



**FINANCIAL AUDIT DIVISION REPORT**

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**Department of Natural  
Resources**

**Federal Compliance Audit**

**Year Ended June 30, 2008**

**March 26, 2009**

**Report 09-07**

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FINANCIAL AUDIT DIVISION

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## OFFICE OF THE LEGISLATIVE AUDITOR

State of Minnesota • James Nobles, Legislative Auditor

March 26, 2009

Senator Ann H. Rest, Chair  
Legislative Audit Commission

Members of the Legislative Audit Commission

Mr. Mark Holsten, Commissioner  
Minnesota Department of Natural Resources

This report presents the results of our audit of certain federal financial assistance programs administered by the Department of Natural Resources during fiscal year 2008. 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 Natural Resources.

We discussed the results of the audit with department staff at an exit conference on March 10, 2009. This audit was conducted by David Poliseno, CPA, CISA, CFE, (Audit Manager) and Carl Otto, CPA, CISA (Auditor-in-Charge), assisted by auditor Xin Wang, CPA.

This report is intended for the information and use of the Legislative Audit Commission and the management of the Department of Natural Resources. This restriction is not intended to limit the distribution of this report, which was released as a public document on March 26, 2009.

We received the full cooperation of department 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 Natural Resources generally complied with and had controls to ensure compliance with provisions of laws, regulations, contracts, and grants applicable to the federal programs we audited for fiscal year 2008. However, the department had several weaknesses as noted in the six findings presented in this report.

## Key Findings

- The Department of Natural Resources did not identify, analyze, and document their internal controls over compliance with federal single audit requirements. ([Finding 1, page 7](#))
- The Department of Natural Resources did not maintain sufficient documentation for some of its federal reimbursement requests for the Sport Fish Restoration Program (CFDA 15.605) and the Wildlife Restoration Program (CFDA 15.611). ([Finding 2, page 8](#))
- The Department of Natural Resources received reimbursement from the federal government for unallowable costs for the Wildlife Restoration Program (CFDA 15.611). ([Finding 3, page 9](#))
- The Department of Natural Resources overdrew federal funds on one grant and under drew federal funds on another grant because it did not accurately report program income for grants within the Sport Fish Restoration (CFDA 15.605) and the Wildlife Restoration (CFDA 15.611) programs. ([Finding 4, page 9](#))

## Audit Scope

Programs material to the State of Minnesota's federal program compliance for fiscal year 2008.

### Selected Audit Areas:

- Fish and Wildlife Cluster<sup>1</sup> (CFDA #15.605 and #15.611)

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<sup>1</sup> A cluster of programs is a group of closely related programs that have similar compliance requirements and are treated as a single program.

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# Department of Natural Resources

## Federal Program Overview

The Department of Natural Resources administered a federal program cluster<sup>2</sup> that we considered a major federal program for the State of Minnesota, subject to audit under the federal Single Audit Act.<sup>3</sup> Table 1 identifies this federal program cluster.

**Table 1**  
**Major Federal Program**  
**Administered by the Department of Natural Resources**  
**Fiscal Year 2008**

<u>CFDA</u> <sup>1</sup>	<u>Program Name</u>	<u>Expenditures</u>
	<u>Fish and Wildlife Cluster</u>	
15.605	Sport Fish Restoration	\$14,945,846
15.611	Wildlife Restoration	<u>9,148,457</u>
	Total	<u>\$24,094,303</u>

<sup>1</sup>The Catalog of Federal Domestic Assistance (CFDA) is a unique number assigned by the federal government to identify its programs.

Source: Minnesota Accounting and Procurement System.

## Objective, Scope, and Methodology

The objective of our audit was to determine whether the Department of Natural Resources complied with federal program requirements in its administration of these federal programs for fiscal year 2008. 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

<sup>2</sup> A cluster of programs is a group of closely related programs that have similar compliance requirements and are treated as a single program.

<sup>3</sup> A major federal program for the State of Minnesota is defined 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 2008 exceeded \$23.8 million.

applicable to each of its federal programs.<sup>4</sup> In addition to specific program requirements, we examined the department's general compliance requirements related to federal assistance, including its cash management practices.

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

We determined our audit procedures based on guidance issued by U.S. Office of Management and Budget in its 2008 Compliance Supplement for federal programs. We used as our criteria to evaluate the department's internal controls the guidance contained in the *Internal Control-Integrated Framework*, published by the Committee of Sponsoring Organizations of the Treadway Commission.<sup>5</sup>

## Conclusion

The Department of Natural Resources generally complied with and had controls to ensure compliance with certain provisions of laws, regulations, contracts, and grants applicable to its major federal programs for fiscal year 2008. However, the department had some weaknesses, as noted in the following *Findings and Recommendations* section.

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<sup>4</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 9, 2008, on the State of Minnesota's basic financial statements for the year ended June 30, 2008. In accordance with *Government Auditing Standards*, we also issued our report, dated December 9, 2008, 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 09-03, Report on Internal Control Over Financial Reporting](#), issued February 13, 2009.)

<sup>5</sup> The Treadway Commission and its Committee of Sponsoring Organizations were established in 1985 by the major national associations of accountants. One of their primary tasks was to identify the components of internal control that organization should have in place to prevent inappropriate financial activity. The resulting *Internal Control-Integrated Framework* is the accepted accounting and auditing standard for internal control design and assessment.

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We have reported these weaknesses to the federal government in the *Minnesota Financial and Compliance Report on Federally Assisted Programs*, prepared by the Department of Finance.<sup>6</sup> 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 programs, and findings about control and compliance weaknesses.

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<sup>6</sup> Effective June 2008 the Legislature reorganized the Department of Finance to include the duties of the Department of Employee Relations. Although still identified in statute as the Department of Finance, in October 2008, the department changed its name to Minnesota Management and Budget. The department will seek legislative approval for the name change in the 2009 legislative session.

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## Findings and Recommendations

**The Department of Natural Resources did not identify, analyze, and document their internal controls over compliance with federal single audit requirements.**

### Finding 1

The department did not document its risk assessment for internal controls over compliance with federal general and specific program compliance requirements and the monitoring process that assesses the quality of internal control performance over time. The department has an increased likelihood of a control deficiency if it does not clearly communicate to all staff its risk, control activity, and monitoring policies and procedures.

State policy states that each agency head is responsible to identify, analyze, and manage business risks that impact the department's ability to maintain its financial strength and the overall quality of its products and government services.<sup>7</sup> This policy also requires communication of the internal control policies and procedures to all staff so they understand what is expected of them and the scope of their freedom to act. This policy further requires follow-up procedures that, at a minimum, should include mechanisms for monitoring results and reporting significant control deficiencies to individuals responsible for the process or activity involved, including executive management and those individuals in a position to take corrective action. A new audit standard<sup>8</sup> reinforced management's responsibility to have effective internal controls over its financial operations. The federal government expects that those controls also ensure compliance with federal program requirements.

The Department of Natural Resources is aware of certain risks, has control activities in place, and performs selected internal control monitoring functions. However, the department has not comprehensively identified and analyzed the risks, designed its controls to address significant risks, or developed monitoring procedures to ensure the controls are in place and are effective to reduce the significant risks identified.

Findings 2 through 6 identify deficiencies in the department's internal control procedures and specific noncompliance with federal requirements which were not prevented or detected by the department's internal control structure. If the department had a comprehensive internal control structure, it should have identified these deficiencies, assessed the degree of risk of these deficiencies, designed control procedures to address significant risks, and monitored whether

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<sup>7</sup> Minnesota Department of Finance Policy Number 0102-01.

<sup>8</sup> Statement on Auditing Standards #109.

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controls were working as designed and effective in reducing the risks to an acceptably low level. It is likely that the department will continue to have noncompliance and weaknesses in internal controls over compliance until it operates within a comprehensive internal control structure.

*Recommendation*

- *The department should regularly review and clearly document its risks, control activities, and internal control monitoring functions for federal program requirements.*

## **Finding 2**

**The Department of Natural Resources did not maintain sufficient documentation for some of its federal reimbursement requests for the Sport Fish Restoration Program (CFDA 15.605) and the Wildlife Restoration Program (CFDA 15.611).**

For 2 out of 30 sample items we tested, the department did not retain detailed documentation to support its reimbursement requests from the federal government. Although the department did not exceed its grant agreement amount, it could not provide expenditure detail to support requests of \$145,106 and \$477,764.

Generally, the department's process to determine federal reimbursement amounts included controls to ensure that costs were allowable for the programs. For example, project leaders and program coordinators reviewed various payroll and other expenditure reports for accuracy and allowable expenditures. The department used these reports to enter expenditure data into an excel spreadsheet and determine the reimbursement request for each grant program. However, the excel spreadsheets are cumulative for each grant agreement, and if staff do not print the spreadsheet, data is overwritten when they prepare the subsequent reimbursement request.

Our test focused on tracing certain reimbursement amounts to related payroll and nonpayroll reports. Since the supporting excel spreadsheets were overwritten for certain requests, we were unable to verify the total drawdown request back to the actual supporting reports.

*Recommendation*

- *The department should retain sufficient documentation to support each federal reimbursement request.*
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**The Department of Natural Resources received reimbursement from the federal government for unallowable costs for the Wildlife Restoration Program (CFDA 15.611).**

### **Finding 3**

One of 30 federal reimbursement requests we tested included vacation, sick leave, and holiday pay totaling \$2,519, which are not allowable costs. The department did not have an independent review of the spreadsheet used to determine the reimbursement amount to ensure that the person preparing the request included only allowable costs and had accurately calculated the reimbursement amount.

#### *Recommendations*

- *The department should have an independent verification of the federal reimbursement requests to ensure that the requests are for only allowable costs and are calculated accurately.*
- *The department should work with the federal government for solutions to the questioned cost of \$2,519.*

**The Department of Natural Resources overdrew federal funds on one grant and underdrew federal funds on another grant because it did not accurately report program income for grants within the Sport Fish Restoration (CFDA 15.605) and the Wildlife Restoration (CFDA 15.611) programs.**

### **Finding 4**

In preparing its final financial status reports for two of the four grants it closed out in fiscal year 2008 that earned program income, the department inaccurately reported program income<sup>9</sup> for the Sport Fish Restoration (CFDA 15.605) and the Wildlife Restoration (CFDA 15.611) programs. For these grants, the federal government allowed the department to offset its program income against the federal award. Because it understated the program income amount for one grant by \$14,013, it overdrew federal funds for that grant by the same amount. Similarly, because it overstated the program income amount for another grant by \$458, it underdrew federal funds for that grant by the same amount. The department did not properly review the program income amounts before including them on the reports to the federal government.

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<sup>9</sup> Program income is gross income received that is directly generated by the federally funded project during the grant period. For example, the department generates program income through timber sales, easements, leases, and farming agreements.

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*Recommendations*

- *The department should correct its final financial status reports for the two grants that is inaccurately reported program income. It should work with the federal government on solutions for the questioned cost of \$14,013 for the first grant and determine whether the federal government will reimburse the state for \$458 for the second grant.*
- *The department should correctly determine and record program income in accordance with program requirements.*

**Finding 5****The Department of Natural Resources did not comply with federal suspension and debarment requirements.**

The department did not verify whether vendors were suspended or debarred from providing services under federal programs. They did not perform any verification of suspension or debarment by reviewing the federal Excluded Parties List System. However, none of the vendors the department used were suspended or debarred.

Federal requirements prohibit state agencies from contracting with vendors listed as suspended or debarred.<sup>7</sup> Therefore, state agencies are required to ensure all contracted vendors over \$25,000 are not suspended or debarred.

*Recommendation*

- *The department needs to ensure compliance with federal requirements by verifying suspension and debarment for all federally funded purchases.*

**Finding 6****The Department of Natural Resources erroneously recorded expenditures in the Wildlife Restoration Federal Program (CFDA 15.611).**

The department charged \$28,535 of expenditures to the Wildlife Restoration Program (CFDA 15.611) that should have been charged to the Fish and Wildlife Management Assistance Program (CFDA 15.608), a non-major federal program administered by the department. Department staff assigned the wrong reporting category to the expenditures in the state's accounting system, resulting in the expenditures being charged to the wrong program.

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<sup>7</sup> U.S. Office of Management and Budget Circular A-133, Part 3 – Compliance Requirements.

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*Recommendations*

- *The department should ensure that it records expenditures to the correct CFDA numbers in the state's accounting system.*
  - *The department should restore \$28,535 to the Fish and Wildlife Management Assistance Program from the Wildlife Restoration Program.*
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# Minnesota Department of Natural Resources

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Office of the Commissioner

651-259-5555



March 13, 2009

James Nobles, Legislative Auditor  
Office of the Legislative Auditor  
658 Cedar Street  
St. Paul, Minnesota 55155

Dear Mr. Nobles:

Thank you for the opportunity to respond to the findings of the single audit work on selected federal programs awarded of the Department of Natural Resources for the year ended June 30, 2008.

**Audit Finding 1: The Department of Natural Resources did not identify, analyze, and document their internal controls over compliance with the federal single audit requirements.**

***Audit Recommendation:***

- ***The department should regularly review and clearly document its risks, control activities, and internal control monitoring functions for federal program requirements.***

**Partially Resolved.** The Department of Natural Resources (DNR) accepts the finding that the department did not identify, analyze, and document its internal controls over compliance with the federal single audit requirements.

An entity-wide risk assessment was completed in January 2009. A grants review project was initiated to strengthen controls over state and federal grant programs. The grant review project incorporates 11 of 13 grant policies recently released by the Minnesota Department of Administration (MDOA). The grant policies released by MDOA provide a comprehensive guide to state agencies in administering state and federal grants. The remaining two policies, pertaining to grant closeouts and grant payments, have not been released by MDOA. Further actions to strengthen controls will be taken by the department after receiving guidance on the two remaining grant policies.

In an effort to provide more internal control and monitoring of DNR federal program expenditures and requirements, the department has developed a Federal Fiscal Monitoring procedure, which will be in effect for all Department of Natural Resources Federal Programs beginning April 2009.

This procedure will clarify oversight responsibilities of the department Federal Fiscal Aid Coordinator. These responsibilities include:

1. Periodic review of drawdown requests for accuracy of calculations; reporting of land and equipment purchase, and indirect costs; availability and accuracy of supporting documentation; accurate use of reporting categories; and eligibility of expenditures.
2. Review of Financial Status Reports (FSR) for status of expenditures vs. federal award and state budget, accuracy of calculations, and appropriateness of expenditures.
3. Review of CFDA numbers and relations to reporting categories.
4. Review of incoming grant application database for identification of new grants.

The Federal Aid Coordinator in the Office of Management and Budget Services will be responsible for ensuring the procedure is followed.

**Audit Finding 2: The Department of Natural Resources did not maintain sufficient documentation for some of its federal reimbursement requests for the Sport Fish Restoration Program (CFDA 15.605) and the Wildlife Restoration Program (CFDA 15.611).**

***Audit Recommendation:***

- ***The department should retain sufficient documentation to support each federal reimbursement request.***

**Resolved.** The DNR agrees with the finding that sufficient documentation is needed to support federal reimbursement requests. The department is:

1. Following the procedure for federal drawdowns by requiring that a new spreadsheet be created for each drawdown request. Applying this process assures documentation is archived for each specific drawdown request.

The Accounting Director in the Division of Fish and Wildlife is responsible for the revision of the procedure and files. The spreadsheet has been updated and is being used for drawdown requests.

2. Requiring that program income deductions be included in the summary sheet of the electronic spreadsheet along with supporting documentation.
3. Copying drawdown requests and the supporting spreadsheets to the Federal Aid Coordinator in the Office and Management and Budget Services. They will be reviewed as outlined in the Federal Fiscal Monitoring procedure referred to in Audit Finding 1.

**Audit Finding 3: The Department of Natural Resources received reimbursement from the federal government for unallowable costs for the Wildlife Restoration Program (CFDA 15.611).**

***Audit Recommendations:***

- *The department should have an independent verification of the federal reimbursement requests to ensure that the requests are for only allowable costs and are calculated accurately.*
- *The department should work with the federal government for solutions to the questioned cost of \$2,519.*

**Resolved.** The DNR agrees with the finding that the department received reimbursement from the federal government for unallowable costs for the Wildlife Restoration Program.

The department has:

1. Developed a Federal Fiscal Monitoring procedure (identified in Audit Finding 1) to provide an independent verification of federal reimbursement requests.
2. Sent the revised Financial Status Report for this program to the U.S. Fish and Wildlife Service on March 10, 2009. This revision will eliminate the questioned costs of \$2,519.

**Audit Finding 4: The Department of Natural Resources overdrew federal funds on one grant and underdrew federal funds on another grant because it did not accurately report income for grants within the Sport Fish Restoration (CFDA 15.605) and the Wildlife Restoration (CFDA 15.611) programs.**

***Audit Recommendations:***

- *The department should correct its final financial status reports for the two grants that is inaccurately reported program income. It should work with the federal government on solutions for the questioned cost of \$14,013 for the first grant and determine whether the federal government will reimburse the state for \$458 for the second grant.*
- *The department should correctly determine and record program income in accordance with program requirements.*

**Partially Resolved.** The DNR agrees with the finding that the department did not accurately report program income for grants within the Sport Fish and Wildlife Restoration programs.

This finding is the result of errors in calculations that occurred during a period of staff turnover. The department has done the following to resolve this issue:

1. Revised the Financial Status Reports (FSR) for these programs. The revised FSR was sent to the U.S. Fish and Wildlife Service on March 10, 2009, and will eliminate the questioned costs of \$458.00.

The Financial Status Report for the Wildlife Restoration program has been adjusted to show a decrease in excess allowable costs of \$14,013 and an increase in reported program income of the same amount. This Financial Status Report will be sent to the U.S. Fish and Wildlife Service by April 1, 2009, and will eliminate the questioned costs of \$14,013.

2. Proposed a procedure that will verify program income numbers with project leaders on a regular basis. The division of Fish and Wildlife will ensure their procedures manual includes procedures on how to calculate and report program income.

The new procedure will include adding program income deductions to federal draw requests, and will provide documentation to support the deductions.

The Accounting Director of the Fish and Wildlife Division will be responsible for updating the procedures manual. This will be completed prior to the start of fiscal year 2010.

3. Implemented new Federal Fiscal Monitoring procedures identified in Audit Finding 1 to verify correct reporting of program income.

**Audit Finding 5: The Department of Natural Resources did not comply with federal suspension and debarment requirements.**

***Audit Recommendation:***

- ***The department needs to ensure compliance with federal requirements by verifying suspension and debarment for all federally funded purchases***

**Partially Resolved.** The DNR agrees with the finding that the department did not comply with federal suspension and debarment requirements.

To resolve the issue the division of Fish and Wildlife will provide training to DJ/PR project managers in the use of the suspension and debarment list, and the Office of Management and Budget Services will offer a segment on this policy in procurement training program offered annually.

In addition, the department has developed a new sub-grant contract template for the DJ/PR program that references the requirement to use the suspension and debarment list when contracting. This template will go through a review process and be ready for use prior to the beginning of fiscal year 2010. Jeanne Daniels will be responsible for ensuring that this contract is used in the DJ/PR program. Kim Montgomery will be responsible for ensuring this statement is in other sub-grant contracts.

**Audit Finding 6: The Department of Natural Resources erroneously recorded expenditures in the Wildlife Restoration Federal Program (CFDA 15.611).**

***Audit Recommendations:***

- *The department should ensure that it records expenditures to the correct CFDA numbers in the state's accounting system.*
- *The department should restore \$28,535 to the Fish and Wildlife Management Assistance Program from the Wildlife Restoration Program.*

**Partially Resolved.** The DNR agrees with the finding that expenditures were erroneously recorded to the Wildlife Restoration Program. This error occurred as a result of a new CFDA number being assigned by the federal government to a program that was already in existence.

To address this finding the Office of Management and Budget Services will:

1. Add the review of CFDA numbers and their corresponding reporting categories to the annual spending plan review process.
2. Work with Minnesota Management and Budget to determine how best to correct the reporting of \$28,535.
3. Follow the new Federal Fiscal Monitoring procedure identified in Audit Finding 1 to verify accuracy of CFDA numbers used.

André Prahll will be responsible for following up on these resolutions by the beginning of fiscal year 2010.

Again, thank you for the opportunity to respond to your audit findings and recommendations. We appreciate the professional and helpful manner of the staff from your office. Audits such as these continue to improve our policies and procedures, and ultimately improve our accountability.

Sincerely,



Mark Holsten, Commissioner  
MN Department of Natural Resources