Department of Natural Resources

Statewide Audit - Selected Audit Areas
For the Year Ended June 30, 1998

February 1999

Financial Audit Division
Office of the Legislative Auditor
State of Minnesota

99-8

Centennial Office Building, Saint Paul, MN 55155 ● 651/296-4708

SUMMARY

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Department of Natural Resources

Statewide Audit
Selected Audit Areas
For the Year Ended June 30, 1998

Public Release Date: February 4, 1999 No. 99-8

Background Information

The Department of Natural Resources 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 (Waters, Forestry, Parks and Recreation, Enforcement, Minerals, Fish and Wildlife, and Trails and Waterways), departmental field operations, and support services. Mr. Rodney Sando was the commissioner of the department during the audit period.

Selected Audit Areas and Conclusions

Our audit scope was limited to those activities material to the State of Minnesota's Comprehensive Annual Financial Report for the year ended June 30, 1998. Our primary audit objective was to render an opinion on the State of Minnesota's financial statements. Our scope within the Department of Natural Resources included timber sales and iron ore rents and royalties revenues, flood damage reduction and Metropolitan Council grants, and sportfish and wildlife restoration expenditures.

We qualified our report, dated December 1, 1998, on the State of Minnesota's Comprehensive Annual Financial Report because insufficient audit evidence exists to support the State of Minnesota's disclosures with respect to the year 2000. Similarly, we do not provide assurance that the Department of Natural Resources is or will be year 2000 ready, that its year 2000 remediation efforts will be successful in whole or in part, or that parties with which the Department of Natural Resources does business will be year 2000 ready.

For the areas audited, the Department of Natural Resources' financial activities were fairly presented in the general purpose financial statements of the State of Minnesota's Comprehensive Annual Financial Report for the year ended June 30, 1998. As a result of our audit procedures, we identified one instance of noncompliance with finance-related legal provisions. We found that the department was not receiving and depositing iron ore rents and royalties in accordance with applicable statutory provisions. For the federal sportfish and wildlife restoration programs, the department complied, in all material respects, with the types of compliance requirements described in the U.S. Office of Management and Budget Circular A-133 Compliance Supplement that are applicable to each of its major federal programs for the year ended June 30, 1998.

The Department of Natural Resources agreed with the audit finding and is working towards it resolution.

Department of Natural Resources

Table of Contents

Audit Participation

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

Claudia Gudvangen, CPA	Deputy Legislative Auditor
Jeanine Leifeld, CPA	Audit Manager
Sonya Johnson, CPA	Auditor-in-Charge
Mike Willis	Auditor

Exit Conference

The findings and recommendations in this report were discussed with the following officials of the Department of Natural Resources at an exit conference held on January 19, 1999:

Peggy Adelmann	Administrator, Office of Management and Budget
Jerry Hampel	Business Manager, Office of Management and Budget
Lori Caspers	Business Manager, Fish and Wildlife Division
Kathy Lewis	Mineral Leasing Manager
Joyce Nyhus	Business Manager, Forestry Division

STATE OF MINNESOTA
OFFICE OF THE LEGISLATIVE AUDITOR
JAMES R. NOBLES, LEGISLATIVE AUDITOR

Senator Deanna Wiener, Chair
Legislative Audit Commission

Members of the Legislative Audit Commission

Mr. Allen Garber, Commissioner
Department of Natural Resources

We have performed certain audit procedures at the Department of Natural Resources as part of our audit of the financial statements of the State of Minnesota as of and for the year ended June 30, 1998. We also have audited certain federal financial assistance programs administered by the Department of Natural Resources as part of our audit of the state's compliance with the requirements described in the U.S. Office of Management and Budget (OMB) *Circular A-133 Compliance Supplement* that are applicable to each of its major federal programs for the year ended June 30, 1998. We emphasize that this has not been a comprehensive audit of the Department of Natural Resources.

Table 1-1 identifies the financial activities within the Department of Natural Resources that were material to the state's financial statements. We performed certain audit procedures on these Department of Natural Resources programs as part of our objective to obtain reasonable assurance about whether the State of Minnesota's financial statements were free of material misstatement.

Table 1-1
Department of Natural Resources
Programs Material to the State's Financial Statements
Fiscal Year 1998
(in thousands)

	Amount
Revenue Areas	
Timber Sales (Permanent School Fund)	$ 5,977
Iron Ore Rents and Royalties (Permanent School Fund)	6,556
Total	$12,533
Expenditure Areas	
Grants to the Metropolitan Council	$ 4,350
Flood Damage Reduction Grants	3,141
Total	$ 7,491

Source: State of Minnesota Comprehensive Annual Financial Report and Minnesota Accounting and Procurement System (MAPS) for fiscal year 1998.

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Department of Natural Resources

Table 1-2 identifies the State of Minnesota's major federal programs administered by the Department of Natural Resources. We performed certain audit procedures on these Department of Natural Resource programs as part of our objective to obtain reasonable assurance about whether the State of Minnesota complied with the types of compliance requirements that are applicable to each of its major federal programs.

Table 1-2
Major Federal Programs Administered by the Department of Natural Resources
Fiscal Year 1998
(in thousands)

Program Name	Federal Share	State Share	Total
Sportfish Restoration (CFDA 15.605)	$9,918	$3,283	$13,201
Wildlife Restoration (CFDA 15.611)	$4,450	$1,483	$ 5,933

Source: Minnesota Accounting and Procurement System (MAPS) for fiscal year 1998.

We conducted our audit in accordance with generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Conclusions

We qualified our report dated December 1, 1998, on the State of Minnesota's Comprehensive Annual Financial Report, because of uncertainties about the potentially adverse effect the year 2000 computer issue may have on state operations. Information technology experts believe that many computer applications in private businesses and government may fail as a result of data integrity problems and erroneous calculations beyond December 31, 1999. Insufficient audit evidence exists to support the State of Minnesota's disclosures with the respect to the year 2000 issue. Because of the unprecedented nature of the year 2000 issue, its effects and the success of related remediation efforts will not be fully determinable until the year 2000 and thereafter.

Similarly, we do not provide assurance that the Department of Natural Resources is or will be year 2000 ready, that its year 2000 remediation efforts will be successful in whole or in part, or that parties with which the Department of Natural Resources does business will be year 2000 ready.

In accordance with *Government Auditing Standards*, we have also issued our report, dated December 1, 1998, on our consideration of the State of Minnesota's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grants. At a later date, we will issue our report on compliance with requirements applicable to each major federal program and internal control over compliance in accordance with OMB Circular A-133.

For the areas audited, the Department of Natural Resources' financial activities were fairly presented in the general purpose financial statements of the State of Minnesota's Comprehensive Annual Financial Report for the year ended June 30, 1998. However, as cited below, as part of our audit procedures, we identified one instance of noncompliance with finance-related legal provisions. For the federal programs tested, the department complied, in all material respects, with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) *Circular A-133 Compliance Supplement* that are applicable to each of its major federal programs for the year ended June 30, 1998.

1. The Department of Natural Resources (DNR) did not comply with certain statutory depositing requirements for iron ore rents and royalties.

The Department of Natural Resources did not receive all iron ore rents and royalties in the timeframes outlined in Minn. Stat. Section 93.20. The department also did not deposit those rents and royalties on a daily basis as required by Minn. Stat. Section 16A.275.

The Minerals Division of the Department of Natural Resources manages the mineral rights to state-owned trust and tax forfeited land. The division negotiates the leases on these lands for the mining of iron ore, as well as other minerals. Mining companies pay rent and royalty payments under these leases. Rental payments are a uniform amount the lessee pays whether or not there is any mining or ore removal done on the land. Royalty payments are payments made by lessees for any ore that is removed from leased lands. The amount of either the rent or the royalty is determined by statute according to the type of lease.

The department did not receive all of its rent and royalty payments according to the statutory timeframes. Minn. Stat. Section 93.20, subd. 7 and 19, require that rent and royalty payments are due on or before the twentieth day of the month following the end of each calendar quarter. During our review of iron ore rent and royalties, we found that in 9 of 12 items tested, mining companies did not make the required iron ore rent and royalty payments by the twentieth day of the month following the end of the quarter. Payments were made anywhere from one to twelve days late, with amounts ranging from $3,750 to $637,250. Since there is no penalty for late payments outlined in statute, the department has limited recourse against companies which do not pay on time.

The department also did not always deposit incoming iron ore rents and royalties daily, as required by Minn. Stat. Section 16A.275. In 2 of 12 items tested, DNR deposited incoming payments, totaling $55,500, late. In those cases, department staff stated that the incoming receipts were probably forwarded to the Minerals Division rather than directly to DNR's Office of Management and Budget, which prepares the deposit and posts to the state's accounting system.

Recommendations

- *The Department of Natural Resources should evaluate the reasonableness of the timeframe outlined in Minn. Stat. Section 93.20 for payment of iron ore rents and royalties. The department should enforce the statutory timeframe or institute a change to the statute.*

- *The Department of Natural Resources should ensure that all iron ore rent and royalties receipts are submitted to the Office of Management and Budget* *section to ensure that receipts are deposited timely as outlined in Minn. Stat. Section 16A.275.*

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 this report, which was released as a public document on February 4, 1999.

James R. Nobles
Legislative Auditor

Claudia J. Gudvangen
Deputy Legislative Auditor

End of Fieldwork: December 22, 1998

Report Signed On: February 1, 1999

Status of Prior Audit Issues
As of December 22, 1998

August 22, 1997, Legislative Audit Report 97-42 examined selected Department of Natural Resources revenues and payroll expenditures for the 21-month period from July 1, 1995, through March 31, 1997. The scope included license center receipts, timber sales, and mineral rents and royalty receipts, as well as department-wide payroll expenditures.

There were no written issues in this report.

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 of Minnesota, any quasi-state organizations, such as the Metropolitan agencies or the State Agricultural Society, the state constitutional officers, or the judicial branch.

Minnesota Department of Natural Resources

OFFICE OF THE COMMISSIONER
500 Lafayette Road
St. Paul, Minnesota 55155-4037

January 28, 1999

Mr. James R. Nobles
Office of the Legislative Auditor
1st Floor Centennial Building
658 Cedar St.
St. Paul, MN. 55155

Dear Mr. Nobles:

Thank you for the opportunity to respond in writing to the Statewide Audit of the Department of Natural Resources for the year ended June 30, 1998. First let me commend your staff for their good work and professionalism in conducting this audit.

Recommendation: The Department of Natural Resources should evaluate the reasonableness of the timeframe outlined in Minn. Stat. Section 93.20 for payment of iron ore rents and royalties. The department should enforce the statutory timeframe or institute a change to the statute.

Recommendation: The Department of Natural Resources should ensure that all iron ore rent and royalties receipts are submitted to the Office of Management and Budget section to ensure that receipts are deposited timely as outlined in Minn. Stat. Section 16A.275.

Department of Natural Resources Response: In most cases the statutory time frame has worked. In a few instances payment is received after the due date. Of the twelve payment items sampled in the audit only two were more than three days late. Late payments can be due to unusual circumstances. For example, the latest payment sampled was from USX and involved a major series of agreements including the exchange of state leases with Ontario Iron Company. Changing the statute would be a significant piece of legislation; and would still necessitate the amendment of each lease, with agreement of the lessee. We think a better approach is to continue to work closely with the mining companies to ensure that payments are received by the statutory date.

Accordingly the Minerals Division will re-emphasize to each iron ore and taconite lessee the requirement to adhere to the payment schedule requirements. Kathy Lewis will draft a letter by February 15, 1999, that will address the following issues. First, it will stress the requirement for receipt of payment of rents and royalties on or before the 20th of January, April, July and October. Second, it will solicit recommendations from the mining companies on how DNR can help them to make timely payments. Electronic transfer of funds has been identified by the mining companies as method to expedite deposit of receipts. Third, it will remind them to send payments directly to Office of Management and Budget Services for immediate deposit. In addition, the Minerals Division will monitor receipts and work with individual companies where a pattern of late payments could indicate problems.

We believe that these steps should resolve the recommendations. Again thank you for your fine work.

Sincerely,

Ray Hitchcock
Acting Commissioner