with provisions of laws, regulations, contracts, and grants that are significant to the audit. Management of the Department of Children, Families & Learning is responsible for establishing and maintaining the internal control structure and complying with applicable laws, regulations, contracts, and grants.

This report is intended for the information of the Legislative Audit Commission and the management of the Department of Children, Families & Learning. This restriction is not intended to limit the distribution of this report, which was released as a public document on March 6, 1998.

James R. Nobles
Legislative Auditor

Claudia Gudvangen, CPA
Deputy Legislative Auditor

End of Fieldwork: December 19, 1997

Report Signed On: February 25, 1998

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SUMMARY

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Department of Children, Families & Learning

Selected Programs
Fiscal Year 1997 Statewide Audit

Public Release Date: March 6, 1998 No. 98-12

Agency Background

The Department of Children, Families & Learning is responsible for providing educational assistance to school districts and local educational agencies. In addition, the department is responsible for programs that address social and economic concerns. The department funds itself mainly from General Fund appropriations and federal grants. Department expenditures for fiscal year 1997 totaled approximately $4 billion. Mr. Robert Wedl is the commissioner of the department.

Selected Audit Areas and Conclusions

Our audit scope included those areas material to the state of Minnesota's Comprehensive Annual Financial Report for the year ended June 30, 1997, and to the Single Audit objectives. The statewide audit and single audit objectives included the determination that financial activities were accurately reported on the accounting system, and that the department complied with material state and federal laws and regulations.

We concluded that the Department of Children, Families & Learning's financial activities for the programs included in the Statewide Audit scope are fairly presented in the state of Minnesota's Comprehensive Annual Report for fiscal year 1997. However, we did find the following concerns. The department did not properly estimate the allowance for uncollectible loans for the Maximum Effort School Loan Fund. The department also made incorrect payments for the Child Care Development Program. The department did not properly establish a monitoring system for subrecipients of federal library grants. Finally, the department continues to lack important quality control mechanisms in its computing environment for state and federal programs.

The Department of Children, Families & Learning agrees with the findings and recommendations in this report. The department is taking actions to resolve these issues.

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Audit Participation

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

Claudia Gudvangen, CPA	Deputy Legislative Auditor
Renee Redmer, LPA	Audit Manager
Jack Hirschfeld, CPA	Auditor-In-Charge
Chris Buse, CPA, CISA	Director Of Information Systems Auditing
Charlie Gill	Senior Auditor
Shane Smeby	Senior Auditor
Brad Falteysek	Auditor
Anna Lamin	Auditor
Neal Dawson	Intern

Exit Conference

The findings and recommendations in this report were discussed with the following staff of the Department of Children, Families & Learning on February 12, 1998:

Robert Wedl	Commissioner
John Hustad	Deputy Commissioner
John Bulger	Director of Finance and Management Services
Don Johnson	Federal Programs and Reporting
Paul Ward	Systems and Programming
William Kieson	Health/Safety and Debt Service Funding
Janice Feye-Stukas	Library Development Supervisor

Chapter 1. Introduction

The 1995 Legislature created the Department of Children, Families & Learning effective October 1, 1995. The department replaced the former Department of Education. The department provides funding to school districts, private schools, and other local educational agencies for education. In addition, the department is responsible for several other children and family programs that address social and economic concerns. The Governor appointed Mr. Robert Wedl as the Commissioner effective November 4, 1996.

The department states that its mission is to increase the capacity of Minnesota communities to measurably improve the well-being of children and families. The department is organized into five offices. These offices include:

Commissioner's Office	The Commissioner serves as the chief executive officer of the state agency and reports to the Governor.
Office of Teaching and Learning	This office works directly with schools to improve academic achievements of students grades K-12. The state agency and the districts seek to improve student learning through the curriculum, instruction, and assessment process.
Office of Management Services	This office handles measurement, monitoring, and regulation work for the agency, including school district funding, organization, and technology leadership.
Office of Lifetime Development	This office works with partnerships at the state and local level to help Minnesota's young people become active citizens, economic players, and lifelong learners.
Office of Community Services	This office helps the collaboration of communities, school districts, and family service providers in support of lifelong learning and safe and healthy lifestyles.

The Department of Children, Families & Learning administered a budget of approximately $4 billion in fiscal year 1997. General Fund appropriations and federal grants provided most of the funding for the department's programs and activities. The department administered over 150 state and federal activities. The department distributed most of its resources in grants and aids to school districts and local educational agencies. Annual state appropriations for fiscal year 1997 funded 90 percent of the current year school aids and the final payment of prior year aids.

The primary objective of the Statewide Audit is to render an opinion on the state of Minnesota's financial statements included in the Comprehensive Annual Financial Report for fiscal year

1997. The Statewide Audit is designed to also meet the requirements of the Single Audit Act of 1994, revised in 1996, relating to federal financial assistance. Our audit scope focused on the 1997 expenditures of the department as shown in Table 1-1. We also reviewed the loan activity for the Maximum Effort School Loan Fund. These financial activities were material to the state's financial statements and to the Single Audit objectives.

Table 1-1
Expenditures for Selected Programs
Fiscal Year 1997

State Programs:(1)	
General Fund:	
General Education Aid	$2,579,751,603
Special Education Aid	250,105,313
Homestead and Agricultural Credit Aid	117,774,577
Targeted Needs Transportation Aid	68,483,888
Endowment School Fund:	
Endowment School Apportionment Aid	30,602,610
Capital Projects Fund:	
Metropolitan Magnet School Grants	3,139,036
Federal Programs:(2)	
Nutrition Cluster:	
Child Care Food (CFDA #10.558)	66,406,270
National School Lunch (CFDA #10.555)	62,422,571
School Breakfast (CFDA #10.553)	11,228,546
Summer Food Service (CFDA #10.559)	2,509,692
Special Milk Program (CFDA #10.556)	883,177
Educationally Deprived Children (CFDA #84.010)	93,130,339
Handicapped State Grants (CFDA #84.027)	37,088,204
Child Care Development (CFDA #93.596)	32,263,648
Infants and Toddlers (CFDA #84.181)	5,277,365
Vocational Education (CFDA #84.048)	5,038,032

Source: (1) State of Minnesota's Comprehensive Annual Financial Report for fiscal year 1997.
(2) Minnesota's Financial and Compliance Report on Federally Assisted Programs

In Chapters 2 and 3, we discuss our conclusions related to state programs and federal programs, respectively. Chapter 4 discusses issues related to the department's computing environment.

Chapter 2. State Grants and School Aids

Chapter Conclusion

The Department of Children, Families & Learning properly recorded its financial activity in the state's accounting system and complied with material finance-related legal provisions for the items tested except for the following issue. The department did not properly estimate the allowance for uncollectible loans for the Maximum Effort School Loan Fund.

The Department of Children, Families & Learning administered about $3.5 billion for 110 state activities in fiscal year 1997. The department classified these activities into ten program categories in the state's biennial budget report. State resources authorized and budgeted for these programs in fiscal year 1997 included mainly General Fund appropriations, income from the Endowment School Fund, and bond proceeds from the Capital Projects Fund. Table 1-1 in Chapter 1 shows fiscal year 1997 expenditures for those state programs that were material to the state's financial statements and were included in our audit scope. We also reviewed the loans receivable balance reported for the Maximum Effort School Loan Fund, a Special Revenue Fund. Following is a brief description of each of these programs by funding source:

General Fund

- General Education Aid--Provides Minnesota school districts and local educational agencies (schools) general operating revenues to promote adequate and equitable systems of elementary and secondary education. Starting in fiscal year 1997, the general education aid formula includes transportation aid.

- Special Education Aid--Provides funding to schools for partial reimbursement of costs incurred in providing instructions and services for children with disabilities.

- Targeted Needs Transportation Aid--Provides funding to schools for partial reimbursement of transportation costs incurred in providing equal opportunities to students.

- Homestead Agricultural Credit--Provides a formula driven general state aid for property tax relief to residents of specific schools.

Special Revenue Funds

- Maximum Effort School Loan Fund-- Provides loans to assist school district construction projects.

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Endowment School Fund

- Endowment School Apportionment Aid--Provides for the semiannual distribution to the schools of income generated from investment of the Permanent School Fund.

Capital Projects Fund

- Metropolitan Magnet School Grants--Provides funding for the purpose of promoting integrated education for students in pre-kindergarten through grade 12, addressing the inability of schools to provide required construction funds through property taxes.

Audit Objectives and Methodology

The audit objectives of our Statewide Audit work in the department include:

- Determining if the department accurately reported its financial activities in the state's accounting system.
- Determining if the department prepared the Maximum Effort School Loan Fund financial statements in accordance with generally accepted accounting principles.
- Determining if the department complied with material state laws and regulations.

To address these objectives, we conducted interviews and reviewed the department's process for recording the programs' financial activities in MAPS. We gained an understanding of the internal controls over administering selected state grants and school aids. We also tested financial transactions to determine compliance with material finance-related statutory and appropriation requirements. The department is responsible for the proper recording of their financial activities on MAPS.

Conclusion

The Department of Children, Families & Learning properly recorded its financial activity in the state's accounting system and complied with material finance-related legal provisions for the items tested except for the following issue. The department did not properly estimate the allowance for uncollectible loans for the Maximum Effort School Loan Fund. This issue is discussed in Finding 1.

1. The Department of Children, Families & Learning did not properly estimate the allowance for uncollectible capital loans for the Maximum Effort School Loan Fund.

The Department of Children, Families & Learning did not properly calculate the allowance for uncollectible loans for the state's annual financial report. The Legislature authorizes Maximum Effort School loans to school districts. The department's responsibilities for the Maximum Effort School Loan Fund include issuing loans, collecting payments on the outstanding loans, and preparing the fund's financial statements. The department provides loans to school districts for capital projects and debt service. The department did not properly estimate uncollectible loans as of June 30, 1997, on the preliminary statements prepared for the Department of Finance. The statements for the Maximum Effort School Loan Fund are presented by the Department of Finance in the state's annual financial report. School districts owed the state loans totaling about $181 million at June 30, 1997. Further analysis by the department showed that certain districts with capital loans totaling approximately $137 million will be unable to repay loan principal and interest.

The department had not properly analyzed and projected the allowance for uncollectible capital loans for several years. The department completed an analysis in the mid-1980's and established an allowance account totaling about $37 million for five districts. However, the department made several new loans since that time. In addition, various legal changes have affected the ability of school districts to repay the loans. The department, as part of the budget process, completes an analysis of projected loan repayments. However, the department did not use this information to project potential defaulted principal and interest when preparing the financial statements. Current projections show that most of the school districts with capital loans will default on principal and interest over the term of the loan. State law provides that capital loans to school districts are forgiven if not repaid within 50 years. Minn. Stat. Section 124.431, Subd. 12, states in part:

> If any loan is not paid within 50 years after it is granted from the maximum effort debt service levies in excess of required debt service levies, the liability of the school district on the loan is satisfied and discharged and interest on the loan ceases.

We questioned the Department of Finance and the Department of Children, Families & Learning regarding the collectibility of the loans receivable reported on the preliminary financial statements. As a result, the department, in cooperation with Finance, analyzed the potential for future principal and interest defaults. The analysis included a review of the payback of current loans to the year 2044. Minn. Stat. Section 124.31, Subd. 12, extended the loan repayment period to 50 years. Prior to 1990, the loan repayment period was 30 years. The Department of Children, Families & Learning determined that a significant number of the loans were uncollectible. The Department of Finance adjusted the loan receivable balance on the final financial statements issued for fiscal year 1997 to reflect the uncollectible amount.

The department estimates show that 18 of the 21 school districts will not repay the capital loans. Table 2-1 shows the June 30, 1997, loan balance for school districts that are estimated to default on the capital loans by 2044. The levying ability of a district determines the amount of its repayment. Several factors impact the levying ability of the school districts. These factors include current obligations, a limited tax base, minimal growth of the tax base, and no increase in the levy capabilities of the district. If the district has an insufficient levying capability, the district cannot repay the loan principal. The levying capability of school districts may vary during the term of the loan; therefore, the department should review the financial condition of the districts annually.

Financial statement users need reliable financial information to make informed decisions. Financial reporting assists users in evaluating the operating results of the government entity for the year and assessing the level of services that can be provided by the governmental entity. These objectives include providing information about the financial position and condition of the governmental entity. To provide an accurate statement of financial position, the correct amount of loans receivable must be reported. In the case of the Maximum Effort Loan Fund, loans should be analyzed annually to determine the net amount of collectible loans. The estimate of collectible loans is for financial reporting purposes only. The outstanding loans identified as uncollectible remain a legal obligation to the state until forgiven in accordance with statutory provisions.

Table 2-1
School Districts Estimated to Default on Capitol Loans by the Year 2044
As of June 30,1997

School District	Date of Initial Loan	Estimated Uncollectible Loans
Askov	January 1982	$ 3,823,632
Barnum	February 1982	7,742,987
Berth-Hewitt	October 1980	1,775,172
Big Lake	February 1981	12,725,817
Cass Lake	March 1993	7,897,036
Cromwell	February 1993	3,799,008
Foley	February 1990	2,427,917
Hill City	March 1982	8,639,100
Kelliher	October 1996	4,921,843
Lake of the Woods	November 1991	10,245,162
Little Fork-Big Falls	November 1996	4,739,168
Net Lake	November 1993	8,760,089
Oglivie	January 1990	16,230,898
Osakis	December 1991	5,760,648
Red Lake	October 1992	11,936,792
Redwood Falls	May 1991	8,317,959
So. Koochiching	July 1977	14,937,062
Warroad	May 1986	2,298,634
Total Estimated Uncollectible Amount		$136,978,924

Source: Department of Children, Families & Learning determination of uncollectible loans.

Recommendation

- *The Department of Children, Families & Learning should annually review all outstanding loans to properly update the allowance for uncollectible loans reported on the Maximum Effort School Loan Fund financial statements.*

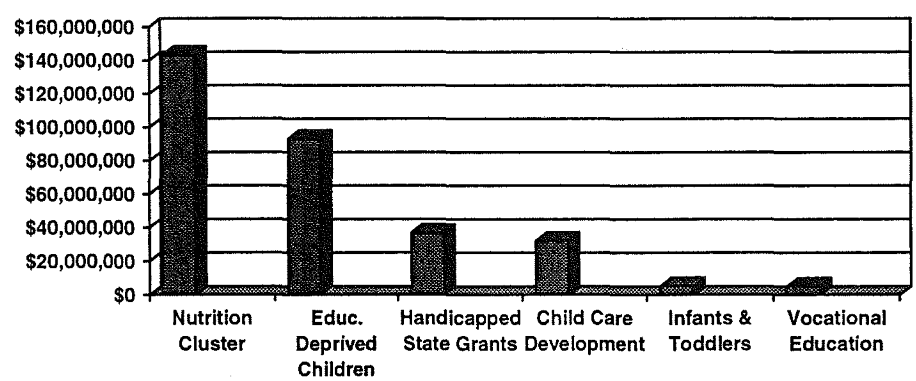
Chapter 3. Federal Programs

Chapter Conclusions

The Department of Children, Families & Learning correctly recorded financial activity in the state's accounting system. However, we noted certain reportable conditions involving internal control over compliance related to the Child Care Development Program and the monitoring process for subrecipients. The department made some incorrect payments under the Child Care Development Program (CFDA #93.575). The Library Services Division did not adequately monitor Single Audit reports for its assigned subrecipients.

The Department of Children, Families & Learning expended about $446 million for 40 federal programs in fiscal year 1997. Based on the provisions of the Single Audit Act our review of federal financial assistance programs included those programs identified in Figure 3-1.

Figure 3-1
Federal Program Expenditures
Fiscal Year 1997



Source: Minnesota's Financial and Compliance Report on Federally Assisted Programs.

Following is a brief description of each of the selected programs.

- Nutrition Cluster Programs (CFDA #s 10.553, 10.555, 10.556, 10.558, and 10.559)--Programs in this cluster include School Breakfast, National School Lunch, Special Milk, Child and Adult Food Care, and Summer Food Service. These programs provide funding for low income persons that need nutritional foods.

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- Title I-Educationally Deprived Children (CFDA #84.010)-- Provides supplemental assistance to students from low income families to help them meet the state's high standards of academic performance.

- Handicapped State Grants (CFDA #84.027)--Provides funding for the public education of handicapped children.

- Child Care & Development Block Grant (CFDA #93.576)--Provides funding to assist low-income families obtain quality child care.

- Vocational Education (CFDA #84.048)--Provides funding for training secondary students and adults to adapt to changing technological and labor market conditions.

- Infants and Toddlers with Disabilities (CFDA #84.181)--Provides funding for early intervention services for infants and toddlers with disabilities and their families.

Audit Objectives and Methodology

The objectives of the Single Audit Act related to federal financial assistance were to:

- Consider internal control over compliance with requirements that could have a material and direct effect on the federal programs;

- Determine whether the department recorded financial activities properly; and

- Determine whether the department complied with material federal rules and regulations applicable to selected federal programs.

To address these objectives, we conducted interviews and reviewed the department's internal controls for managing the selected programs in compliance with federal laws and regulations. We also tested financial transactions for the selected programs to determine compliance with the programs' regulations.

The U. S. Office of Management and Budget Compliance Supplement provides a listing of compliance requirements for federal programs. Our audit scope included testing the department's compliance with the applicable requirements identified in the Compliance Supplement.

Conclusion

The Department of Children. Families & Learning correctly recorded financial activity in the state's accounting system. However, we noted certain reportable conditions involving internal control over compliance related to the Child Care Development Program and the monitoring process for subrecipients. The department made some incorrect payments under the Child Care Development Program (CFDA #93.575) as discussed in Finding 2. The Library Services Division did not adequately monitor Single Audit reports for its assigned subrecipients as discussed in Finding 3.

2. The department improperly reimbursed some counties for AFDC Child Care.

The department incorrectly reimbursed two counties from the Child Care and Development Program (CFDA #93.596). This federal program provides child care assistance to families through the AFDC program. Federal funds partially reimburse counties for their actual AFDC program expenditures for providing child care assistance to low-income families. The department incorrectly reimbursed two counties in fiscal year 1997 primarily due to isolated keying errors. Table 3-1 shows the correct amount of the reimbursement, the amount actually paid, and the incorrect amount. The department made a net underpayment of $349,000.

Table 3-1
Payments to Selected Counties

County	Correct Amount	Payment Amount	Difference
Dakota	$202,151	$222,151	$ 20,000
Ramsey	$410,665	$ 41,665	($369,000)
Net Difference	$612,816	$263,816	($349,000)

Source: Department of Children, Families & Learning records.

Recommendation

- *The department should correct the payments made in error in fiscal year 1997.*

3. The Library Services Division does not adequately monitor subrecipients as required by federal regulations.

The Library Services Division of the Department of Children, Families & Learning did not monitor subrecipients as required by the Single Audit Act. The Education Finance, Food and Nutrition, and Library Service Divisions within the department are responsible for monitoring subrecipients. However, Library Services did not complete the control activities applicable to its assigned subrecipients.

The Education Finance Division determines whether subrecipients meet thresholds requiring a Single Audit, and this division monitors the receipt of audit reports. Food and Nutrition and Library Services are responsible to track and resolve specific audit findings for assigned subrecipients. However, the Library Services Division did not review its assigned subrecipient reports. Library Services also did not maintain a system to track and follow-up on material findings and did not resolve issues with the subrecipients.

Recommendation

- *The Library Services Division should follow subrecipient monitoring procedures used in other department areas to ensure that subrecipients are in compliance with federal requirements.*

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Chapter 4. The Computing Environment

Chapter Conclusions

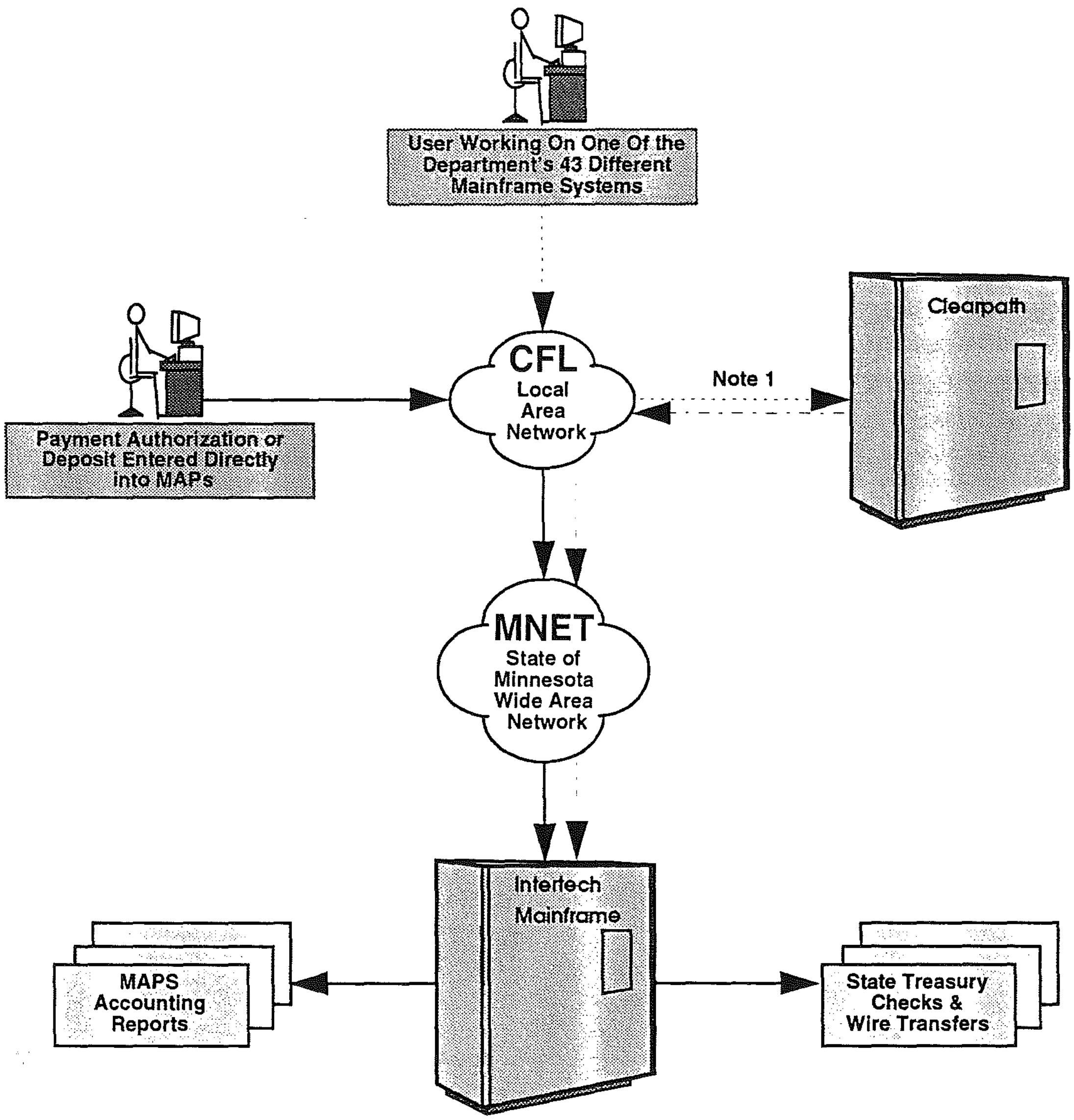
The Information Technologies Division in the Department of Children, Families & Learning has made improvements but still lacks important quality control mechanisms in some areas. Security controls that govern access to the department's systems continue to be inadequate for many applications. The department still has not implemented a comprehensive disaster recovery plan. Key technical and user documentation remains limited. Finally, the department places an unreasonable level of reliance on the internal knowledge of key system users. These employees operate applications on a daily basis with no employee back-up.

The Department of Children, Families & Learning is a large, complex state agency. The department maintains approximately 43 different mainframe-based computerized information systems. In addition, the department has a large number of information systems that run on personal computers and its local area network. Employees in the Information Technologies Division developed and support most of these systems.

The department purchased a new Unisys Clearpath Enterprise Server in January 1997. This new system replaced a lease agreement the department had with a private organization, Metro II Educational Service Center. The annual lease agreement with Metro II cost the department approximately $430,000 per year. The cost of the new Clearpath mainframe was $726,000 with annual subscription and maintenance costs of approximately $100,000. The department fully implemented the Clearpath system for all department software and data in April 1997. Employees access mainframe systems through the department's local area network.

The department uses the Minnesota Accounting and Procurement System (MAPS) to account for its financial activities and make payments to vendors. MAPS resides on the state's central mainframe computer center, administered by the Department of Administration. The department enters many transactions directly in MAPS. However, it also electronically transfers a substantial amount of payment data from Clearpath to MAPS. Figure 4-1 illustrates the primary components of the computing environment at the Department of Children, Families & Learning.

Figure 4-1
The Computing Environment at the Department of Children, Families & Learning
As of December 1997



Note 1: Some of the department's mainframe applications have features that allow users to transfer data from Clearpath to MAPS.

Source: Auditor prepared from discussions with employees in the Information Technologies Division.

Controlling access to computer resources and sensitive data is difficult in complex computing environments. To make effective access decisions, the department must determine what computer resources and data every employee needs to access to complete their job responsibilities. The department also must be familiar with the various security software packages that control the access to those computer resources and data. For example, the department runs Novell Netware and Windows NT software on its local area network. Novell and Windows NT have their own security modules that control access to the network. The department developed its own program logic to control access to the computerized systems that run on Clearpath. A different security software package named ACF2 protects the state's central mainframe computers. Finally, a software package called CORE controls access to the various MAPS screens and data. Employees in the Department of Children, Families & Learning must make important security decisions for each of these software packages.

Employees follow a four-step process to access information systems that reside on Clearpath. They begin by entering their unique user identification code and password to access the department's local area network. Once on the network, a terminal emulation package connects the user to the Clearpath mainframe. Each information system on Clearpath has a generic identification code and password. Users also must enter a second shared password to access a menu of available system options.

Audit Scope, Objectives, and Methodology

We reviewed computer access controls as part of our annual financial audit of the Department of Children, Families & Learning in fiscal year 1996. For fiscal year 1997, we limited our work to interviews of key department personnel to identify changes in the computing environment and follow-up on prior audit issues. These discussions focused on how the department secures its computerized information systems and data that now reside on the new Clearpath mainframe and what steps the department has taken to address prior audit issues.

Conclusion

The Information Technologies Division within the Department of Children, Families & Learning has made improvements during fiscal year 1997. However, the department still lacks important quality control mechanisms in some areas. Finding 4 discusses the inadequacies of security controls for many applications. Finding 5 discusses the department's failure to implement a comprehensive disaster recovery plan. Finally, Finding 6 discusses the weakness in the cross-training of employees.

4. PRIOR FINDING PARTIALLY RESOLVED: Security controls over information systems are weak in several respects.

The fiscal year 1996 audit of the Department of Children, Families & Learning identified a control weakness giving users an inappropriate level of clearance to several sensitive computer programs and data. Entering the code and password for a system effectively gives users access to the region on the mainframe where key system programs and data are stored. The department has been working during fiscal year 1997 to resolve this issue in conjunction with Project 2000. Information systems are systematically being redesigned to restrict employee access to sensitive areas and be compliant by the year 2000. About one-third of the department's information systems have been redesigned, but there are still systems where employees have an unnecessary level of clearance.

Allowing users to share passwords is also a weakness in the department's access controls. Unique identification codes and passwords are an important control because they help authenticate system users. They also make specific users accountable for all transactions and computer activities. Currently, it may not be possible to trace computer activities or transactions to a specific user.

Recommendations

- *The department should continue to redesign their systems to only give users access to the computer resources and data that they need to fulfill their job responsibilities.*

- *The department should assign every system user a unique identification code and password so that computing events can be traced to people.*

5. PRIOR FINDING PARTIALLY RESOLVED: The Department of Children, Families & Learning may have difficulty recovering its critical business functions in a crisis situation.

In fiscal year 1996, we found that the Department of Children, Families & Learning did not have any written disaster recovery procedures. In addition, the high-level technical documentation we reviewed was very limited and not updated to reflect system changes. Therefore, should a disaster occur, the department may have difficulty recovering its critical business functions. During fiscal year 1997, the department developed a proposal for a Business Continuation Program with the Department of Administration's InterTechnologies Group. This proposal, if implemented, would provide an effective plan for disaster recovery of information systems and data, along with other critical business function information crucial to the operation of the department. Until effective disaster recovery procedures are developed, the department information systems will continue to be at risk.

Recommendations

- *The department should work with the InterTechnologies Group to fully implement the business continuity proposal.*

- *The department should establish technical and user documentation standards and update documentation to reflect system changes.*

6. The Department of Children, Families & Learning did not adequately cross-train users of the information systems.

The Department of Children, Families & Learning places an unreasonable level of reliance on the internal knowledge of key employees. These employees operate an application on a daily basis with little or no back-up by other employees. The most serious example is the department's IDEAS (Integrated District Education Aids System) program. This application calculates state aid payments due to school districts and is responsible for the accurate expenditure of over $3 billion annually. The department's Office of Information Technologies designed this program. One employee in Education Finance is responsible for the day-to-day operation of this application. This employee has a good understanding of the application and how to use the system to account for state aid programs. No other employee could effectively operate the system if this employee should leave.

Cross-training would provide instruction for other employees to operate specific applications. This training also provides for continual processing of state aid payments if the current employee is unavailable. Without this training, state aids to school districts may be severely impacted.

Recommendation

- *The department should provide cross-training for users of the information systems to ensure that more than one employee can operate an application.*

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Status of Prior Audit Issues
As of December 19, 1997

Most Recent Audit

February 28, 1997, Legislative Audit Report 97-12 focused on selected state and federal programs as part of the Statewide Financial and Federal Compliance Audit. The audit covered expenditures in fiscal year 1996 material to the state's financial statements and the Single Audit. The department implemented the recommendations discussed in the audit except for certain issues related to the computing environment. The department allocated additional funding to resolve issues concerning the computing environment. Two prior findings were partially resolved. First, security controls over information systems remain weak in several respects. (See Finding 4 in the current report.) Secondly, the department may have difficulty recovering its critical business functions in a crisis situation. (See Finding 5 for the current status of this issue.) The department is in the process of resolving the two issues; however, to fully address these findings requires an extended period of time.

Other Audit History

March 29, 1996, Legislative Audit Report 96-12 objectives were similar to the Legislative Audit Report 97-12 described above. The audit covered fiscal year 1995 expenditures material to the state's financial statements and the Single Audit. The report included some issues related to the administration of federal programs. These issues were corrected by the department in 1996.

State of Minnesota Audit Follow-Up Process

The Department of Finance, on behalf of the Governor, maintains a quarterly process for following up on issues cited in financial audit reports issued by the Legislative Auditor. The process consists of an exchange of written correspondence that documents the status of audit findings. The follow-up process continues until Finance is satisfied that the issues have been resolved. It covers entities headed by gubernatorial appointees, including most state agencies, boards, commissions, and Minnesota state colleges and universities. It is not applied to audits of the University and quasi-state organizations, such as the metropolitan agencies or the State Agricultural Society. the state constitutional officers, or the judicial branch.

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February 23, 1998

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

Dear Mr. Nobles:

Enclosed are responses to findings from the Fiscal Year 1997 Statewide Audit.

We would like the opportunity to thank the audit team for their helpfulness and professionalism. Please contact John Bulger, Director of Finance and Management Services at 297-4725 if there are any questions regarding our response.

Sincerely,

Robert J. Wedl
Commissioner

RJW/JB

Enclosures

DEPARTMENT OF CHILDREN, FAMILIES & LEARNING
AUDIT RESPONSE - STATEWIDE AUDIT FOR F.Y. 1997

Finding #1

The Department of Children, Families & Learning did not properly estimate the allowance for uncollectable capital loans for the Maximum Effort School Loan Fund.

Recommendation:

The Department of Children, Families & Learning (CFL) should annually review all outstanding loans to properly update the allowance for doubtful accounts for uncollectable loans reported on the Maximum Effort School Loan Fund financial statements.

Agency Response:

General Comments about the Maximum Effort School Loan Program:

The Maximum Effort School Loan program provides financial support to school districts. Capital loans provide funds to districts that have capital bonding needs that are greater than the local property tax base can reasonably support and/or greater than the maximum bonding capacity. The Debt service loan provide debt service property tax relief to districts with high debt service tax rates. There are state general fund appropriations (open appropriation) for payment of principal and interest on the state bonds to the extent repayments from the districts are inadequate to make the required bond fund payments.

Capital loans can only be used for the replacement of facilities that are dangerous to the health and safety of children, or to provide facilities where no adequate facilities exist and such facilities could not be made available through consolidation or leasing. Debts service loans are available to districts if the districts adjusted net debt service levy is at least 10% or $5,000 greater than the maximum effort debt service levy. Districts having an outstanding capital loan or debt service loan must levy the greater of the maximum effort debt service levy or the required debt service levy less any reduction for a debt service loan and debt service aid. Interest payments on capital loans and debt service loans are due each December. Any unpaid interest is added to the principal of the loan. The repayment of the loan is determined by either the annual debt excess in the debt redemption fund or the amount of the Maximum Effort debt service levy over the required debt service levy of that year or refunding of the state loans with general obligation bonds. The required debt service levy is what the local school district bond schedule specifies the amount to be levied for the district's bonded debt. It is equal to at least 105% of principal and interest for the ensuing fiscal year. Capital loan applications are reviewed by the department and the legislature debates, creates and approves all capital loans. The

Department of Children, Families & Learning is required to implement the loans according to current law.

By Minnesota Statutes (124.36-124.46), all Maximum Effort School Loans are receivable. Under current law, if the capital loan is not repaid within 50 years from the date of issue, it is canceled and the district's liability ceases. The Department of Children, Families & Learning reported the loans to Department of Finance according to current state law.

Financial Statement Responsibility

The Department of Children, Families & Learning does prepare preliminary state financial statements for this program. The Department of Children, Families & Learning provides data to Department of Finance for this purpose but CFL does not prepare the final financial statements for this program. State financial statement preparation is clearly a Department of Finance responsibility and the Department of Finance has the expertise in accounting standards and methodology to properly prepare these financial statements. The Department of Finance has not provided the Department of Children, Families & Learning with draft copies of relevant portions of the final financial statements or asked for CFL comments after changes were made to submitted data.

Calculating the allowance for uncollectable capital loans for the Maximum Effort School Loans

When Department of Finance requires information from The Department of Children, Families & Learning to prepare financial statements, the Department of Finance normally requests this information in writing, provides specific due dates, and provides instructions on how the estimates are to be prepared. The Department of Children, Families & Learning calculated an allowance of doubtful accounts under the agreed methodology specified by Department of Finance and the Legislative Auditor in 1985. In 1994, when the Legislature changed the Maximum Effort School Loan law and in 1997 when additional changes were made to the district loan repayment calculations, no changes were made in reporting methodology of data to the Department of Finance.

This program has been reviewed by Legislative Auditor periodically in the last 12 years and no findings were found in previous audits with the calculation methodology or the preparation of data provided to the Department of Finance for the Maximum Effort School Loan program.

Capital loans are included in the Governor's capital budget requests, which is put together by the Finance Department with input from the Department of Children, Families & Learning and other agencies, and require specific legislative approval. Materials prepared by the Department for each capital loan request, and provided to the Finance Department as part of the budget process, include analysis of whether or not the loan will be paid back based on current economic data. These materials clearly indicated that many of the loans would not be repaid. The Department of Children, Families & Learning analysis of these issues is reviewed and discussed in legislative hearings before the loans are approved. As part of the legislative process, the Department of Finance tracks both the executive budget proposals and enacted legislation. It would be reasonable for the Department of Children, Families & Learning to assume that given the CFL analysis and the legislative record, that Department of Finance would routinely be aware of the loans not likely to be repaid at the time of issuance, and would track these accordingly and show them as uncollectable on the state's financial statements.

Children, Families & Learning maintains records on loan repayments and provides periodic updates on the status of loans to Department of Finance. These materials should have alerted Department of Finance of any material changes in the projections of capital loan repayments made at the time the loans were issued.

Agency Response:

The Department of Children, Families & Learning will comply fully with the recommendations of the Legislative Auditor. The Department of Children, Families & Learning will work with the Department of Finance to determine procedures and methodologies as is currently done with other information required by Department of Finance, including written notice of due dates and procedures to be followed for making the estimates.

Don Johnson and Bill Kiesow of the Department are responsible for the implementation of the agency response. We will work with the Department of Finance and the Legislative Auditor's Office on the next financial report for the Maximum Effort School Loan program.

Finding #2

The department improperly reimbursed some counties for AFDC Child Care.

The improper payment was due to a keypunch error.

Recommendation:

The Department should correct the payments made in error in fiscal year 1997.

Agency Response:

The department has corrected the keypunch error.

Don Johnson is responsible for the resolution of this finding. The correction has been made.

Finding #3

The Library Services Division does not adequately monitor subrecipients as required by federal regulations.

Recommendation:

The Library Services Division should follow subrecipient monitoring procedures used in other department areas to ensure that subrecipients are in compliance with federal requirements.

Agency Response:

The department will follow subrecipient monitoring procedures used in other areas to ensure that subrecipients are in compliance with federal regulations.

Joyce Swonger is responsible for the resolution of this finding. New monitoring procedures will be implemented immediately.

Finding #4

Prior finding partially resolved: Security controls over information systems are weak in several respects.

Recommendation:

The Department should continue to redesign their systems to only give users access to the computer resources and data that they need to fulfill their job responsibilities.

Agency Response:

The department is continuing the redesign of systems to increase security and restrict access to resources and data only to individuals that need to fulfill their job responsibilities.

Carol Hokenson is responsible for resolution of this audit finding. The department is currently working to resolve this issue.

Recommendation:

The department should assign every system user an unique identification code and password so that computing events can be traced to people.

Agency Response:

The department is in the process of increasing computer security.

Carol Hokenson is responsible for resolution of this audit finding. The department is currently working to resolve this issue.

<u>Finding #5</u>

Prior Finding Partially Resolved: The Department of Children, Families & Learning may have difficulty recovering its critical business functions in a crisis situation.

<u>Recommendation:</u>

The department should work with the InterTechnologies Group to fully implement the business continuity proposal.

<u>Agency Response:</u>
The department is in the process of entering into a contract with InterTechnologies Group to fully implement the business continuity proposal.

Carol Hokenson is responsible for resolution of this audit finding. The department is currently working to resolve this issue.

<u>Recommendation:</u>

The department should establish technical and user documentation standards and update documentation to reflect system changes.

<u>Agency Response</u>:
The department is continuing to work on technical and user documentation standards and to update documentation to reflect system changes.

Carol Hokenson is responsible for resolution of this audit finding. The department is currently working to resolve this issue.

<u>Finding #6</u>

The Department of Children, Families & Learning did not adequately cross-train users of the information systems.

<u>Recommendation:</u>

The department should provide cross-training for users of the information system to ensure that more than one employee can operate an application.

<u>Agency Response:</u>

The department is providing cross training for users of the information systems to ensure that more than one employee can operate an application.

Carol Hokenson (computers systems) and Tom Melcher (IDEAS) are responsible for resolution of this audit finding. The department is currently working to resolve this issue.