

O L A

OFFICE OF THE LEGISLATIVE AUDITOR
STATE OF MINNESOTA

Financial Audit Division Report

Department of Corrections

Oak Park Heights, Red Wing, and Stillwater Facilities

July 1, 2004, through June 30, 2006



September 21, 2007

07-26

Financial Audit Division

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- Promote Accountability,
- Strengthen Legislative Oversight, and
- Support Good Financial Management.

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Financial Audit Division Report

Department of Corrections

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Stillwater Facilities**

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Ms. Lynn Dingle, Warden
Minnesota Correctional Facility – Stillwater

We audited Department of Corrections' facilities at Oak Park Heights, Red Wing, and Stillwater (the facilities) for the period July 1, 2004, through December 31, 2006. Our audit scope included computer systems security controls, payroll expenditures, professional/technical contract expenditures, offender accounts, and canteen operations. Our objectives focused on a review of the facilities' internal controls over these financial activities and their compliance with applicable legal provisions. Our review also included selected controls at the Department of Corrections' central office and MINNCOR division. We limited the selected control review to the financial activity identified in our scope for the Oak Park Heights, Red Wing, and Stillwater facilities.

The enclosed Report Summary highlights our overall audit conclusions. The specific audit objectives and conclusions for each area are contained in the individual chapters of this report.

We would like to thank the staff from the Department of Corrections and its facilities for their cooperation during this audit.

/s/ James R. Nobles

James R. Nobles
Legislative Auditor

/s/ Cecile M. Ferkul

Cecile M. Ferkul, CPA, CISA
Deputy Legislative Auditor

End of Fieldwork: April 11, 2007

Report Signed On: September 18, 2007

**Department of Corrections Facilities:
Oak Park Heights, Red Wing, and Stillwater**

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Audit Participation

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

Cecile Ferkul, CPA, CISA	Deputy Legislative Auditor
David Polisen, CPA, CISA, CFE	Audit Manager
Ken Vandermeer, CPA, CFE	Audit Coordinator
Thom Derus	Auditor
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Exit Conference

We discussed the results of the audit with the representatives of the Department of Corrections and the facilities at an exit conference on September 7, 2007:

Dennis Benson	Deputy Commissioner
Lisa Cornelius	Assistant Commissioner
Chris Dodge	Chief Financial Officer
Lon Erickson	Chief Information Officer
Paul Anderson	Budget Manager
Lori Caspers	Financial Services Director
Shelby Richardson	Contracts Manager
Chris Pizinger	MINNCOR Chief Executive Officer
Rich Schoenthaler	MINNCOR Chief Financial Officer

Department of Corrections Facilities: Oak Park Heights, Red Wing, and Stillwater

Report Summary

Overall Conclusion:

Except for computer systems security, the Minnesota Department of Corrections' correctional facilities at Oak Park Heights, Red Wing, and Stillwater generally had internal controls that ensured assets were safeguarded and transactions were properly recorded in the state's accounting records. Also, the facilities generally complied with material finance-related legal requirements.

The audit report contains eight findings relating to internal control and legal compliance.

Key Findings:

- The department's overall computer security strategy for some systems lacked important components, such as documentation and monitoring for basic security procedures and standards for its three major computer systems. ([Findings 1 - 3, pages 6 - 11](#))
- The department inconsistently charged expenses to the offender benefit account. ([Finding 6, page 17](#))
- The department inappropriately charged sales commissions and other administrative expenses to the canteen operations. ([Finding 7, page 21](#))
- The department did not prepare canteen profit and loss statements by facility and did not transfer canteen profits to each facility's Social Welfare Fund. ([Finding 8, page 21](#))

Audit Scope:

Oak Park Heights, Red Wing, and Stillwater facilities

Period Audited:

July 1, 2004, through June 30, 2006

Activities Audited:

- Computer Systems Security Controls
 - Payroll Expenditures
 - Professional/Technical Services
 - Offender Accounts
 - Canteen Operations
-

Agency Background:

The Department of Corrections is a service and regulatory agency focused on holding offenders accountable and offering opportunities for change while restoring justice for victims and contributing to a safer Minnesota. The department operates ten correctional facilities for adults and juveniles. It has consolidated its facilities' financial operations by creating regional business offices. Oak Park Heights, Red Wing, and Stillwater facilities have a combined regional business office located at the Stillwater facility.

**Department of Corrections Facilities:
Oak Park Heights, Red Wing, and Stillwater**

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Department of Corrections Facilities: Oak Park Heights, Red Wing, and Stillwater

Chapter 1. Introduction

The Minnesota Department of Corrections is a service and regulatory agency focused on holding offenders accountable and offering opportunities for change while restoring justice for victims and contributing to a safer Minnesota. It has a broad range of activities and responsibilities, including the operation of ten correctional facilities for adults and juveniles. The department organized its operations into three main divisions: Facility Services, Operations Support, and Community Services. The department consolidated facility business offices into four regional offices serving ten facilities. The department consolidated the Oak Park Heights and Stillwater business offices in 2000 and added the Red Wing facility in 2003 to form one regional office located at the Stillwater facility.

Oak Park Heights is the only maximum security facility in the system. Except for one adult cottage, Red Wing is a juvenile facility. The Stillwater facility is a closed custody facility.

Offenders in state facilities have access to a variety of work, education, and other program activities. The correctional industries program, MINNCOR, provides offenders with work skills that could transfer to productive employment after release. The department provides educational programs at all of the facilities.

The Department of Corrections received the majority of its funding for operations from the state's General Fund. In fiscal year 2006, General Fund appropriations financed 83 percent of the department's total expenditures. The department allocated state appropriations to the correctional facilities based on various factors, including prior year allocation, proposed spending plan, and offender population estimates. In addition to the state appropriations, the department had resources from other sources, including federal grants and profit from the operation of MINNCOR Industries. These other resources are dedicated for specific purposes. For example, profit from MINNCOR Industries is dedicated to offenders' vocational training.

Table 1-1 summarizes the department's General Fund allocations for Oak Park Heights, Red Wing, and Stillwater and use of those funds at the facilities for fiscal year 2006.

**Department of Corrections Facilities:
Oak Park Heights, Red Wing, and Stillwater**

**Table 1-1
Correctional Facilities
Financial Sources and Uses (General Fund Only)
Budget Fiscal Year 2006 - by Facility**

	<u>Oak Park Heights</u>	<u>Red Wing</u>	<u>Stillwater</u>
Sources of Funds:			
Appropriations	\$19,075,676	\$12,601,778	\$33,477,507
Balance Forward In	72,642	33,439	265,340
Total Sources	<u>\$19,148,318</u>	<u>\$12,635,217</u>	<u>\$33,742,847</u>
Uses of Funds:			
Payroll	\$15,477,997	\$10,247,937	\$24,615,829
Other Expenditures	3,542,858	2,185,912	8,848,312
Total Expenditures	<u>\$19,020,855</u>	<u>\$12,433,849</u>	<u>\$33,464,141</u>
Balance Forward Out	\$ 93,256	\$ 132,464	\$ 206,882
Transfers Out	34,207	68,904	71,824
Total Uses	<u>\$19,148,318</u>	<u>\$12,635,217</u>	<u>\$33,742,847</u>

Source: Minnesota Accounting and Procurement System.

The Office of the Legislative Auditor selected the correctional facilities at Oak Park Heights, Red Wing, and Stillwater for audit based on an annual assessment of state agencies and programs. We used various criteria to determine the entities to audit, including the size and type of each agency's financial operations, length of time since the last audit, changes in organizational structure and key personnel, and available audit resources.

Audit Approach

Our audit was conducted in accordance with *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we obtain an understanding of the department's internal controls relevant to the audit objectives. We used the guidance contained in *Internal Control-Integrated Framework*, published by the Committee of Sponsoring Organizations of the Treadway Commission,¹ as our criteria to evaluate agency controls. The standards also require that we plan the audit to provide reasonable assurance that the department complied with financial-related legal provisions that are significant to the audit. In determining compliance with legal provisions, we considered requirements of laws, regulations, contracts, and grant agreements.

To meet the audit objectives, we gained an understanding of the facilities' financial policies and procedures. We considered the risk of errors in the accounting records and noncompliance with relevant legal provisions. We analyzed accounting data to identify unusual trends or significant changes in financial operations. We examined documents supporting the facilities' internal controls and compliance with laws, regulations, contracts, and grant provisions.

¹ The Treadway Commission and its Committee of Sponsoring Organizations (COSO) were established in the mid-1980s by the major national associations of accountants. One of their primary tasks was to identify the components of internal control that organizations should have in place to prevent inappropriate financial activity.

Chapter 2. Computer Systems Security Controls

Chapter Conclusions

The Department of Corrections and the Oak Park Heights, Red Wing, and Stillwater facilities did not adequately restrict computer security clearances to certain computerized business systems. The department's overall security strategy lacked important components. In addition, the department and these facilities did not provide adequate security access controls to its offender accounting system or to the state's accounting and payroll systems.

Background

The Department of Corrections' central office and its individual facilities share the responsibility to protect the integrity of its computerized business systems, which include the department's offender accounting system, the state's accounting and procurement system, and the state's payroll and personnel system. The central office designated a security administrator to monitor and maintain security profiles for the department's financial services staff. Each facility assigns security profiles needed by its employees to perform their work with approval by the central office security administrator. The department conducts an annual security review where the central office security administrator and the facility supervisors assess whether any security profiles require deletion from the system.

Offender Transaction Account Group System

The department maintains a custodial bank account for offenders on its computerized offender accounting system. The department records offenders' financial activity, such as canteen purchases, payments to victim restitution funds, deposits, interest earnings, transfers, and other withholding on the system.

Minnesota Accounting and Procurement System and State Employee Management System

The department, like most state agencies, uses the state's accounting system (the Minnesota Accounting and Procurement System) to purchase goods and services, pay vendors, record accounting transactions, and prepare required financial reports. The department also uses the state's central personnel and payroll system (the State Employee Management System). Two central oversight agencies maintain the systems: 1) the Department of Employee Relations provides support for personnel functions, and 2) the Department of Finance oversees payroll processing.

Department of Corrections Facilities: Oak Park Heights, Red Wing, and Stillwater

Audit Objective

The primary objective of our computer systems security access audit focused on answering the following question:

- Did the department's and the Oak Park Heights, Red Wing, and Stillwater facilities' internal controls provide reasonable assurance that access to computer subsystems, the state's accounting system, and the state's personnel and payroll system are limited to the duties of individuals authorized to work in each respective area and are reviewed for incompatible groups on a periodic basis?

Current Findings and Recommendations

1. The Department of Corrections' security strategy for its offender accounting system and access to the state's accounting system lacked important components.

The department's security strategy for its offender accounting system and the state's accounting system lacked important components, such as implementing procedures that identified potential vulnerabilities and incompatible security profiles, informing the security administrator about changes in job responsibilities, and monitoring and assessing existing controls. These deficiencies contributed to Findings 2 and 3 in this chapter.

Security procedures and standards are essential components in a security infrastructure. Effective security policies typically require security administrators to understand the system they administer and the security profiles offered to system users. The department's security administrators did not identify which security profiles created incompatible access for its offender accounting system, because the department did not identify potential vulnerabilities. The department also did not implement view only options, typically used to limit or eliminate security profiles with unnecessary or excessive access. Management communicated its commitment to security in broad policies, but it did not transform these policies into detailed security standards for specific systems. Documenting this information is vital, because it provides security professionals with criteria to configure security tools and make consistent security decisions. Documentation also helps ensure the continued understanding and operation of critical security controls should key employees leave the organization.

Supervisors also play a key role in the security infrastructure. Supervisors must understand security risks so they can properly authorize access to users. Supervisors need to promptly report staffing changes, such as changes in job responsibilities or employment, to the security administrators so their access can be updated. The department did not have a formal process to communicate staffing changes to the security administrators.

Finally, the department did not periodically validate the effectiveness of its security controls. On a continuing basis, security administrators must review user profiles for excessive, unneeded, and incompatible access and make changes or delete access as necessary. User profiles should

Department of Corrections Facilities: Oak Park Heights, Red Wing, and Stillwater

be based on access given only for those duties that are essential to the position responsibilities. In cases where the employee's job duties make it difficult to remove incompatible access from an employee, other mitigating controls must exist to prevent or detect these transactions. State policies² require agencies to develop written plans describing the independent and periodic review of the mitigating controls to properly maintain a secure environment. The department's security policy³ requires unscheduled audits, although these audits are not currently performed.

Recommendations

- *The department should document basic security procedures and standards for its computerized offender accounting system. Incompatible access profiles and mitigating controls should be established in policy for its systems.*
- *The department should limit unnecessary or excessive access by providing view only clearances for selected users and implementing a form to capture and communicate staffing changes to the security administrators. The department should also communicate these policies into detailed security standards for specific systems.*
- *The department should periodically validate the effectiveness of its security controls. Mitigating control reviews should be performed to supplement the annual security reviews. Unscheduled audits by information technology units should also be performed.*

2. The department did not adequately control access to the offender accounting system.

The department did not limit incompatible security profiles and other system vulnerabilities within the offender accounting system. The department uses an accounting system to manage offender account transactions at all of the facilities. The system records detailed account information by offender and posts daily summary transactions to the state's accounting system.

The following weaknesses existed in the offender accounting system:

- The department did not identify or mitigate incompatible security access profiles for 27 employees with access to offender accounts.
- The department did not promptly remove access for five former employees and four employees that transferred job duties.

² Minnesota Accounting and Procurement System Operations Manual 1101-07 states, "In circumstances where staffing limitations prevent an agency from adequately separating incompatible functions, compensating controls, such as independent reviews, should be established."

³ DOC Policy 105.205, Procedure F states, "IT units will conduct unscheduled audits to verify software security tools, detect unauthorized or misuse of software or hardware, and to maintain the security and integrity of agency computer resources."

Department of Corrections Facilities: Oak Park Heights, Red Wing, and Stillwater

- The department also did not limit access to a powerful “administrator” security profile, allowing 11 users to change employee security profiles within the offender accounting system. Typically, the administrator security profile is limited to two or three individuals.
- Finally, the department did not require users to change passwords periodically and did not design sophisticated password requirements regarding length and composition of password characters, such as requiring combinations of lower and upper case alpha and numeric characters and special symbols.

A successful computer security system requires that the department and the facilities work together to ensure that the required controls are in place. Without a proper understanding and administration of security systems by the security administrator, users may receive unneeded or incompatible system access. Allowing users to have unneeded or incompatible system access may give them the opportunity to initiate, process, and complete a transaction without independent or supervisory approval. In the absence of proper mitigating controls, this creates the risk that an employee may abuse this access and possibly use it for personal benefit. It also increases the risk of a user erroneously entering transactions without detection by another department employee.

Recommendations

- *The department should review and eliminate incompatible security profiles for the offender accounting system. In addition, the department should regularly review security profiles and eliminate access for former employees and employees that transferred to another division.*
- *The department should review the number of users with security administrator clearance and eliminate unnecessary ones.*
- *The department should implement and enforce comprehensive password management controls.*

3. The department and the Oak Park Heights, Red Wing, and Stillwater facilities did not adequately restrict employees’ access to the state’s accounting and payroll/personnel systems.

The central office and facility computer security administrators did not detect certain incompatible or unnecessary security profiles during the annual systems access reviews. For the state’s accounting system, 11 of 20 employees in the consolidated business office had incompatible access without any mitigating controls. Each employee had access to purchasing, receiving, and disbursing functions, enabling them to process erroneous transactions without

Department of Corrections Facilities: Oak Park Heights, Red Wing, and Stillwater

detection. In addition, the department did not remove access to the accounting system for two former employees in a timely manner.

For the payroll and personnel system, three employees had incompatible security access profiles to key payroll security components, allowing access to both establish and make payments to that account. Three financial service employees had greater system access than needed to perform their job duties.

The security administrators appeared unaware of incompatible profiles identified by the Department of Finance for the state's accounting system and, therefore, could not provide a proper review of security access as discussed in Finding 1. Allowing incompatible, unnecessary, or excessive access increases the risk of intentional and unintentional errors occurring without detection by the department. Without mitigating controls, unauthorized accounting and payroll transactions may occur and remain undetected.

Recommendation

- *The department should eliminate incompatible security profiles for the state's computerized business systems or implement mitigating controls. In addition, the department and the facilities should review security profiles and eliminate access for former employees.*

**Department of Corrections Facilities:
Oak Park Heights, Red Wing, and Stillwater**

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**Department of Corrections Facilities:
Oak Park Heights, Red Wing, and Stillwater**

Chapter 3. Payroll Expenditures

Chapter Conclusions

The Oak Park Heights, Red Wing, and Stillwater facilities' controls provided reasonable assurance that payroll expenditures were accurately reported in the accounting records and complied with applicable legal provisions and management's authorizations.

For the items tested, employee pay rates and leave accrual rates complied with compensation plans.

Background

Payroll represented the largest expenditure for the three facilities, comprising about 71 percent of the Oak Park Heights, Red Wing, and Stillwater facilities' total expenditures. Employees at the three facilities used the self-service time entry process in the personnel and payroll system to record their hours worked and leave taken. The self-service time entry process automated employee timesheets and allowed for electronic supervisory approval. The department used a standardized exception report to monitor transactions where an employee did not enter their own time, or where the primary supervisor did not authorize hours worked. At the end of each pay period, the financial services staff at the Stillwater Correctional Facility processed the payroll transactions.

Department policy⁴ requires supervisors to review time records for accuracy by comparing employee timesheets with shift schedules and other leave records. The verification gave assurance on the accuracy of pay codes charged, hours entered, and supervisory approval. The guidelines used by the Department of Corrections required facilities to select a minimum sample of ten percent of its employees each quarter for review. Upon completion of the review, a report must be written "detailing problems found, corrective actions needed, concerns, or excellence noted."⁵

Table 3-1 shows the region's total personnel and payroll costs by facility for fiscal years 2005 and 2006.

⁴ DOC Policy 104.450, Procedure B, Part 1 states: "Time records must be reviewed for accuracy by comparison with a time record system, approved leave and overtime requests, shift exchange slips, and other appropriate documents or reports."

⁵ DOC Policy 104.450, Procedure D, Part 5.

**Department of Corrections Facilities:
Oak Park Heights, Red Wing, and Stillwater**

**Table 3-1
Correctional Facility
Payroll Expenditures
Budgetary Fiscal Years 2005 and 2006**

<u>Facility</u>	<u>2005</u>	<u>2006</u>
Oak Park Heights	\$14,473,551	\$15,261,751
Red Wing	9,318,002	10,022,601
Stillwater	<u>22,899,642</u>	<u>23,814,617</u>
Total	<u>\$46,691,195</u>	<u>\$49,098,969</u>

Source: Minnesota Accounting and Procurement System as of March 22, 2007.

Audit Objectives

Our audit of personnel and payroll expenditures focused on the following questions:

- Did the Oak Park Heights, Red Wing, and Stillwater facilities' controls provide reasonable assurance that payroll expenditures were accurately reported in the accounting records and complied with applicable legal provisions and management's authorizations?
- For the items tested, did the department comply, in all material respects, with the significant finance-related legal provisions concerning payroll?

There were no findings or recommendations in this area.

**Department of Corrections Facilities:
Oak Park Heights, Red Wing, and Stillwater**

Chapter 4. Professional/Technical Services

Chapter Conclusions

For professional/technical services, the Oak Park Heights, Red Wing, and Stillwater facilities' controls provided reasonable assurance that it adequately safeguarded its assets and complied with applicable legal provisions and management's authorizations. However, as discussed in Finding 4, the facilities did not accurately record certain professional/technical services in the state's accounting system and did not always prepare written contracts for certain professional/technical services.

Background

Professional/technical services represent expenditures that are intellectual in nature and include consultation, analysis, evaluation, prediction, planning, programming, or recommendation. These services generally cannot be performed by the staff and need to be obtained from outside vendors. Most of the Oak Park Heights, Red Wing, and Stillwater facilities' professional/technical costs related to educational and technology services.

Table 4-1 shows the facilities' total professional/technical expenditures by service type for fiscal years 2005 and 2006.

**Table 4-1
Oak Park Heights, Red Wing, and Stillwater Correctional Facilities
Professional/Technical Expenditures by Service
Budgetary Fiscal Years 2005 and 2006**

<u>Professional/Technical Service</u>	<u>2005</u>	<u>2006</u>
Educational and Instruction	\$103,381	\$226,631
Information Technology Development	89,473	0
Health Care	57,772	66,715
Environmental Agriculture and Science	35,477	800
Architect and Engineering	27,551	72,685
Other Services	8,076	7,743
Total Expenditures	<u>\$321,730</u>	<u>\$374,574</u>

Source: Minnesota Accounting and Procurement System as of March 26, 2007.

Department of Corrections Facilities: Oak Park Heights, Red Wing, and Stillwater

Audit Objective

The primary objective of our audit of professional/technical services was to answer the following questions:

- Did the Oak Park Heights, Red Wing, and Stillwater facilities' controls provide reasonable assurance that professional/ technical service expenditures were accurately reported in the accounting records and complied with applicable legal provisions and management's authorizations?
- For the items tested, did the facilities comply, in all material respects, with the significant finance-related legal provisions concerning professional/technical services?

Current Finding and Recommendations

4. The Oak Park Heights, Red Wing, and Stillwater facilities did not properly record or prepare written contracts for certain professional and technical service transactions in the state's accounting system.

The facilities did not prepare contracts for one dietician service (\$200) and several court reporter service contracts totaling \$4,169. Our test of ten sample items found that seven were miscoded and did not have written contracts for the required services. The miscodings contributed to the facilities not preparing contracts for these purchases as the state's accounting system prompts agencies to prepare contracts if certain codes are used.

The state's procurement and accounting system requires specific commodity codes to identify the type of professional/technical services. The commodity code in the procurement system defaults to specific accounting code to ensure an accurate coding of purchases. The facilities, however, changed the default commodity codes from professional/technical services to different codes that did not require contracts.

Commodity and accounting codes should accurately reflect the nature of the expenditure. Regardless of how the facilities code their transactions, they should properly prepare contracts when required. Additionally, without written contracts, the facilities are at risk for overcharges, liability claims, and other deliverables relating to quality and time restrictions.

Recommendations

- *The department should prepare written contracts for all professional/technical services.*
- *The department should accurately record professional/technical services in the accounting system.*

Chapter 5. Offender Accounts

Chapter Conclusions

The department and the Oak Park Heights, Red Wing, and Stillwater facilities properly recorded offender account transactions in the accounting records and in accordance with management's authorizations. However, the facilities did not properly monitor offender account reconciliations, as discussed in Finding 5.

For the items tested, the department and the facilities complied with legal provisions governing the order it applies charges to offender account balances and the posting of interest earned. However, the department inconsistently charged costs to the offender benefit account, resulting in certain unallowable expenses, as discussed in Finding 6.

Background

Minnesota Statutes⁶ designate the warden of each correctional facility as custodian over funds belonging to confined offenders. The department accounted for offender funds on the state's accounting system and maintained detailed records on its computerized offender accounting system. The state invested the funds through the State Board of Investment and posted interest to the individual accounts and facility benefits account quarterly. Each facility also had an account established for the benefit of all offenders.

The Moose Lake Correctional Facility processed offender deposits for all facilities. Each facility recorded detailed information supporting offender purchases or payments on the offender accounting system. Each facility disbursed cash and checks for offender transactions through its local bank account and periodically requested reimbursement from the state's accounting system to an authorized level. Facility accounting staff reconciled the bank account to the offender accounting system monthly. Facility staff also reconciled the offender accounting system to the state's accounting system on a monthly basis. This reconciliation included the authorized checking accounts discussed above and additional savings accounts invested at the state level for offenders.

⁶ *Minnesota Statutes* 2006, 241.08, subd. 1

**Department of Corrections Facilities:
Oak Park Heights, Red Wing, and Stillwater**

Table 5-1 summarizes the financial activity of offender accounts by facility for fiscal year 2006.

**Table 5-1
Offender Financial Activity by Correctional Facility
Fiscal Year 2006**

	Oak Park Heights	Red Wing	Stillwater
Revenues	\$758,338	\$172,633	\$3,052,969
Expenditures	(768,080)	(188,086)	(2,986,395)
Total	<u>\$(9,742)</u>	<u>\$(15,453)</u>	<u>\$66,574</u>

Source: Offender Accounting System as of April 6, 2007.

Audit Objectives

Our audit of offender account activity focused on the following questions:

- Did the department’s controls ensure that it properly safeguarded offender funds and accurately recorded transactions on the state’s accounting system and the offender accounting system?
- Did the department’s controls ensure that it was in compliance with legal provisions governing the order it applied charges to offender account balances and the posting of interest earned?

Current Findings and Recommendations

5. The Oak Park Heights, Red Wing, and Stillwater facilities did not properly review offender account reconciliations.

The department’s facility accounting supervisors at Oak Park Heights, Red Wing, and Stillwater did not review documentation for offender account reconciliations. Each of the facilities’ staff reconciled the bank statements to the offender accounts, but did not provide the supervisors with documentation, such as cancelled checks, to properly review the propriety of each transaction. Also, staff at the Stillwater facility did not submit supporting documentation to their supervisors for the reconciliation between the state accounting system and the offender accounting system.

Proper documentation is essential to support reconciliations of financial transactions. Without proper documentation, supervisors cannot verify the propriety of reconciling items or the monthly activity.

Department of Corrections Facilities: Oak Park Heights, Red Wing, and Stillwater

Recommendation

- *The facilities should ensure that supporting documentation is provided for both the local bank checking accounts and the state accounting system reconciliations.*

6. The department inconsistently charged expenses to the offender benefit account.

The department did not consistently charge certain costs to the facilities. Each facility maintained an offender benefit account.⁷ The department established a policy⁸ to provide guidelines on allowable and prohibited costs from the benefit account, which typically is used to cover purchases or expenses benefiting all or most offenders. An analysis of the benefit account transactions resulted in the following concerns:

- The Stillwater facility charged the benefit account for coffee purchases specifically for the industry program. From April to August 2004, the facility charged over \$1,900 to the benefit account for coffee consumed by offenders in the industry program. Other facilities with an industry program routinely charge coffee to the food services area, as did Stillwater before and after the five-month period in question.
- The Stillwater facility charged approximately \$586 of laundry machine repairs to the facility benefit account in fiscal year 2005. An additional \$13,500 was charged to a phone commission account for laundry equipment and repairs, which is another discretionary account controlled by the facility. Red Wing and Oak Park Heights facilities charged laundry repairs to plant operations. According to the offender account policy, routine maintenance costs are not an allowable use of benefit account funds unless the state owned property “benefits all or most offenders, or benefits the specific operation generating funds....” Facilities did not handle repair costs consistently.
- The Oak Park Heights facility charged approximately \$1,100 of barber shop costs to the offender benefit account in fiscal years 2005 and 2006. Although basic hair cuts were free at all three facilities, only the Red Wing facility paid for a contract barber out of the operating budget. The Stillwater and Oak Park Heights facilities used offenders to cut hair of other offenders. The facilities used operating funds for the Red Wing barber contract and the Stillwater supplies but charged the offender benefit account for the Oak Park Heights’ supplies. Although the barber shop supplies or costs do benefit all or most offenders at a facility, these costs were not accounted for consistently.

⁷ The offender benefit account receives funding from various sources by statutory authority. Some of these items include contraband seized from offenders, unclaimed offender funds who have died, been released, or escaped, excess interest earnings not allocated to specific offender accounts, and canteen profits from offender purchases.

⁸ Department of Correction Policy 300.100 Inmate Accounts.

**Department of Corrections Facilities:
Oak Park Heights, Red Wing, and Stillwater**

By charging these costs to the benefit trust account instead of the general operations account, the department reduced the amount that could be used for the benefit of all the offenders.

Recommendation

- *The department should comply with its offender benefit account policy and consistently apply charges made to it.*

Chapter 6. Canteen Operations

Chapter Conclusions

The department's controls provided reasonable assurance that it accurately recorded canteen sales in the accounting records, adequately safeguarded its assets, and complied with applicable legal provisions and management's authorizations. However, the department reduced canteen profits inappropriately by charging sales commissions, as discussed in Finding 7.

For the items tested, the department generally complied with significant finance-related legal provisions. However, the department did not account for canteen operations in the correct fund in the state's accounting system, as discussed in Finding 8.

Background

Canteen operations are part of the MINNCOR division of the Department of Corrections. MINNCOR is an enterprise activity that provides offenders with an opportunity to work and acquire certain knowledge and skills prior to release. MINNCOR operates the canteen for the benefit of the offenders where they can purchase approved items that extend beyond necessities. Prior to 2003, each facility operated its own canteen, where offenders would purchase items on site. After that, the department consolidated the canteen operations into the Oak Park Heights Correctional Facility. The department uses a warehouse at that facility to maintain the canteen inventory and processes offender requests from all adult correctional facilities. The Oak Park Heights Correctional Facility receives the offenders' orders, packages them, delivers them to the respective facility, and posts the transactions to the offender's account. The department records all of the financial transactions on its computerized offender accounting system and purchasing system (Traverse). Summarized financial data from the department's computer systems is uploaded periodically to the state's accounting system. The canteen is required to operate on at least a break-even basis.

Table 6-1 shows the total canteen sales, selected expense categories, and profit or loss calculations for all correctional facilities for fiscal years 2003 through 2006.

**Department of Corrections Facilities:
Oak Park Heights, Red Wing, and Stillwater**

**Table 6-1
Canteen Profit Calculations – All Facilities
Fiscal Years 2003 to 2006**

	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>
Sales	\$2,942,954	\$5,279,802	\$5,618,260	\$5,812,851
Less:				
Cost of Goods Sold	(2,337,077)	(3,196,470)	(3,796,515)	(3,732,397)
Direct Costs:				
Staff Labor	(269,987)	(339,417)	(342,216)	(379,824)
Offender Labor	(56,785)	(82,996)	(78,176)	(83,669)
Other Overhead		(576,087)	(666,197)	(660,000)
Other Direct Costs	(88,138)	(288,800)	(306,576)	(338,644)
General/Administrative:				
Staff Salaries	(28,641)	(32,221)	(65,785)	(75,695)
Other G/A Costs	(46,159)	(23,234)	(32,064)	(25,080)
Central G/A Costs:				
Marketing	(42,772)	(35,805)	(30,726)	(14,676)
Interest Income – Investments	11,792	14,351	31,599	48,948
Agency Indirect	(49,197)	(76,268)	(123,035)	(111,280)
Other Central G/A Costs	<u>(264,270)</u>	<u>(357,645)</u>	<u>(273,756)</u>	<u>(192,487)</u>
Net Profit (Loss)	<u>\$ (228,280)</u>	<u>\$ 285,211</u>	<u>\$ (65,188)</u>	<u>\$ 248,047</u>

Source: Summarized from Department of Corrections' MINNCOR profit and loss statements as of March 22, 2007.

Audit Objectives

The scope of our audit of canteen operations concentrated primarily on sales and focused on the following questions:

- Did the department's controls provide reasonable assurance that canteen operations were accurately reported in the accounting records and complied with applicable legal provisions and management's authorizations?
- For the items tested, did the department comply, in all material respects, with the significant finance-related legal provisions concerning canteen operations?

Department of Corrections Facilities: Oak Park Heights, Red Wing, and Stillwater

Current Findings and Recommendations

7. The Department of Corrections' MINNCOR division inappropriately retained commissions collected from canteen sales.

MINNCOR did not credit canteen operations for commissions it charged on telephone minute sales and the sales of tickets and other tokens offenders used instead of cash. Instead, MINNCOR included this revenue as part of its prison industries operation.

MINNCOR charged a one percent commission on telephone minute sales. Facilities paid this commission from general offender accounts, but did not allocate it to specific offenders. In addition, offenders paid a ten percent commission to buy canteen tokens and tickets. They then used the tokens and tickets to purchase goods from third party vendors or offender services offered by the facility. MINNCOR retained these commissions. Since fiscal year 2003, MINNCOR's annual revenue from these commissions averaged over \$28,000.

According to DOC policy 302.010, "...The canteen is operated solely for the benefit of the offenders and will be a self-supporting operation. Operating costs directly involved with the canteen will be charged to and paid for from canteen revenue." The policy defines operating costs as "...breakage, theft, spoilage, delivery, supplies, equipment depreciation, inventory, equipment, software purchases or rentals, offender and staff wages, and facility and general administrative expenses allocated to the canteen."

Recommendations

- *The department should eliminate commission charges for phone and ticket sales unless they offset costs of the canteen operations.*
- *The department should credit past commission revenue to canteen operations.*

8. The Department of Corrections' MINNCOR division did not account for canteen operations in the fund required by statute, nor did it credit canteen profits to that fund.

MINNCOR did not account for canteen operations in its prison industries fund in the state's accounting system. In addition, MINNCOR did not transfer canteen profits or related interest earning to the Social Welfare Fund. *Minnesota Statutes*⁹ require that the canteen be operated in the Social Welfare Fund, which is a fund in the state's accounting system that records offender funds held by the state or other funds held on behalf of the offenders, such as the Offender Benefit Account. *Minnesota Statutes* further state that any profit generated by the canteen would remain in the Social Welfare Fund and be used for the benefit of the offenders at each institution.

⁹ *Minnesota Statutes* 2006, 16A.72, subd. 7.

Department of Corrections Facilities: Oak Park Heights, Red Wing, and Stillwater

However, MINNCOR did not distribute any canteen profits (estimated to be about \$533,000¹⁰) since taking over control of canteen operations in 2003.

While under its control, MINNCOR prepared profit and loss statements for the overall canteen operation, but did not allocate profit and loss by facility. Without facility level profit and loss statements, MINNCOR could not determine the amount to credit to each facility's offender benefit account. The department established procedures¹¹ for MINNCOR's preparation of canteen financial statements and the distribution of profit. Those procedures included the preparation of monthly facility level profit and loss statements; however, staff stated they were not aware of the procedures' requirements.

In addition, in its overall canteen profit and loss statements, MINNCOR included certain general administrative costs that may not be appropriate to the canteen's operations. For example, the profit and loss statements included costs identified as "marketing." Since canteen items are marketed only to the offender population, these costs may not be appropriate.

Recommendations

- *The department should account for canteen operations in the state's Social Welfare Fund.*
- *The department should prepare monthly profit and loss statements by facility for canteen operations and credit the profits and related interest earnings to each facility's offender benefit account.*
- *The department should ensure all costs charged to the canteen are appropriate.*

¹⁰ This estimate does not include the commission revenue not credited to canteen operations discussed in Finding 7.

¹¹ DOC Policy 302.010, Procedure B, Part 4 states, "MINNCOR will distribute canteen profit in excess of net income and debt to the facilities' social welfare funds to be used for the benefit of the offenders."

**Department of Corrections Facilities:
Oak Park Heights, Red Wing, and Stillwater**

**Status of Prior Audit Issues
As of April 6, 2007**

July 27, 2006, Legislative Audit Report 06-20 covered the selected Department of Corrections' activities for the two years ended June 30, 2005. The scope of the audit included employee payroll and governmental grants and subsidies. The report contained six findings that we considered resolved.

Other Audit Coverage

July 27, 2006, Legislative Audit Report 06-21

We also issued a Special Review of MINNCOR Industries for the period July 1, 2003, through March 31, 2006. We conducted a special review after receiving allegations concerning conflicts of interest, questionable contracting practices, improper disposition of state surplus property, and inappropriate donations to certain nonprofit organizations. The special review contained eight findings. These findings were outside our audit scope and, accordingly, we did not follow up on them.

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.

**Department of Corrections Facilities:
Oak Park Heights, Red Wing, and Stillwater**

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September 14, 2007

James R. Nobles, Legislative Auditor
Office of the Legislative Auditor
Room 140 Centennial Building
658 Cedar Street
St. Paul, MN 55155-1603

Dear Mr. Nobles:

Thank you for the opportunity to discuss and comment on the recommendations arising from the recent audit of the Department of Corrections. The efforts of your office are appreciated in conjunction with completing this audit. Below please find a response for each finding identified in the audit report.

Recommendation

The department should document basic security procedures and standards for its computerized offender accounting system. Incompatible access profiles and mitigating controls should be established in policy for its systems.

Response

The Department of Corrections agrees with this recommendation. Documentation and procedures will be prepared in conjunction with a scheduled upgrade to the computerized offender accounting system, to occur in the next several months.

Person Responsible:
Lon Erickson

Estimated Completion Date:
March 2008

Recommendation

The department should limit unnecessary or excessive access by providing view only clearances for selected users and implementing a form to capture and communicate staffing changes to the security administrators. The department should also communicate these policies into detailed security standards for specific systems.



Response

The Department of Corrections agrees with this recommendation and already provides view only clearance for certain users. The department will review and adjust the clearance profiles as appropriate. We will work internally to develop and implement the use of a form to communicate staffing changes to security administrators in a more timely manner. The new procedures will be documented in the security standards discussed in the previous finding.

Person Responsible:
Lori Caspers

Estimated Completion Date:
March 2008

Recommendation

The department should periodically validate the effectiveness of its security controls. Mitigating control reviews should be performed to supplement the annual security reviews. Unscheduled audits by information technology units should also be performed.

Response

The Department of Corrections agrees with this recommendation. Identification of mitigating controls and related procedures will be developed and implemented in conjunction with a scheduled upgrade to the computerized offender accounting system in the next several months.

Person Responsible:
Lon Erickson

Estimated Completion Date:
March 2008

Recommendation

The department should review and eliminate incompatible security profiles for the offender accounting system. In addition, the department should regularly review security profiles and eliminate access for former employees and employees that transferred to another division.

Response

The Department of Corrections agrees with this recommendation. Incompatible security profiles for the offender accounting system will be identified and documented. The department will limit the use of incompatible profiles to the extent possible, while continuing to ensure transactions are processed in an efficient manner. Mitigating and internal controls are used and will continue to be used to ensure employees who are granted incompatible profiles process transactions in an appropriate manner. Security profiles will be reviewed and modified as necessary on at least an annual basis, in addition to using the form discussed previously to eliminate access for former employees or employees who have changed jobs.

Person Responsible:
Lori Caspers

Estimated Completion Date:
December 2007

Recommendation

The department should review the number of users with security administrator clearance and eliminate unnecessary ones.

Response

The Department of Corrections agrees with this recommendation. The list of users with security administrator clearance in the offender accounting system will be reviewed and the clearance will be limited to key staff.

Person Responsible:
Lori Caspers

Estimated Completion Date:
October 2007

Recommendation

The department should implement and enforce comprehensive password management controls.

Response

The Department of Corrections agrees with this recommendation. The department's security administrator will work with the vendor to develop and implement appropriate password management controls in conjunction with a scheduled upgrade to the computerized offender accounting system.

Person Responsible:
Lon Erickson

Estimated Completion Date:
March 2008

Recommendation

The department should eliminate incompatible security profiles for the state's computerized business systems. In addition, the department and the facilities should review security profiles and eliminate access for former employees.

Response

The Department of Corrections agrees with this recommendation. Incompatible security profiles will be reviewed and limited as appropriate, with the proper controls in place. In the past, security profiles have been reviewed on an annual basis as recommended in a previous audit report. The department will continue the annual review process, but will also incorporate the use the previously mentioned form.

Person Responsible:
Lori Caspers

Estimated Completion Date:
Completed

Recommendation

The department should prepare written contracts for all professional/technical services.

Response

The Department of Corrections recognizes the value and importance of written contracts and agrees with this recommendation. The department works very hard to ensure written contracts are processed whenever necessary, and routinely delivers training to staff on the appropriate use of professional/technical contracts. The failure to process a contract for one dietician service (\$200) was an oversight. There was a misinterpretation regarding the nature of court reporter services that were purchased (\$4,169) and whether they were considered a professional/technical service or a purchased service. These, and other service purchases, will be carefully reviewed by fiscal and contract management staff to ensure contracts are processed as required.

Person Responsible:
Lori Caspers

Estimated Completion Date:
Completed

Recommendation

The department should accurately record professional/technical services in the accounting system.

Response

The Department of Corrections recognizes the importance of accurately reporting expenditures and agrees with this recommendation. The findings in the audit report were errors as the result of a misinterpretation of instructions distributed by the department’s central office finance staff. Procedures have been clarified and the use of proper object codes will continue to be monitored.

Person Responsible:
Lori Caspers

Estimated Completion Date:
Completed

Recommendation

The facilities should ensure that supporting documentation is provided for both the local bank checking accounts and the state accounting system reconciliations.

Response

The Department of Corrections agrees with this recommendation. Procedures have been implemented to ensure facility accounting supervisors are provided with and properly review all reconciliations and the supporting documentation.

Person Responsible:
Lori Caspers

Estimated Completion Date:
Completed

Recommendation

The department should comply with its offender benefit account policy and consistently apply charges made to it.

Response

The department's policy allows facilities a certain amount of discretion when determining what items to charge to the trust fund benefit account and other sources of offender-generated funds. This is a necessary practice as the revenues of these non-general funds available can vary significantly by facility based on the offender population and location of each facility. The guiding principle is the funds should be used for the benefit of all offenders. Existing guidelines provide specific examples in addition to broader categories to aid department staff in making informed decisions.

Person Responsible:
Chris Dodge

Estimated Completion Date:
Completed

Recommendation

The department should eliminate commission charges for phone and ticket sales unless they offset costs of the canteen operations.

Response

The Department of Corrections will continue to charge a commission on the sales of phone time and tickets to help offset the cost of producing and/or selling the items. Any residual profit is similar to the profit generated by the sales of other products sold in the canteen. Phone time, tickets and tokens are used by offenders to purchase goods or services that are not provided by MINNCOR.

Person Responsible:
Richard Schoenthaler

Estimated Completion Date:
Completed

Recommendation

The department should credit past commission revenue to canteen operations.

Response

The commissions were recorded on the profit and loss statements as sales, with no corresponding cost of goods. The result is the full amount is already included in the gross profit calculation. No additional action is necessary.

Person Responsible:
Richard Schoenthaler

Estimated Completion Date:
Completed

Recommendation

The department should account for canteen operations in the state's Social Welfare fund.

Response

In May 2007 MINNCOR deposited cumulative net profits from fiscal year 2003 through fiscal year 2006, in the amount of \$239,790.27, into the social welfare fund. The department deposited *cumulative net profits* with no recognition of losses because, historically, general fund appropriations have not been used to offset canteen losses. Profits from fiscal year 2007 will be deposited in the social welfare fund by the end of the second quarter of fiscal year 2008. Due to a change in the law effective July 1, 2007, MINNCOR will now retain all canteen profits and deposits to the social welfare fund will no longer be necessary.

Person Responsible:
Richard Schoenthaler

Estimated Completion Date:
December 2007

Recommendation

The department should prepare monthly profit and loss statements by facility for canteen operations and credit the profits and related interest earnings to each facility's offender benefit account.

Response

MINNCOR operates a centralized canteen operation, versus separate operations in each facility. All transactional and physical work is completed at one location, and merchandise is shipped to individual facilities for distribution. Consequently, it is not feasible to prepare separate profit and loss statements for each facility. The department made the decision to deposit canteen profits, through fiscal year 2007, into a centralized social welfare fund to be used for the benefit of all offenders within the system, including a scheduled upgrade to the computerized offender accounting system. Due to a change in the law effective July 1, 2007, MINNCOR will now retain all canteen profits and deposits to the social welfare fund will no longer be necessary.

Person Responsible:
Richard Schoenthaler

Estimated Completion Date:
Completed

Recommendation

The department should ensure all costs charged to the canteen are appropriate.

Response

The Department of Corrections agrees with this recommendation. MINNCOR is a consolidated business, and the canteen operation is only one unit within that business. The majority of general and administrative costs are allocated to each business unit based on use. Costs are carefully monitored to ensure they are valid costs associated with the business unit. Some costs, however, are allocated across

all business units because they benefit all business units and ensure the continued success and fulfillment of MINNCOR's mission to be self-sufficient. The department will continue to monitor and review these cost allocations to ensure they are applied appropriately.

Person Responsible:
Richard Schoenthaler

Estimated Completion Date:
Completed

It is the goal of the department to have corrected all of the audit report findings no later than March 2008. Thank you again for the efforts of your staff.

Sincerely,

Joan Fabian
Commissioner

Copy: Dennis Benson, Deputy Commissioner
Harley Nelson, Deputy Commissioner
Lisa Cornelius, Assistant Commissioner
Chris Dodge, Agency Chief Financial Officer