Minnesota Indian Affairs Council

Financial Related Audit
For the Period July 1, 1995, through June 30, 1998

July 1999

Financial Audit Division
Office of the Legislative Auditor
State of Minnesota

99-34

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SUMMARY

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Public Release Date: July 15, 1999 No. 99-34

Council Background

The Minnesota Indian Affairs Council was created by the Legislature in 1963, and is the official liaison between the state and its eleven tribal governments. The council provides the Legislature with information about the nature of tribal governments, the relationship of tribal governments to the Indian people of Minnesota, and other Indian affairs issues. The council administers various programs intended to strengthen economic opportunities and protect cultural resources. For example, the council administers the Indian business loan program, offering Minnesota-based Indians the opportunity to establish or expand a business enterprise in Minnesota by providing low-interest loans.

The current chair of the council is Dallas Ross. The executive director, appointed by the council, is Joseph B. Day. The council has seven other staff positions.

Audit Scope and Conclusions

Our audit scope included the three fiscal years ending June 30, 1998, and covered the financial activity of the Indian business loan program and certain administrative expenditure categories, including payroll, professional/technical services, travel, and rent.

The council did not administer the Indian business loan program in a reasonable and prudent manner, and did not comply with some statutory provisions and state policy. Findings 1 through 8 in Chapter 2 discuss the council's significant weaknesses in its administration of this program.

The council's administrative expenditures were generally reasonable and prudent; however, Finding 9 explains that the council did not pay employees in accordance with applicable bargaining agreements, and Findings 10 - 12 describe weaknesses in the way the council obtained certain goods and professional/technical services. Finding 13 explains the council's noncompliance with state policies related to accounting for and labeling its personal property.

In its response, the council indicated that it plans to implement the recommendations in the report in a timely manner.

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

Representative Dan McElroy, Chair
Legislative Audit Commission

Members of the Legislative Audit Commission

Mr. Dallas Ross, Chair
Minnesota Indian Affairs Council

Members of the Minnesota Indian Affairs Council

Mr. Joseph B. Day, Executive Director
Minnesota Indian Affairs Council

We have conducted a financial related audit of the Minnesota Indian Affairs Council for the period July 1, 1995, through June 30, 1998. Our audit scope included the Indian business loan program and certain administrative expenditure categories, including payroll, purchased goods and services, travel, and rent.

We conducted our audit in accordance with generally accepted auditing standards and *Government Auditing Standards* 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 also require that we design the audit to provide reasonable assurance that the Minnesota Indian Affairs Council complied with provisions of laws, regulations, contracts, and grants that are significant to the audit. Management of the Minnesota Indian Affairs Council is responsible for establishing and maintaining the internal control structure and complying with applicable laws, regulations, contracts, and grants.

We intend this report to be for the information of the Legislative Audit Commission and management of the Minnesota Indian Affairs Council. We do not, however, limit the distribution of this report, which we released as a public document on July 15, 1999.

James R. Nobles
Legislative Auditor

Claudia J. Gudvangen, CPA
Deputy Legislative Auditor

End of Fieldwork: May 21, 1999

Report Signed On: July 7, 1999

Minnesota Indian Affairs Council

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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
Cecile Ferkul, CPA, CISA	Audit Manager
Scott Tjomsland, CPA	Auditor-in-Charge
Charles Klein	Auditor

Exit Conference

We discussed the issues in this report with the following staff of the Minnesota Indian Affairs Council on June 22, 1999:

Joseph Day	Executive Director
Jim Jones, Jr.	Cultural Resource Specialist
Bobbie Jo Donat	Executive Assistant
Sharon Romano	Staff Assistant

Chapter 1. Introduction

The Minnesota Indian Affairs Council was created by the Legislature in 1963. It is the official liaison between the state's eleven tribal governments and the State of Minnesota. The council strives to protect the sovereignty of the tribes and ensure the well being of American Indian citizens throughout the state. The council's vision, as stated in its 1997 Annual Report, is to attain social, economic, and political justice for all American Indian people living in the state, while embracing traditional Indian culture and spiritual values.

The council's membership consists of the elected chair of each of the eleven tribal governments and two at-large members who represent Indians residing in Minnesota, but not from a Minnesota-based tribe. The council's current chair is Dallas Ross. The council appoints an executive director to manage its day-to-day operations. Since 1994, the council's executive director has been Joseph B. Day. The executive director oversees seven staff. As of March 1999, three of the council's staff positions were vacant. The council's main office is in Bemidji; the council also has an office in St. Paul.

The council provides the Legislature with information about the nature of tribal governments, the relationship of tribal governments to the Indian people of Minnesota, and Indian affairs issues. The council monitors legislation and informs the tribal communities about the impact of that legislation. The council also serves as an intermediary between tribal communities and state agencies, allowing for the discussion of issues and concerns in an environment that encourages resolution.

The council administers various programs intended to strengthen economic opportunities and protect cultural resources. For example, the council administers the Indian business loan program, offering Minnesota-based Indians the opportunity to establish or expand a business enterprise in Minnesota by providing low-interest loans. As discussed in Chapter 2, we found significant weaknesses in the council's administration of this program. Table 2-1 in Chapter 2 recaps the program's financial activity.

Table 1-1 below summarizes the council's available resources and its expenditures during the audit period. In Chapter 3 we discuss the major administrative expenditure areas, including payroll, professional/technical services, travel, and rent. Findings in the chapter explain that the council did not pay employees in accordance with applicable bargaining agreements, did not comply with state policies when it obtained certain goods and professional/technical services, and did not comply with state policies related to accounting for and labeling its personal property.

Table 1-1
Indian Affairs Council
Sources and Uses of Fund

	Fiscal Years Ending June 30		
	1996	1997	1998
Sources:			
Appropriations	$ 508,000	$ 463,001	$ 523,000
Appropriation for Battle Point Historic Site			71,823 **(1)**
Balance Forward from Prior Fiscal Year	901,442	1,099,451 **(2)**	1,120,652 **(2)**
Tax on Severed Mineral Interests	136,145	131,021	116,270
Federal Grants/Subgrants	56,120	74,458	41,891
Interagency Agreements	10,589	6,750	75,000
Loan Principal and Interest Payments	57,114 **(2)**	54,766	63,587
Transfers In	7,813	16,071	0
All Other Sources	550	22	51
Total Sources	$1,677,773	$1,845,540	$2,012,274
Uses:			
Payroll	$ 353,516	$ 360,213	$ 433,330
Rent	24,609	25,311	24,870
Purchased Goods and Services	72,504	143,861	160,715 **(1)**
Travel	43,259	49,248	70,680
Indian Business Loans	56,864	49,000	99,750
Claim Paid	0	0	30,700
All Other Uses	27,570	34,975	71,379
Balance Forward to Next Fiscal Year	1,099,451 **(2)**	1,120,652 **(2)**	1,120,850 **(2)**
Appropriation Cancellation	0	62,280	0
Total Uses	$1,677,773	$1,845,540	$2,012,274

Note **(1)** In fiscal year 1995, the Legislature appropriated $350,000 for design of the Battle Point Historic Site. In fiscal year 1998, the Indian Affairs Council used $71,823 of the appropriation.

Note **(2)** As explained in Chapter 2, Finding 1, fiscal year 1996 receipts were overstated on the state's accounting system by $47,244. In Table 1-1, above, we adjusted the fiscal year 1996 receipts figure and the balance forward to fiscal year 1997 amount. In fiscal years 1997 and 1998, we adjusted the balance forward in and the balance forward out to correct the subsequent impact of this error.

Source: Minnesota Accounti ng and Procurement System (MAPS) data.

Chapter 2. Indian Business Loan Program

Chapter Conclusions

The Indian Affairs Council did not administer the Indian business loan program in a reasonable and prudent manner, and did not comply with some statutory provisions and state policy. The council had serious weaknesses in its administration of the program. The council did not properly monitor Indian business loan receipts. The council's loan documentation did not support the eligibility of some borrowers. The council did not properly file security interests and a mortgage against the collateral for several Indian business loans. The council did not accurately maintain its loan ledger and did not report loan information to borrowers. The council's write-off of uncollectible Indian business loans was not in accordance with applicable legal provisions. The council contracted with an organization to perform some administrative duties for the loan program even though organization members, including the individual performing the duties, had outstanding Indian business loans. The council did not receive interest on its Indian business loan account balance. Finally, the council has not adequately utilized the funds available to the Indian business loan program.

The Minnesota Legislature established the Indian business loan program to provide eligible recipients with a portion of the financial resources needed to start or expand a business enterprise. The Legislature gave the Indian Affairs Council the program's administrative responsibilities. The loans are available to start or expand a business, or to provide technical or managerial support. Indians interested in applying for a loan through this program submit an application to the Indian Affairs council, which in turn sends it to the appropriate tribal council for approval or disapproval.

The Legislature provided funding for the program in two ways. First, the Legislature allocated the loan principal and interest payments to the program. Second, the Legislature dedicated 20 percent of the tax on severed mineral interests (mineral interest separate from the land interest) to the program. Owners of severed mineral interests pay the tax to the counties, who submit it to the Department of Revenue. The Department of Revenue deposits the appropriate amount in a Special Revenue Fund account in the state treasury.

Starting in fiscal year 1997, the Department of Finance assisted the council with some of the program's administrative duties. Staff in Finance's small agency assistance group deposited loan payments, posted receipts to the state's accounting system, and maintained a ledger of loan activity. The Department of Finance reported loan payment information to the council.

Table 2-1 summarizes the financial activity of the Indian business loan program for the three fiscal years ended June 30, 1998.

Table 2-1
Indian Business Loan Program
Summary of Financial Activity

	Fiscal Years Ending June 30		
	1996	**1997**	**1998**
Beginning Cash Balances	$883,388	$ 974,766	$1,085,593
Sources of Funds:			
Severed Mineral Interest Taxes	136,146	131,021	116,270
Loan Principal Payments	47,244	45,421	54,178
Interest Payments	9,870	9,366	9,409
Total Sources	$193,260	$ 185,808	$ 179,857
Uses of Funds:			
Loans	$ 56,864	$ 49,000	$ 99,750
Settlement **(1)**	0	0	30,700
Payroll	40,283	24,444	53,747
Other Administrative Costs	4,735	1,537	7,562
Total Uses	$101,882	$ 74,981	$ 191,759
Ending Cash Balances	$974,766	$1,085,593	$1,073,691
Outstanding Loan Balances (2)	$735,722	$739,301	$784,873

(1) The council paid a settlement to a bank because of a loan processing error.
(2) Calculated by the OLA based on transactions in the Minnesota Accounting and Procurement System (MAPS).

Source: Minnesota Accounting and Procurement system data.

Objectives

We designed our review of the Indian business loan program to determine whether the Indian Affairs Council administered the program in a reasonable and prudent manner. Our specific objectives were as follows:

- Did the Indian Affairs Council deposit, record, and properly dedicate loan principal and interest payments and its share of the Severed Mineral Interest Tax to the Indian business loan program?
- Did the council comply with the program's statutory requirements governing loan eligibility?
- Did the council properly file security interests and mortgages against loan collateral?
- Did the council identify, monitor, and resolve loans in delinquent status?
- Did the council write off uncollectible loans?
- Were the administrative costs charged to the program appropriate and reasonable?
- Did the council adequately utilize the funds available to the Indian business loan program to maximize the program's effectiveness?

To accomplish these objectives we performed various audit techniques. We interviewed individuals responsible for administering the program to gain an understanding of the program and procedures. We performed a review of new loans issued during the audit period. We reviewed administrative expenditures charged to the program. We also reviewed severed mineral tax receipts and loan payments. Finally, we reviewed the status of outstanding loans, collection efforts, and write-offs of uncollectible accounts.

Conclusions

The Indian Affairs Council did not administer the Indian business loan program in a reasonable and prudent manner, and did not comply with some statutory provisions and state policy. The administrative expenditures charged to the program account were appropriate and reasonable.

As explained in Findings 1 – 8, the council had serious weaknesses in its administration of the program. The council did not properly monitor Indian business loan receipts. The council's loan documentation did not support the eligibility of some borrowers. The council did not properly file security interests and a mortgage against the collateral for several loans. The council did not accurately maintain its loan ledger and did not report loan information to borrowers. The council's process for writing-off uncollectible Indian business loans was not in accordance with applicable legal provisions. The council contracted with an organization to perform some administrative duties for the loan program even though organization members, including the individual performing the duties, had outstanding Indian business loans. The council did not receive interest on its Indian business loan account balance. Finally, the council has not adequately utilized the funds available to the Indian business loan program.

1. The council did not properly monitor Indian business loan receipts.

The council failed to monitor Indian business loan receipts in three key areas: posting to the accounting system, verifying severed mineral interest tax receipts, and depositing receipts in a timely manner.

First, the council did not verify that Indian business loan receipts were accurately posted to the state's accounting system. The council did not detect a discrepancy between actual program receipts and receipts posted to the program account in the accounting system. In fiscal year 1996, receipts posted to the accounting system exceeded actual receipts by $47,244, overstating the funds available to the program. The Department of Finance made the error when they were adjusting the council's receipt transactions. The council should have detected and corrected the error when it compared the accounting system's posted receipts to its deposit records.

Also, the council did not verify whether the Department of Revenue accurately recorded the dedicated tax receipts in the program account. Revenue collected the taxes and recorded the portion allocated to the Indian business loan program in the council's account. Revenue also reported to the council the amount of tax receipts posted. The council did not compare Revenue's reported receipts to the actual receipts posted to its account. Revenue's reports included three deposits (totaling $4,385) that were not recorded on the state's accounting system. The state's accounting system included two deposits (totaling $3,480) not supported by Revenue's reports. The net of these discrepancies resulted in approximately $900 less on the state's accounting system than reported by Revenue.

Finally, the council did not promptly deposit loan payments in fiscal year 1996, and did not monitor the timeliness of deposits made by the Department of Finance in fiscal years 1997 and 1998. We found instances throughout the audit period when loan payment deposits were delayed for several days after receipt. Minnesota Statute 16A.275 requires state agencies to deposit receipts daily when they exceed $250.

Recommendations

- *The council should verify the accuracy of receipts credited to the Indian business loan program account by comparing the posted amount to actual receipts. The council should work with the Department of Finance to reduce the program's available funds by $47,244.*

- *The council should monitor recorded tax receipts to ensure the Department of Revenue accurately posts the receipts to the program account. If posting errors exist, the council should work with the Department of Revenue to make corrections as necessary.*

- *The council should monitor the timeliness of loan payment deposits to ensure compliance with statutory requirements.*

2. The council's loan documentation did not support the eligibility of some borrowers.

The council did not document borrower eligibility for some loans issued. For two of the eight loans issued during fiscal years 1996, 1997, and 1998, loan files did not contain tribal certifications documenting the eligibility of the borrower. The council uses the certifications to verify that loan applicants are enrolled members of a Minnesota tribe and are at least one-quarter Indian. Without the certifications, the council had no evidence that the borrowers were eligible to receive an Indian business loan.

In fiscal year 1998, the council was involved in a dispute related to borrower eligibility. The council approved a loan without first verifying the applicant's eligibility. A bank relied upon the council's approval, and provided the applicant with additional funding. The council subsequently canceled its loan when it discovered that the applicant was less than one quarter Indian, but it did not notify the bank. When the applicant's business failed, the bank could not recover its money, and sued the council. The council used $30,700 from the Indian business loan account to settle the lawsuit with the bank.

Recommendations

- *The council should obtain the missing tribal certifications for the two loans to verify borrower eligibility, and take corrective action if necessary.*

- *The council should obtain tribal certifications to verify borrower eligibility before processing Indian business loan applications.*

3. The council did not properly file security interests and a mortgage against the collateral for several Indian business loans.

The council did not file security interests in equipment, inventory and other assets and a mortgage on commercial property designated as collateral for six of the eight Indian business loans issued during fiscal years 1996, 1997 and 1998. Five of the eight loans designated security interests in equipment, inventory and other assets as collateral, but the council did not file the security interests for four of those loans. The other three loans designated both security interests in equipment, inventory and other assets and mortgages on commercial property as collateral. However, the council did not file the security interest for one of those loans and did not file either the security interest or the mortgage for another. Loan contracts specified that borrowers grant to the State of Minnesota, acting by and through the Indian Affairs Council, a mortgage on commercial property and/or a security interest in equipment, inventory and other assets designated as collateral in an amount equal to the face value of the loan. Minn. Stat. Section 336.9-401 states that a security interest in collateral must be properly filed in the county of the borrower's residence, or in the office of the secretary of state, to perfect the security interest. Mortgages must be properly filed in the county of the property being mortgaged to place a valid lien on the property. Without perfecting security interests or placing valid liens on property, the council cannot make claims against collateral to recover loans that default.

Recommendations

- *The council should file the missing security interests and mortgage for the six loans.*
- *The council should obtain the documents necessary to file security interests and mortgages before disbursing loan proceeds, and should file security interests and mortgages immediately upon disbursement.*

4. The council did not accurately maintain its loan ledger and did not report loan information to borrowers.

The council's Indian business loan ledger did not accurately represent outstanding loan balances. The council kept this ledger to have detailed information about the financial activity of each loan. Loan payments recorded in the program ledger did not agree with amounts on the state's accounting system. The council also had not recorded three loans issued in fiscal year 1998 and had not updated the loan ledger for any financial activity during the first half of fiscal year 1999. The council's loan officer position has been vacant since June 1998. Since the council did not fill the position, the duties went unperformed. Midway through fiscal year 1999, the council hired an outside organization to update the records. (However, refer to Finding 5 for concerns about this outside organization's participation in the loan program.)

The council did not send loan payment information (such as payment due dates and where to send payments) to the three people receiving loans in fiscal year 1998. As of February 1999, none of these borrowers had made any loan payments. Also, the council did not send account statements to any borrowers. Thus, borrowers were not able to review their accounts to ensure that the council received and accurately recorded all loan payments, and properly calculated the remaining amount outstanding.

Reliable loan information is essential for the council to monitor the timeliness of borrowers' payments, determine outstanding balances, and identify delinquent loans. Also, by sending statements to borrowers, the council would keep borrowers informed of their loan payment progress and potentially identify errors.

Recommendations

- *The council should review its loan ledger and determine the correct outstanding loan balances.*
- *The council should regularly reconcile the loan ledger to the state's accounting system and to the Department of Finance's loan ledger to ensure that new loans and loan payments are accurately posted.*
- *The council should periodically send statements to individuals with outstanding loans.*

5. The council's write-off of uncollectible Indian business loans was not in accordance with applicable legal provisions.

The council did not include sufficient information about loans it had written off when reporting to the Department of Finance. The council did not report specific information on individual loans written-off when it submitted quarterly accounts receivable reports to Finance. Minn. Stat. Section 16D.09 states that "the determination of the uncollectibility of a debt must be reported by the state agency along with the basis for that decision as part of its quarterly reports to the commissioner of finance." Without specific information on individual loans written-off, Finance cannot determine if the write-offs are reasonable and in the state's best interest.

In addition, after the council had negotiated with a borrower to close out a loan, it did not report the unpaid portion of the loan to Finance as a write-off. According to state policy, the deduction of the unpaid portion of the debt from financial records should be reported to Finance as a write-off.

The council also did not adequately document all its loan activities. The council could not locate any documentation regarding Indian business loans written off in fiscal year 1997. Minn. Stat. Section 15.17 requires state agencies to make and preserve all records necessary to retain a full and accurate knowledge of their official activities. The council had not established a record retention schedule. Minn. Stat. Section 138.17 requires state agencies to have records retention schedules detailing the length of retention for certain records.

Recommendations

- *The council should report loan write-offs to the Department of Finance in accordance with statutory provisions and state policy.*
- *The council should make and preserve records of all official activities and retain that documentation according to a record retention schedule, as required by statutory provisions.*

6. The council contracted with an organization to perform some administrative duties for the loan program even though organization members, including the individual performing the duties, had outstanding Indian business loans.

The executive director of the Minnesota Chippewa Tribe, whom the council hired to temporarily perform administrative duties for the Indian business loan program, and the employee assigned to perform the duties, had outstanding Indian business loans. Thus, they had access to their own loan accounts. The contracted duties included posting loan payments to the loan ledger and monitoring outstanding loan status. (The council's loan officer position had been vacant for about six months.) Without proper oversight, the contractors could post fictitious payments or not identify their own loans as being delinquent.

Recommendation

- *The council should closely monitor the work done by the Minnesota Chippewa Tribe, to ensure the integrity of the Indian business loan records.*

7. The council did not receive interest on its Indian business loan account balance.

The council did not receive interest on its balance in the Indian business loan account recorded on the state's accounting system. The statutes applicable to the loan program state that the council "shall record in the Indian business loan account the receipt and disbursement of the money and of the income, gain and loss from the investment and reinvestment of the money." The Department of Finance had not identified the Indian business loan account as one that could retain its investment earnings, and had credited the interest earned to the state's general fund.

Recommendations

- *The council should work with the Department of Finance to ensure that the Indian business loan account receives its appropriate share of investment earnings.*

8. The council has not adequately utilized the funds available to the Indian business loan program.

The funds available to the Indian business loan program have grown, far exceeding the volume of loans issued. The cash balance in the Indian business loan program has grown from $883,388 at the beginning of fiscal year 1996, to $1,073,693 at the end of fiscal year 1998. The available cash balance increased because the severed mineral interest tax and the loan payments exceeded the loans issued. During the three-year period, the program's receipts totaled nearly $560,000, while the eight loans issued totaled $205,614. As of March 1999, the council had not issued any new loans during fiscal year 1999.

The council had not determined why the loan funds were not being utilized. Possibly, the council did not adequately communicate the availability of funds, the application process was too complex, or the eligibility requirements were too rigid. The council should review the current account balance and anticipated future needs to determine whether adjustments to available funding are warranted. One alternative would be to cap available funding at an agreed upon level and periodically transfer any excess funds to the General Fund.

Recommendation

- *The Indian Affairs council should make a greater effort to reach potential borrowers, or should assess whether the program's funding structure needs revision.*

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Chapter 3. Administrative Expenditures

Chapter Conclusions

The council's administrative expenditures were generally reasonable and prudent; however, we noted several weaknesses. The council did not comply with employee bargaining agreements, resulting in payroll errors. Also, the council did not comply with state policies when it obtained certain professional/ technical services, or when it purchased certain goods. Finally, the council did not comply with state policies related to accounting for and labeling its personal property.

The Indian Affairs Council incurred payroll and other administrative expenditure to carry out its mission. We focused our review on the four largest expenditure areas, as shown in Table 3-1.

Table 3-1
Selected Administrative Expenditures
For the Three Fiscal Years Ending June 30, 1998

Administrative Expenditures:	1996	1997	1998	Total
Payroll	$353,516	$360,213	$433,330	$1,147,059
Purchased Goods and Services	72,504	143,861	**(1)** 160,715	377,080
Travel	43,259	49,248	70,680	163,187
Rent	24,609	25,311	24,870	74,790
Total	$493,888	$578,633	$689,595	$1,762,116

Note **(1)** Includes $71,823 paid from a 1995 appropriation for the Battle Point Cultural and Education Center project.

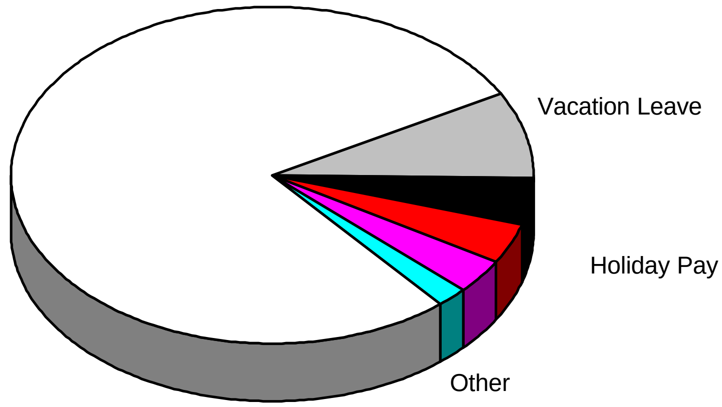
Source: Minnesota Accounting and Procurement System.

We examined these administrative expenditure categories to determine whether they were reasonable and prudent. The sections below define our specific objectives for each category. We found that the council's administrative expenditures were generally reasonable and prudent, except as explained in Findings 9 - 13.

Payroll

The council's staff consisted of eight full-time positions. Five of those positions were assigned to the council's Bemidji office, while the other three were assigned to the council's St. Paul office. The council used the state's personnel and payroll systems. The council's staff maintained its personnel records and authorized its payroll, but submitted timesheets to the Department of Finance's small agency assistance group for input into the state's payroll system. Figure 3-1 shows a breakdown of payroll expenditures by type of pay.

Figure 3-1
Payroll Expenditures
For the Three Fiscal Years Ending June 30, 1998



Source: The state's payroll/personnel system (SEMA4).

Objectives

Our specific objectives for the payroll expenditure category were as follows:

- Did the council pay employees for hours worked?
- Did the council pay employees in accordance with applicable bargaining agreement provisions?

We interviewed the council's staff to gain an understanding of payroll policies and procedures. We performed analytical procedures on payroll transactions, and reviewed personnel records and bargaining agreements. We also reviewed and recalculated certain transactions.

Conclusions

The council paid employees for hours worked. The council did not, however, pay employees in accordance with certain bargaining agreement provisions. As discussed in Finding 9, the council paid employees at incorrect pay rates, did not accurately calculate retroactive payments to several employees, and paid an inappropriate severance payment.

9. The council did not pay employees in accordance with certain bargaining agreement provisions.

The council paid employees at incorrect pay rates for most of the audit period. The bargaining agreements provided for salary increases based on length of service. The council's staff incorrectly believed that these increases would happen automatically through the state's payroll system. When the council identified its error, it corrected the pay rates for over two years of missed salary increases. The council calculated and paid about $31,340 in retroactive pay to its eight employees.

The council did not accurately calculate seven of the eight retroactive payments. The council overpaid six employees by nearly $4,300, with individual overpayments ranging from $171 to $2,233. The council underpaid one other employee by $187. The calculations were complicated due to the long time period included in the retroactive payment calculations and several pay rate changes within that time period.

The council paid $514 as severance pay to an employee who was not eligible. According to the employee's bargaining agreement, employees were only entitled to severance pay after at least twenty years of service or retiring after at least ten years of service. The employee did not meet these provisions and was not eligible for severance pay.

Recommendations

- *The council should monitor employees' length of service and pay rates to ensure compliance with applicable bargaining agreements.*
- *The council should collect the overpaid retroactive payments from the six employees, and should make an additional retroactive payment to the underpaid employee.*
- *The council should collect the severance overpayment from the former employee.*

Purchased Goods and Services

The Indian Affairs Council purchases supplies and equipment for its operations, and contracts for various professional/technical services. The council used professional/technical services to identify, protect, and rebury Indian remains, and for administrative and technical support services. The council also contracted with an architectural firm for the schematic design of the Battle Point Cultural and Education Center planned for construction in Cass Lake.

The Department of Administration has statutory authority to purchase goods and services for state agencies. The department controls state agency purchases in various ways. Through the department's Materials Management Division (MMD) a state agency can obtain local purchase authority for an employee. After MMD's local purchase authority training, this designated employee can, within specified limits, purchase certain types of goods and services for the agency. (A major exception is the authority to purchase professional/technical services.) During the audit period, the council had one employee with local purchase authority for purchases of up to $1,500.

A state agency can obtain professional/technical services in the following ways:

- Contract with the vendor through the Department of Administration's Materials Management Division (MMD).

- Contract directly with the vendor in accordance with an Annual Plan approved by the MMD.

- Establish through the MMD a master professional/technical services contract. An agency would want to establish a master service contract when it has identified the need for a particular service, but has no reasonable way to determine when and to what extent the need will arise. A master service contract specifies the maximum annual amount an agency can spend, and lists several vendors qualified to perform the service. When an agency needs the service, it can issue a work order to one of the vendors, which would incorporate the terms from the master professional/technical contract. Work can then start immediately.

Objectives

Our specific objectives for the purchased goods and services category were as follows:

- Did the council purchase goods and obtain services that were consistent with its duties?
- Did the council obtain goods and professional/technical services in accordance with state policy?
- Did the council encumber funds prior to incurring obligations?
- Did the council receive the goods and services paid for?
- Did the council accurately record payments for goods and services in the accounting records?
- Did the council properly account for and label its personal property in accordance with state policy?

We met with council staff to gain an understanding of procedures related to purchasing and paying for goods and services. We reviewed documentation for a sample of expenditures for purchased goods and services, including significant professional/technical services.

Conclusions

The council generally purchased goods and obtained services consistent with its duties. However, as explained in Findings 10-13, the council did not obtain professional/technical services or purchase goods in accordance with state policy, and did not always encumber funds prior to incurring obligations. The council did receive the goods and services paid for, and except as explained in Finding 12, accurately recorded expenditures for purchased goods and services. As explained in Finding 13, the council did not properly account for and label its personal property in accordance with state policy.

10. PRIOR AUDIT FINDING NOT RESOLVED: The council did not comply with state policies when it obtained certain professional/technical services.

The council did not have proper authority when it contracted for some professional/technical services. According to state policy, agencies can only obtain professional/technical services through the MMD or based on an Annual Plan or master professional/technical service contract approved by MMD. The council did not have an Annual Plan for fiscal years 1997, 1998, or 1999. (The council did have an approved Annual Plan for fiscal year 1996 that gave it authority to obtain certain services not to exceed $1,000 per vendor per year.) The council also did not have any master professional/technical service contracts.

The council entered into a number of unauthorized contracts for professional/technical services. During fiscal years 1997 and 1998 the council entered into seven $1,000 service contracts with a vendor, and paid that vendor over $17,000 for services, supplies, and equipment. (Purchasing supplies and equipment from this vendor is a separate issue discussed in Finding 11). The council also entered into one $1,500 and two $1,000 service agreements with another vendor during fiscal years 1997 and 1998, and paid that vendor a total of $3,675. Finally, in fiscal year 1998 the council paid two vendors over $1,000 each for services related to the identification and reburial of Indian remains: it paid one vendor $1,744 and the other $1,300.

We also question the reasonableness of some services the council obtained. For example, the council obtained computer-related technical support for both its Bemidji and St. Paul offices from a vendor located in Bemidji. For services performed in St. Paul, the council reimbursed the vendor nearly $600 for mileage between Bemidji and St. Paul. The council could perhaps have found a qualified vendor in the St. Paul area to perform the services at a lower cost. The fiscal year 1999 contract with the Minnesota Chippewa Tribe to perform services for the Indian business loan program (as discussed in Finding 6) is also questionable, since state agencies cannot generally enter into professional/technical contracts for services usually provided by a state employee. MMD may have also questioned whether $1,000 was enough for the tribe to perform the contracted duties. The council paid the tribe $992 for 48 hours of work. However, the tribe has agreed not to submit a bill to the council for an additional 218 hours of work it subsequently performed. Instead, the council and the tribe will treat the hours as donated services.

The council twice allowed a vendor to begin work under professional/technical services contracts before the effective dates of the contracts. The council properly entered into contracts with the vendor in fiscal years 1996, 1997 and 1998 for fiscal and technical assistance services, but in fiscal years 1996 and 1997 the vendor started performing the services before the date specified in the contracts. The council paid the vendor $650 in fiscal year 1996 and $720 in fiscal year 1997 for services performed before the effective date of the contract.

The council did not properly monitor the hours worked by the same vendor during fiscal year 1998. As a result, the council paid the vendor $220 more than the maximum compensation amount specified in the contract. The contract specified the vendor could work up to 100 hours at $20 per hour. However, the vendor worked and received payment for 111 hours during the year.

Recommendations

- *The council should work with the Department of Administration's Materials Management Division to establish procedures to ensure it obtains professional/technical services in accordance with state policy.*

- *The council should not allow vendors to begin work until after the effective dates of contracts, and after contracts have been signed by all parties.*

- *The council should establish monitoring procedures to ensure vendors do not perform services resulting in compensation in excess of contracted amounts.*

11. The council did not comply with state policy when it purchased some goods.

Some council employees who did not have local purchase authority certification purchased goods, and some of those purchases exceeded the council's local purchase authority limit. According to state policy, MMD delegates local purchase authority to individual employees within an agency, and only those authorized employees may purchase goods for that agency up to a specified dollar limit. In fiscal years 1996, 1997, and 1998 only one council employee had local purchase authority, with a dollar limit of $1,500 per purchase. Also, the council purchased computer supplies and equipment from a vendor under a service agreement. According to state policy, materials, supplies, and equipment may not generally be obtained through a service contract. The following paragraphs highlight the specific instances of noncompliance:

- Early in fiscal year 1998, a council employee without local purchase authority attempted to purchase over $16,000 of office furniture. MMD found out about the attempted purchase and canceled the order, but not before the council had already received furniture worth $1,125. MMD and the council agreed that the council would retain and pay for the furniture it received. As a result of the canceled order, MMD, the council and the vendor also agreed on a $500 payment from the council to the vendor for "restocking" charges. The council's response to MMD concerning the incident, dated September 26, 1997, stated "…future purchasing practices by agency personnel will follow state procedures: i.e. purchase orders will be generated and we are all cognizant of the local purchasing authority limit of the agency."

  Subsequently, we found three instances where council employees without local purchase authority purchased goods. The three purchases occurred between December 1997 and February 1998, and ranged from $209 to $1,704. In each instance, a council employee in the council's Bemidji office purchased the goods. The council employee with local purchase authority worked in the council's St. Paul office.

- The council purchased over $11,000 worth of computer supplies and equipment from a vendor under several service agreements. Purchases included computer-related parts and supplies, software, and three laptop computers. The council employee with local purchase authority did not make any of the purchases. The council purchased the last of the three laptops in May 1998, and the cost ($1,749) exceeded the council's local purchase authority. Although the council received the laptop, and the vendor believed it had been paid for, as of March 1999, the state's accounting system did not indicate that any payment had been made.

Also, at the end of fiscal year 1998, a council employee without local purchase authority ordered a computer server for the Bemidji office from the same vendor. When the council received an invoice for the server, a Department of Finance employee assisting with council payments refused to pay the invoice because the council did not purchase the server in compliance with state policy. Since the council needed the server and the vendor had no other immediate use for it, the vendor informally agreed to allow the council to use the server until it could make other arrangements to meet its computer needs. As of May 1999, the council continued to use the server. Although the agreement was informal, the vendor stated that he would likely charge the council for the depreciation on the server, which he estimated to be $300.

Recommendations

- *The council should establish procedures to ensure it obtains goods and services in accordance with state policy.*

- *The council should consult with MMD and the Department of Finance concerning the laptop and server to determine whether to keep or return the equipment, and how to compensate the vendor for the items.*

12. The council did not always encumber funds prior to incurring obligations.

We found several purchases where the council did not properly encumber funds prior to incurring obligations. Minn. Stat. Section 16A.15, Subd. 3, states that an obligation may not be incurred prior to funds being encumbered. By not properly encumbering funds, the council could incur obligations without having sufficient funds available to pay for them.

To ensure compliance, state policy requires employees incurring obligations in violation of the statute to write letters of explanation, and for agency management to review the explanations before authorizing the expenditures. The policy also requires agencies to establish written internal procedures to handle violations. However, the council did not write letters of explanation for violations and did not establish written procedures to handle violations.

State policy also states that “all purchases of goods and services must be made through the Minnesota Accounting and Procurement System (MAPS) procurement component, and must be encumbered using a specific commodity code and vendor number. Payments for goods and services cannot be made without entering information into the MAPS procurement component.” The council paid for some goods and services without entering information into the procurement component.

Recommendations

- *The council should encumber funds prior to incurring obligations in accordance with state statute.*

- *The council should write letters of explanation for violations of Minnesota Statute 16A.15, subd.3 and establish written procedures to handle violations in accordance with state policy.*

- *The council should not pay for goods or services without entering information into the MAPS procurement component in accordance with state policy.*

13. The council did not comply with state fixed asset policies.

The Indian Affairs Council did not comply with aspects of the state's fixed asset policy. It did not establish its own policy about how it will account for personal property and it did not properly identify assets purchased as state property.

State policy requires each agency to establish a policy on how it will account for personal property it acquires. The council had not established such a policy. The policy should address who is responsible for the personal property inventory, at what amount and what types of goods, the agency will establish fixed asset accountability, and how the agency will perform physical inventories of the fixed assets it identified. Without an established policy, the council cannot properly account for personal property it holds.

Some of the council's assets did not have either a state fixed asset sticker or a state property sticker. These stickers identify the property as state property and identify the asset number assigned to the item, to allow for its accountability. The council's personal property policy would have identified when each type of sticker should have been used, but state policy specifies that items exceeding $2,000 with a useful life of more than two years and any sensitive items the agency identifies should have a fixed asset sticker. Other assets should have a state property sticker.

Recommendations

- *The council should develop a personal property policy, in accordance with Department of Administration's guidelines.*
- *The council should properly identify state property with either a fixed asset sticker or a state property sticker.*

Travel

To perform their duties, staff members travel extensively throughout the state. The council has offices in both Bemidji and St. Paul. Staff members regularly meet with representatives from the eleven reservations throughout Minnesota, as well as with state legislators.

Objectives

Our specific objectives for travel expenditures were as follows:

- Did the council pay for travel expenditures that were reasonable and appropriate?
- Did the council pay travel reimbursements in accordance with employee bargaining agreements?
- Did the council accurately record travel expenditures in the accounting records?

Minnesota Indian Affairs Council

We interviewed council staff to gain an understanding of the process for authorizing and paying travel expenditures. We tested a sample of travel expenditures reimbursed to employees and a sample paid directly to vendors, such as hotels.

Conclusions

We found that the council paid reasonable and appropriate travel expenditures in accordance with employee bargaining agreements, and accurately recorded the expenditures in the accounting records.

Rent

The council rents its office space in both Bemidji and St. Paul. In fiscal year 1998, the council paid rent of $825 per month for its Bemidji office and $1,229 per month for its St. Paul office.

Objectives

Our specific objectives for rent expenditures were as follows:

- Did the council pay rent based on valid lease agreements?
- Did the council properly record rent expenditures in the accounting records?

We reviewed lease agreements and compared to the rent payments.

Conclusions

We found that the council accurately paid rent based on valid lease agreements and properly recorded rent expenditures in the accounting records.

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Status of Prior Audit Issues
As of February 19, 1999

October 20, 1995, Legislative Audit Report 95-48 covered the four fiscal years ending June 30, 1995. The audit scope included payroll expenditures, professional/technical service expenditures, and the Indian business loan program. The report had three findings: one about the lack of contracts for professional/technical services and two identifying weaknesses in the council's administration of the Indian business loan program.

The council did not resolve the prior finding related to professional/technical services. See current Finding 10. Of the two prior findings related to the Indian Business Loan Program, the council did not resolve one and partially resolved the other. As discussed in Finding 1, the council did not promptly deposit Indian business loan receipts. The council did write-off some uncollectible Indian business loans, but as discussed in Finding 5, it did not write them off in accordance with applicable legal provisions.

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 Metropolitan agencies or the State Agricultural Society, the state constitutional officers, or the judicial branch.

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June 25, 1999

Cecile Ferkul
Audit Manager
1st Floor South
Centennial Building
658 Cedar Street
St. Paul, MN 55155

Dear Ms. Ferkul:

This letter is in response to the draft audit that you and members of the Legislative Audit Committee presented to the Minnesota Indian Affairs Council on June 22, 1999 at 13:30 in our St. Paul Office. The audit was for the period July 1, 1995 through June 30, 1998.

Chapter 2. Indian Business Loan Program

The following is the response of the Minnesota Indian Affairs Council to the Legislative Audit.

1. **The Council did not properly monitor Indian business loan receipts.**

   Recommendations

   a. The Minnesota Indian Affairs Council has hired Laura Theroux as a business loan specialist to handle accounts payable in connection with the business loan program and Bobbie Donat as an office service specialist. These individuals will be, in large part, responsible for the monitoring of the receipts for the Indian business loan program.

   b. Within 90 days Laura, Joe and Bobbie will establish procedures to verify the accuracy of receipts credited to the Indian business loan program by comparing the posted amount to the actual receipts.

   c. Within 30 days Laura will work with the Department of Finance to reduce the program's available funds by $47,244.00.

d. Within 90 days Laura, Joe and Bobbie will monitor recorded tax receipts to ensure that the Department of Revenue accurately posts the receipts to the program account. The Council will work with the Department of Revenue to correct any posting errors that do occur.

e. Within 30 days Bobbie, Laura, Joe and Jim will set up accounts to facilitate electronic transfer of loan payment deposits to ensure compliance with statutory requirements.

2. The Council's loan documentation did not support the eligibility of some borrows.

Recommendations

a. Laura will ensure that eligibility requirements for loans are being met. She will ensure that a person is a quarter American Indian, and enrolled in one of the eleven Minnesota tribes.

b. Laura will also place this information in the files for the borrowers.

c. Laura will obtain tribal certifications to verify borrower eligibility before processing Indian business loan applications. This will be done within 60 days.

3. The Council did not properly file security interests and a mortgage against the collateral for several Indian business loans.

Recommendations

a. Within 90 days Laura will file the security interests or the mortgage interests for the loans. These will be filed for the six loans that are referenced in the Legislative Audit.

b. In addition, the Council will obtain documents necessary to file security interests and mortgages before disbursing loan proceeds in the future.

c. The documents will be filed immediately upon disbursement of the loan.

4. The Council did not accurately maintain its loan ledger and did not report loan information to borrowers.

Recommendations

a. Laura will review the loan ledger of the Council and determine the correct outstanding loan balances. This will be done within 30 days.

b. Laura will regularly reconcile the loan ledger to the state's accounting system and to the Department of Finance's loan ledger to ensure that new loans and loan payments are accurately posted. She will do this quarterly.

c. Also quarterly, Laura will send statements to individuals with outstanding loans.

5. **The Council's write-off of uncollectible Indian business loans was not in accordance with applicable legal provisions.**

Recommendations

a. Laura will report loan write-offs according to MAPS procedure by October.

b. The loan write-offs will be reported to the Department of Finance in accordance with statutory provisions and state policy.

c. Bobbie and Laura will develop procedures for record retention as required by statutory provisions. They will do so within 60 days.

6. **The Council contracted with an organization to perform some administrative duties for the loan program even though organization members, including the individual performing the duties, had outstanding Indian business loans.**

Recommendations

a. The Indian Affairs Council has hired Laura so the Minnesota Chippewa Tribe ("MCT") is not involved with the business loan program anymore.

b. Bobbie and Laura have taken over this program beginning immediately.

7. **The Council did not receive interest on its Indian business loan account balance.**

Recommendations

a. This recommendation is addressed by the procedures that will be developed under Item No. 1, which has Laura and Bobbie and Joe developing procedures for monitoring the business loans, verifying the mineral interests owed, and facilitating the electronic transfer of funds into the accounts.

b. The Council also will be looking into the retroactivity of interest it may be or is possibly owed on the revolving and mineral accounts.

8. **The Council has not adequately utilized the funds available to the Indian business loan program.**

Recommendations

a. The Minnesota Indian Affairs Council will be doing a brochure to advertise the business loan program. It will aggressively promote the program and identify markets into which the program can be expanded.

b. The Minnesota Indian Affairs Council will explore opportunities for partnerships with education and development firms.

c. Laura will be responsible for the marketing of the business loan program over the next six months to one year.

Chapter 3. Administrative Expenditures

9. The Council did not pay employees in accordance with certain bargaining agreement provisions

Recommendations

a. Within 90 days Bobbie will research and process collection of over payments made to employees through retroactive payments. Bobbie will also oversee personnel transactions so salary increases, etc. are processed in a timely manner.

10. PRIOR AUDIT FINDING NOT RESOLVED: The Council did not comply with state policies when it obtained certain professional/technical services.

Recommendations

a. Bobbie, Laura, Joe and Jim will receive training by the Department of Administration's Materials and Management Division ("MMD") to develop procedures and develop monitoring procedures to ensure it obtains professional/technical services in accordance with state policy.

b. The Council will develop monitoring procedures using the training provided by MMD of Administration to monitor contracts so that it does not allow vendors to begin work until after the effective dates of contracts and after contracts have been signed by all parties.

c. It is hoped that training can be completed within 6 months.

11. The Council did not comply with state policy when it purchased some goods.

Recommendations

a. Within 30 days Bobbie will undergo training to be certified with MMD for procurement.

b. Janet will be certified as soon as MMD or Administration runs another class.

c. Bobbie and Janet are consulting with the Department of Finance to determine whether or not the vendor of the laptop and server has been paid, thus, resolving the matter. This should be completed within 60 days.

12. The Council did not always encumber funds prior to incurring obligations.

Recommendations

a. The Council will encumber funds prior to incurring obligations in accordance with state statute.

b. The Council will follow the procedures outlined in MAPS.

c. The Council will establish written procedures to handle violations in accordance with state policy. The procedures will follow MAPS.

d. Procedures will be followed, so procurement will be entered into MAPS in accordance with state policy automatically.

13. The Council did not comply with state fixed asset policies.

Recommendations

a. Bobbie and Joe will develop a fixed asset policy in accordance with the Department of Administration guidelines.

b. The Council will identify state property with either a fixed asset sticker or a state property sticker.

c. The above will be done within 6 months.

If you have any questions regarding our response to the audit, please call me at 218-755-3825.

Thank you for this opportunity.

Sincerely,

Joseph B. Day
Executive Director
Minnesota Indian Affairs Council

Attachment

cc: Dallas Ross, Chairman of the Board
Jerilyn K. Aune, Assistant Attorney General