



**OFFICE OF THE LEGISLATIVE AUDITOR**  
STATE OF MINNESOTA

**FINANCIAL AUDIT DIVISION REPORT**

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# **Department of Management and Budget**

## **Federal Compliance Audit**

### **Year Ended June 30, 2009**

**March 25, 2010**

**Report 10-12**

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FINANCIAL AUDIT DIVISION

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## OFFICE OF THE LEGISLATIVE AUDITOR

State of Minnesota • James Nobles, Legislative Auditor

March 25, 2010

Senator Ann H. Rest, Chair  
Legislative Audit Commission

Members of the Legislative Audit Commission

Mr. Tom Hanson, Commissioner  
Department of Management and Budget

This report presents the results of our audit of the Department of Management and Budget's responsibilities for the state's federal financial assistance programs, including general compliance requirements related to federal assistance, and the preparation of the *Minnesota Financial and Compliance Report on Federally Assisted Programs*, including the state's Schedule of Expenditures of Federal Awards for fiscal year 2009. We conducted this audit as part of our audit of the state's compliance with federal program requirements. We emphasize that this has not been a comprehensive audit of the Department of Management and Budget.

We discussed the results of the audit with department staff at an exit conference on March 12, 2010. This audit was coordinated by Michael Hassing, CPA, CISA (Audit Manager).

This report is intended for the information and use of the Legislative Audit Commission and the management of the Department of Management and Budget. This restriction is not intended to limit the distribution of this report, which was released as a public document on March 25, 2010.

We received the full cooperation from the department's staff while performing this audit.

*/s/ James R. Nobles*

James R. Nobles  
Legislative Auditor

*/s/ Cecile M. Ferkul*

Cecile M. Ferkul, CPA, CISA  
Deputy Legislative Auditor

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# Report Summary

## Conclusion

The Department of Management and Budget generally complied with and had controls to ensure compliance with certain provisions of laws, regulations, contracts, and grants applicable to the state's administration of federal programs and the preparation of the *Financial and Compliance Report on Federally Assisted Programs* for fiscal year 2009. However, the state had deficiencies in its internal controls over the preparation of the Schedule of Expenditures of Federal Awards, in calculating and reporting general support service costs, and in protecting not public data within the state's accounting system, as noted below.

## Findings

- Prior Finding Partially Resolved: The state's procedures for preparing the Schedule of Expenditures of Federal Awards resulted in some significant misclassifications and other errors to the draft schedules. ([Finding 1, page 5](#))
- The Department of Management and Budget did not always use correct projected costs when it calculated the statewide indirect cost charges and misreported certain cost information to the federal government. ([Finding 2, page 7](#))
- The Department of Management and Budget did not adequately protect not public data on individuals maintained within the state's information data warehouse. ([Finding 3, page 8](#))

## Audit Objective and Scope

The objective of our audit was to determine whether the Department of Management and Budget complied with federal program requirements in its oversight and administration of the state's federal programs, including the general compliance requirements related to federal assistance and preparation of the Schedule of Expenditures of Federal Awards for fiscal year 2009. This audit is part of our broader federal Single Audit 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 federal programs.

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# Department of Management and Budget

## Federal Program Overview

As the manager of the state's financial affairs, the Department of Management and Budget has high-level responsibility for the state's compliance with federal program requirements and has specific responsibility for some cross-cutting federal compliance requirements, such as the determination of the state's indirect cost allocations to federal programs and cash management of federal funds. The department provides oversight to the other executive branch agencies related to statewide internal controls over the state's system for accounting, personnel, payroll, and procurement and establishes the appropriate policies for managing the state's financial resources, including federal program awards.

Each year, the department prepares the state's *Financial and Compliance Report on Federally Assisted Programs*, required as part of the state's Single Audit.<sup>1</sup> As a part of that report, the department prepares, with the assistance from other state agencies, the state's Schedule of Expenditures of Federal Awards for federal programs that we considered major federal programs for the State of Minnesota, subject to audit under the federal Single Audit Act.<sup>2</sup>

## Objective, Scope, and Methodology

The objective of our audit was to determine whether the Department of Management and Budget complied with federal program requirements in its oversight and administration of the state's federal programs, including the general compliance requirements related to federal assistance and preparation of the Schedule of Expenditures of Federal Awards for fiscal year 2009. This audit is part of our broader federal Single Audit 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 federal programs.

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<sup>1</sup> The State of Minnesota's Single Audit is an entity audit of the state that includes both the financial statements and the expenditures of federal awards by all state agencies. We issued an unqualified audit opinion, dated December 11, 2009, on the State of Minnesota's basic financial statements for the year ended June 30, 2009. In accordance with *Government Auditing Standards*, we also issued our report on our consideration of the State of Minnesota's internal control over financial reporting and our tests of compliance with certain provisions of laws, regulations, contracts, and grants. (Office of the Legislative Auditor's Financial Audit Division [Report 10-01, Report on Internal Control Over Financial Reporting](#), issued February 11, 2010.) This report included control deficiencies related to the Department of Management and Budget and other state agencies.

<sup>2</sup> We defined a major federal program for the State of Minnesota in accordance with a formula prescribed by the federal Office of Management and Budget as a program or cluster of programs whose expenditures for fiscal year 2009 exceeded \$30.1 million.

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We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in the *Government Auditing Standards*, issued by the Comptroller General of the United States of America and with the U.S. Office of Management and Budget's *Circular A-133 Compliance Supplement*.

## **Conclusion**

The Department of Management and Budget generally complied with and had controls to ensure compliance with certain provisions of laws, regulations, contracts, and grants applicable to the state's administration of federal programs and the preparation of the *Financial and Compliance Report on Federally Assisted Programs* for fiscal year 2009. However, the state had deficiencies in its internal controls over the preparation of the Schedule of Expenditures of Federal Awards, in calculating and reporting general support service costs, and in protecting not public data within the state's information data warehouse, as noted in the following *Findings and Recommendations* section.

We will report these control deficiencies to the federal government in the *Minnesota Financial and Compliance Report on Federally Assisted Programs*, prepared by the Department of Management and Budget. This report provides the federal government with information about the state's use of federal funds and its compliance with federal program requirements. The report includes the results of our audit work, conclusions on the state's internal controls over and compliance with federal program requirements, including the preparation of the state's Schedule of Expenditures for Federal Awards, and our findings about control and compliance deficiencies with major federal programs administered by the State of Minnesota.

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## Findings and Recommendations

### Finding 1

**Prior Finding Partially Resolved:**<sup>3</sup> The state's procedures for preparing the Schedule of Expenditures of Federal Awards resulted in some significant misclassifications and other errors to the draft schedules.

Although the Department of Management and Budget improved its review of agency information used to prepare the state's Schedule of Expenditures of Federal Awards, the department continued to have errors in the fiscal year 2009 schedule that required audit adjustments. In addition, there were significant misclassifications of expenditures between American Recovery and Reinvestment Act funds and other related federal funds. The department and the applicable agencies could have detected the misstatements by reviewing adjusted amounts and by comparing variances in amounts between fiscal years and following up on significant differences.

The state's process to prepare the schedule requires extensive adjustments to the data provided by the state's accounting system. The Department of Management and Budget relies on other departments to determine federal expenditures, additional accruals or other adjustments when those amounts are not readily available from the state's accounting system, or when it accounts for programs outside of the state's Federal Fund.

The Department of Management and Budget and other agencies had the following misclassifications and errors related to the 2009 Schedule of Expenditures of Federal Awards:

- The departments of Management and Budget and Employment and Economic Development did not accurately report the funding sources for the Unemployment Insurance Program on the 2009 Schedule of Expenditures of Federal Awards.<sup>4</sup> The schedule overstated the program's regular federal expenditures by about \$143.5 million and understated the related federal American Recovery and Reinvestment Act expenditures by the same amount.
- The departments of Management and Budget and Human Services did not accurately report the funding sources for the Medical Assistance and Child Support Enforcement programs. For the Medical Assistance Program, the departments overstated the federal American Recovery and Reinvestment Act

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<sup>3</sup> Office of the Legislative Auditor's Financial Audit Division [Report 09-14](#), *Department of Finance Federal Compliance Audit*, issued March 26, 2009.

<sup>4</sup> CFDA 17.225 and CFDA 17.225A, with total expenditures of \$1.9 billion. The Catalog of Federal Domestic Assistance (CFDA) is a unique number assigned by the federal government to identify its programs.

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expenditures by \$502.7 million and understated the other related federal expenditures by the same amount on the 2009 Schedule of Expenditures of Federal Awards.<sup>5</sup> In addition, the Department of Management and Budget overstated the Child Support Enforcement Program's regular federal expenditures by \$4.1 million and understated the related federal American Recovery and Reinvestment Act expenditures by the same amount.<sup>6</sup>

- The Department of Health did not accurately report financial activity on its fiscal year 2009 Schedule of Expenditures of Federal Awards for the Special Nutrition Program for Women, Infants and Children.<sup>7</sup> The department did not exclude \$2.5 million of infant formula rebates that the department had included as a receivable on its June 30, 2008, federal schedules. The departments of Health and Management and Budget's controls over the preparation of this schedule should have included a step to ensure that it eliminated rebate amounts reported in the prior fiscal year.
- The departments of Management and Budget and Natural Resources did not accurately report federal expenditures; they erroneously included \$7.4 million in state matching expenditures and omitted \$3 million of direct federal administrative expenditures in the Schedule of Expenditures of Federal Awards for the Fish and Wildlife Cluster.<sup>8</sup> Although both departments exchanged information and several communications about the amounts reported in the schedule, misunderstandings resulted in the errors being reported and going undetected.

Finally, the Department of Management and Budget did not provide draft expenditure schedules to us for audit until January 8, 2010, which was three weeks after our agreed upon due date. The Single Audit Act requires that the state's major programs be determined based on the final audited schedules. Changes in the determination of major federal programs may result in the need for additional audit work before the state can issue its *Financial and Compliance Report on Federally Assisted Programs*, possibly risking its ability to issue the report by March 31, as required by the federal government.

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<sup>5</sup> CFDA 93.778 and 93.778A, with total expenditures of \$4.4 billion.

<sup>6</sup> CFDA 93.563A.

<sup>7</sup> CFDA 10.557, with total expenditures of \$95 million.

<sup>8</sup> Fish and Wildlife Cluster includes the Sport Fish Restoration Program (CFDA 15.605) and the Wildlife Restoration Program (CFDA 15.611).

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### *Recommendations*

- *The Department of Management and Budget and applicable state agencies should:*
  - *Ensure that they properly reflect expenditures and accruals in the draft federal expenditure schedules.*
  - *Enhance its analytical procedures to include non-Federal Fund activity.*
- *The Department of Management and Budget should more promptly prepare the Schedule of Expenditures of Federal Awards to allow an earlier determination of major programs.*

## **The Department of Management and Budget did not always use correct projected costs when it calculated the statewide indirect cost charges and misreported certain cost information to the federal government.**

## **Finding 2**

The Department of Management and Budget used the wrong fiscal year's projected general support service costs when it calculated the 2009 statewide indirect cost charges. *Minnesota Statutes*<sup>9</sup> require the department to allocate all statewide general support service costs to the entities that use the services.<sup>10</sup> The department determines the indirect cost rates based on projected costs for the upcoming fiscal year's general support services and adjustments to the prior year's projected costs to align with the actual costs incurred. Generally, the department used the appropriation amounts passed into law as the projected costs for fiscal year 2009. However, for one of seven departments we tested, the department mistakenly used the fiscal year 2008 projected costs instead of the 2009 projected costs. This error overstated the projected budget costs for the department by \$407,000. For one of the other departments we tested, the Department of Management and Budget understated the costs for the Office of Enterprise Technology by \$1,803,000 due to an undetermined error. We estimate that these errors resulted in a net understatement of the federal share of indirect costs totaling approximately \$315,000. These errors will be offset in fiscal year 2011 when the department adjusts the projected fiscal year 2009 costs to the actual costs.

The department used the correct fiscal year 2007 amounts in its calculation of the indirect costs but reported incorrect information to the federal government in the supplementary schedules for 5 out of 32 general support services functions we tested. The department is required to submit the cost allocation plan to the United

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<sup>9</sup>*Minnesota Statutes* 2009, 16A.127.

<sup>10</sup>These services include centralized services provided by the departments of Administration, Management and Budget, and the offices of Enterprise Technology, Legislative Auditor, and others.

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States Department of Health and Human Services each year the state intends to claim indirect costs under federal awards. This plan includes supplementary cost allocation schedules for the prior year's actual cost. The department overstated the cost for the state's accounting system operations by \$4 million and understated the costs for the other four functions by \$36,652 in these supplementary schedules.

An independent person at the department reviewed both the indirect cost calculation and the statewide cost allocation plan. However, the reviews were not detailed enough to identify the above errors.

#### *Recommendation*

- *The department should perform a detailed review to ensure it accurately calculates the indirect cost charges and reports accurate information in the statewide cost allocation plan.*

## **Finding 3**

**The Department of Management and Budget did not adequately protect not public data on individuals maintained within the state's information data warehouse.**

The department did not sufficiently protect not public data on individuals that reside within the state's information warehouse. The department is responsible for the management and security of the state's accounting system and information data warehouse. State policy prohibits agencies from entering not public data into unprotected fields in the state's accounting system.<sup>11</sup> Some state agencies, however, have recorded the names or social security numbers of public assistance recipients in unprotected fields in the state's accounting system, inadvertently making the data available to state employees and contractors with access to detailed information in certain tables in the state's warehouse.

Not public data includes any government data which is classified by statute, federal law, or temporary classification as confidential, private, nonpublic, or protected nonpublic. State statutes define data on individuals that is collected, maintained, used, or disseminated by a welfare or public assistance program as private data on individuals.<sup>12</sup> The statutes prohibit state departments with public assistance systems from disclosing the data except under very restricted circumstances. In addition, state policy categorizes accounting system data as public and specifically instructs state agencies that names and certain health-related information on individuals should not be included.<sup>13</sup>

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<sup>11</sup> Department of Management and Budget Policy 0803-01.

<sup>12</sup> *Minnesota Statutes* 2009, 13.791.

<sup>13</sup> Department of Management and Budget Policy 0803-01.

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In fiscal year 2009, the Department of Employment and Economic Development discontinued the practice of entering not public data into the state's accounting system; it had not, however, removed prior years' client information from the state's information warehouse. The Department of Human Services continued to record not public information on public assistance recipients in unprotected fields within the state's accounting system, allowing this data to be included in the state's information warehouse and its own data warehouse.

*Recommendation*

- *The Department of Management and Budget should work with state agencies to identify and remove or protect not public data that is stored in the state's information warehouse.*





March 16, 2010

James R. Nobles, Legislative Auditor  
Office of the Legislative Auditor  
140 Centennial Office Building  
658 Cedar Street  
St. Paul, MN 55155-4708

Dear Mr. Nobles:

Thank you for the opportunity to discuss your audit findings with the individuals responsible for the single audit. We are committed to providing accurate financial information on federally assisted programs to the federal government. We will continue to work toward improvements in our processes and value suggestions which will make our existing processes even stronger.

### **Finding**

Finding 1. Prior Finding Partially Resolved: The state's procedures for preparing the Schedule of Expenditures of Federal Awards resulted in some significant misclassifications and other errors to the draft schedules.

### **Response**

We agree with the recommendation. Thank you for recognizing the improvement in our process. We continue to place a high priority on ensuring the accuracy of the Schedule of Expenditures of Federal Awards totaling over \$10 billion for Fiscal Year 2009 and on enhancing the controls and processes related to its preparation. Our process was strengthened this year by providing agencies with drafts of the adjusted schedules for final review prior to submission to the auditors. In addition, we continued to reconcile all data included in the state's Federal Fund to appropriate federal programs. This reconciliation ensured that all accruals and adjustments made to the Federal Fund were also made to the appropriate federal programs. We also continued to compare prior year and current year balances by federal program and worked with agencies to obtain explanations for significant variances to ensure accuracy.

Fiscal year 2009 was the first year the state reported expenditures of American Recovery and Reinvestment Act (ARRA). Agencies were provided with instructions to separately report ARRA expenditures. We compared the ARRA expenditures reported to us with our expectations of programs receiving ARRA funds and then contacted and worked with

Mr. James R. Nobles  
March 16, 2010  
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applicable agencies on any discrepancies. Although total expenditures reported were accurate, misclassifications of expenditures between ARRA and non-ARRA funding remained after these efforts. We will continue to work with agencies to ensure accurate identification of ARRA and non-ARRA expenditures and to stress the importance of separating these amounts.

We will also continue working with agencies to ensure the accuracy and timeliness of the Schedule of Expenditures of Federal Awards. We will continue to emphasize to agencies the importance of thorough reviews and comparisons of current and prior year data.

Person Responsible: Barb Ruckheim, Financial Reporting Director

Implementation Date: March 31, 2011

### **Finding**

Finding 2. The Department of Management and Budget did not always use correct projected costs when it calculated the statewide indirect cost charges and misreported certain cost information to the federal government.

### **Response**

We agree with the recommendation. The state's indirect cost plan is a very lengthy and complex document. The allocation of indirect costs is extremely complex with multiple levels of allocations using data from numerous sources. The state's indirect cost plan calculates the indirect costs based on projected costs for the upcoming fiscal year and the settle-up on the difference between the projected costs and actual costs for the previous fiscal year. As you noted, accurate actual fiscal year 2007 costs were used for calculation of indirect costs, but the estimated projected costs did not include the most recent information available at the time the plan was completed. In the future, we will ensure that the documentation is maintained for the determination of the projected costs based on the information available at the time the plan is prepared in a couple instances. In addition, we will ensure the information included in supplementary schedules supporting the detail of costs included in the indirect cost plan are updated and reviewed.

Person Responsible: Barb Ruckheim, Financial Reporting Director

Implementation Date: April 30, 2010

### **Finding**

Finding 3. The Department of Management and Budget did not adequately protect not public data on individuals maintained within the state's information data warehouse.

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## **Response**

We agree with the recommendation. As noted in the audit report, MMB policy is to restrict private data in MAPS and agencies have been instructed not to enter private data into MAPS public data fields. We do not provide access to the public for these fields through any of our public access methods. Access to this data is limited to individuals who have been granted security roles with authorization to view this type of MAPS data in the warehouse. We have taken steps to develop further security controls. We are testing a new security process to limit access to those authorized individuals of the agency owning the data and to those with clearance to view all state agency data (such as MMB) who have security roles authorizing access to this data. Development of this new increased security level has been a very complex effort, requiring over 1,000 hours of MMB time. The effort is nearly complete. In addition, we will send a notice to all MAPS users reminding them of the policy to restrict private data from MAPS public data fields.

Persons responsible: Ellen Schwandt, Administrative Systems Supervisor and technical director of the Information Warehouse. Delores Staffanson, Agency Support Director

Implementation date: April 2010

Sincerely,



Tom J. Hanson  
Commissioner