A Report
to the
Montana
Legislature

Financial-Compliance Audit

Department of Natural Resources and Conservation

For the Two Fiscal Years Ended June 30, 2010

October 2010

Legislative Audit
Division

10-17

Financial-Compliance Audits

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October 2010

The Legislative Audit Committee
of the Montana State Legislature:

This is our financial-compliance audit report on the Department of Natural Resources and Conservation for the two fiscal years ending June 30, 2010. The report contains an unqualified opinion on the department's financial schedules. Included in this report are eleven recommendations primarily related to trust land administration, internal controls, and compliance with state law. The report also includes a disclosure issue related to a Board of Land Commissioners resolution.

The department's written response to the audit recommendations is included in the audit report at page B-1. We thank the director and her staff for their cooperation and assistance throughout the audit.

Respectfully submitted,

/s/ Tori Hunthausen

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	Joe Lamson, Deputy Director
	Tricia Schiltz, Centralized Services Division Administrator
	Ray Beck, Conservation and Resource Development Division Administrator
	Bob Harrington, Forestry Division Administrator
	Tom Richmond, Oil and Gas Conservation Division Administrator
	Bill Schultz, Reserved Water Rights Compact Commission Administrator
	Tom Schultz, Trust Land Management Division Administrator and Interim Water Resources Division Administrator
	Candace F. West, Chief Legal Counsel
State Board of Land Commissioners	Brian Schweitzer, Governor
	Monica Lindeen, State Auditor
	Linda McCulloch, Secretary of State
	Denise Juneau, Superintendent of Public Instruction
	Steve Bullock, Attorney General
Administratively Attached Boards, Commissions & Committees	Board of Water Well Contractors Board of Oil and Gas Conservation Reserved Water Rights Compact Commission Rangeland Resources Committee Drought Advisory Committee Resource Conservation Advisory Council Montana Grass Conservation Commission Flathead Basin Commission

Montana Legislative Audit Division

Financial-Compliance

Department of Natural Resources and Conservation

For the Two Fiscal Years Ended June 30, 2010

October 2010 10-17 Report Summary

The Department of Natural Resources and Conservation (DNRC) manages trust lands totaling over 5.1 million surface acres, 6.2 million mineral acres, and 6,000 miles of navigable waterways. DNRC establishes statewide forestry programs and provides wildfire suppression on over 50 million acres of state and private property; manages several loan and grant programs for local communities, local governments, state agencies and private citizens; issues drilling permits and classifies and inspects wells for the state's oil and gas programs; and manages and maintains the state-owned dams, reservoirs, and canals.

Context

DNRC categorizes its expenditures in seven expenditure programs, the largest of which (Trust Funds) reflects the transfer of trust earnings to the beneficiaries of the twelve land trusts administered by the department. Total revenues earned by the trusts exceed $120 million annually.

Fire costs in the past four years have ranged from $5.9 million to $81.5 million.

Loan programs include State Revolving Fund program loans to communities for water and waste water systems, Coal Severance Tax loans to governmental entities, and loans to private entities for water development projects. Loans outstanding exceed $297 million at June 30, 2010.

The department is authorized to employ approximately 575 full time staff in Helena and at locations around the state.

Results

Areas for improvement discussed in the report are related to three main topics: Trust Lands Administration, Fire Expenditures, and compliance with state laws.

Regarding Trust Lands Administration, we identified instances where the state land trusts and trust beneficiaries have not been properly compensated for use of trust lands, including three state parks currently occupying state trust lands and cabin site lease rates that do not achieve fair market value. The report also discusses identification of administrative costs incurred on behalf of each trust through fiscal year 2008-09.

Weaknesses in DNRC's internal controls over fire expenditures, including documentation of fiscal year-end fire estimates and proper authorization for fire expenditures, are outlined in the report. In addition, the department's practice of paying for meals for employees assigned to fires at rates in excess of those allowed under state law is also discussed.

We noted instances where the department did not review, prepare, or submit reports for two programs.

The audit report also includes a disclosure issue related to a State Board of Land Commissioners resolution to use settlement funds to purchase additional state land, which is not authorized by the Montana Constitution or state law.

Recommendation Concurrence	
Concur	7
Partially Concur	2
Do Not Concur	2

Source: Agency audit response included in final report.

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Chapter I – Introduction

Introduction

We performed a financial-compliance audit of the Montana Department of Natural Resources and Conservation (department) for the two fiscal years ended June 30, 2010.

The objectives of this audit were to:

1. Determine whether the department complied with selected state and federal laws and regulations.
2. Obtain an understanding of the department's control systems to the extent necessary to support our audit of the department's financial schedules, and if appropriate, make recommendations for improvement in management and internal controls of the department.
3. Determine whether the department's financial schedules present fairly the results of operations for the two fiscal years ended June 30, 2010.
4. Determine the status of prior audit recommendations.

Auditing standards require us to communicate, in writing, control deficiencies we identified as a result of audit objective #2 above and considered to be significant or material. A control deficiency exists when the design or operation of a control does not allow management or employees to prevent or detect misstatements on a timely basis. A significant deficiency is one or more control deficiencies that affects management's ability to accurately process transactions. A material weakness is one or more significant deficiencies that adversely affect management's ability to fairly present its financial schedules.

Table 1 below outlines the status of significant deficiencies and material weaknesses we identified during this audit.

Table 1
Summary of Control Deficiencies

Subject	Significant Deficiency	Material Weakness	Page
Fire Expenditures	Yes	No	14

This report contains eleven recommendations to the department and one disclosure issue. Other concerns not having a significant effect on the successful operations of the department are not specifically included in this report but have been discussed with management.

In accordance with §5-13-307, MCA, we analyzed and disclosed the cost, if significant, of implementing the recommendations made in this report.

We evaluated charges for services in the Internal Service Fund as required by §17-8-101(6), MCA. We found the charges and fund equity reasonable for the operations in the fund in fiscal years 2009-10 and 2008-09.

Background Information

The Executive Reorganization Act of 1971 established a department to manage the state's natural resources. In 1995, the reorganization of Montana's natural resources and environmental agencies created the current Department of Natural Resources and Conservation. The department promotes the stewardship of Montana's water, soil, forest, and rangeland resources, manages state-owned land, facilitates funding for certain infrastructure improvement projects, and regulates forest practices and oil and gas exploration and production.

Department Organization

The State Board of Land Commissioners, comprised of the Governor, State Auditor, Attorney General, Superintendent of Public Instruction, and Secretary of State, exercises the general authority, direction, and control over the care, management, and disposition of state lands under its administration. The Department of Natural Resources and Conservation director is the chief administrative officer of the board.

The Reserved Water Rights Compact Commission is attached to the department for administrative purposes. The Reserved Water Rights Compact Commission, budgeted for 5 full-time equivalent (FTE) positions, was created by the legislature in 1979 as part of the water rights adjudication effort. The commission negotiates water rights with Indian tribes and federal agencies claiming federal reserved water rights within the state in order to establish a formal agreement or compact on the amount of water to be allocated to each interest.

The department's divisions are described below:

Centralized Services Division (41.5 FTE) provides management and administrative support services to the department through the Director's Office and Support Services. The Director's Office includes the director, legal staff, and public information personnel. Support Services includes fiscal affairs, data processing, personnel, reception, and mail. The division manages all financial activities, coordinates information systems and procurement, produces publications and graphic materials, and performs general administrative support services. Other responsibilities include trust revenue collection

and distribution, and maintenance of ownership records for trust and nontrust state-owned land.

Oil and Gas Conservation Division (21.5 FTE) administers the Montana oil and gas conservation laws. It promotes conservation and prevents waste in the recovery of oil and gas resources through regulation of exploration and production. The division issues drilling permits; classifies wells; establishes well spacing units and pooling orders; inspects drilling, production, and seismic operations; investigates complaints; and does engineering studies. The division also determines incremental production for enhanced recovery and horizontal wells in order to implement the tax incentive program for those projects, operates the underground injection control program, plugs orphan wells, and collects and maintains complete well data and production information. The division provides administrative support to the Board of Oil and Gas Conservation.

Conservation and Resource Development Division (25.5 FTE) assists local entities in managing the state's natural resources and provides financing for conservation resource management and reclamation activities. The division provides technical, administrative, financial and legal assistance to Montana's 58 conservation districts. The division also manages several loan and grant programs for local communities, local governments, state agencies and private citizens. The programs include State Revolving Fund loans to communities for water and waste water systems, Coal Severance Tax loans to governmental entities, and loans to private entities for water development projects. Loans outstanding exceed $297 million at June 30, 2010. Grant programs administered by the division include the Reclamation Development, Renewable Resource, and Conservation District grant programs.

Water Resources Division (156.25 FTE) is responsible for programs associated with the use, development, and protection of Montana's water. It manages and maintains state-owned dams, reservoirs, and canals. The division develops and recommends intrastate, interstate, and international water policy to the director, governor, and legislature. The division also resolves water resource use conflicts, investigates water use violations, ensures dam safety compliance, and provides water adjudication support to the Water Court. The division consists of an administration unit and five bureaus: Water Adjudication Bureau, Water Management Bureau, Water Rights Bureau, Water Projects Bureau, and the Water Operations Bureau. The 2003 Legislature attached the Flathead Basin Commission to the department for administrative purposes. The commission is charged with protecting the natural resources and environment of the Flathead Basin.

Forestry Division (193.19 FTE) is responsible for planning and implementing forestry programs statewide. The division protects Montana's natural resources from

wildfire, regulates forest practices, and provides a variety of services to private forest landowners. The Fire and Aviation Management Program protects 50 million acres of state and private forest and watershed lands from wildfire through a combination of direct protection and county support. Total fire suppression costs have ranged from $5.9 million to $81.5 million over the past four years. The Forest Practice Regulation program enforces Montana's streamside management zone regulations and monitors the voluntary best management practices program on all forests in Montana. In administering Montana's Fire Hazard Reduction Law, the division helps ensure fire hazards created by logging and other forest management operations on private forestlands are adequately reduced, or that additional fire protection is provided until the hazard is reduced. The division provides technical forestry assistance to private landowners, businesses and communities.

Trust Land Management Division (139.90 FTE) provides for the administration and management of trust lands granted to the state of Montana by the Enabling Act of 1889. In the process of producing revenue for trust beneficiaries, the division considers environmental factors and protects the future income-generating capacity of the trust lands. These lands currently total over 5.1 million surface acres and 6.2 million mineral acres. Additionally, the division is responsible for the administration of approximately 6,000 miles of the beds of navigable waterways. The Trust Land Management Division is divided into four primary programs: forest management, agriculture and grazing management, real estate management and minerals management.

Prior Audit Recommendations

We performed the prior audit of the department for the two fiscal years ended June 30, 2008. The report contained 17 recommendations and two disclosure issues. The department implemented 12, partially implemented two, and did not implement three of the recommendations.

The recommendations partially implemented relate to administrative costs allocated to the various trusts administered by the department and documentation of internal controls over the fiscal year-end fire accrual process. These areas are discussed beginning on pages 9 and 15, respectively. The recommendations not implemented relate to an easement agreement, meal reimbursement rates, and accounting for donated property, and are discussed on pages 5, 12, and 15, respectively.

Chapter II – Findings and Recommendations

Trust Lands Administration

The Department of Natural Resources and Conservation (department) administers twelve separate land trusts. Of these, nine were established in the federal Enabling and Morrill Acts and Article X of the Constitution of the State of Montana (constitution). The legislature began using trust revenues to finance the cost of administering these trusts in 1963. From 1963 to 2003, the legislature established seven separate funding sources to pay for various types of administration costs. These include the Forest Improvement, Resource Development, Recreational Use, Timber Sale, Trust Land Administration and Commercial Leasing Accounts, and the State Land Bank Fund. Currently, land trust administration costs are recovered through charges against revenues.

Under Montana law, the department has a duty of complete loyalty to each individual trust, solely in the interest of that trust's beneficiaries. Trust beneficiaries include Montana's public schools and universities, and other entities such as the State Reform School, Montana School for the Deaf and Blind, and the Montana Development Center. Section 72-34-110, MCA, requires the trustee to keep trust property separate from other property not subject to the trust and to see that trust property is so designated. Article X, Section 3, of the constitution guarantees the public school fund against loss or diversion. The same guarantee exists for the university funds in Article X, Section 10 of the constitution. In addition, Article X, Section 11 of the constitution requires all public land trusts be disposed of for the purposes for which they were granted.

The following sections discuss instances where the department violated the trust agreements, its trust duty, and state law.

State Parks on Trust Lands

Trusts are not compensated for use of lands for state parks purposes.

The department entered into an agreement with the Department of Fish, Wildlife and Parks to sell a permanent easement on Common School trust land, which was purchased in October 2006 using proceeds from a previous land sale. Under the agreement, the Department of Fish, Wildlife and Parks must pay a specified amount per year for up to five years, at which time the right to purchase the easement expires. Should the easement be fully executed, any payments made during the five year period will be credited to the purchase of the easement. The last payment received by the department was in August 2008. However, the Department of Fish, Wildlife and

Parks continues to occupy the land and utilizes it as part of First Peoples Buffalo Jump State Park.

If the agreement is executed as written, the Common School trust will not be fully compensated for the use of trust land because crediting these payments towards the purchase of the easement does not provide any income to the trust or trust beneficiaries over a period of up to five years.

Our last audit report recommended the department maximize trust revenues as required by their fiduciary duty to the Common School trust by leasing this property to the fullest extent possible, and by ensuring fair market value is reflected in the final easement transaction with the Department of Fish, Wildlife and Parks. By allowing the land to remain under the Department of Fish, Wildlife and Parks control without receiving payment, the lost revenues for the Common School trust continue to grow.

Department personnel indicated the land is currently being re-surveyed, which has resulted in a delay in finalization of the easement agreement. Department personnel also indicated the Department of Fish, Wildlife and Parks would be credited for payments made through August 2008 totaling $23,408, which the department recorded to the Common School trust corpus.

During the audit, we reviewed information in the department's Trust Land Management System for all trust lands within 20 feet of the borders of Montana's state parks. We identified two additional state parks that include state trust lands for which the trusts are not properly compensated.

- **Madison Buffalo Jump State Park** – was acquired in 1966 through land exchanges involving Common School and Montana Tech trust lands. These land exchanges were executed with two private Montana citizens. To finalize one agreement, the then Fish and Game Department entered into a 10-year grazing lease for the former land owner's use of park land, the revenue from which was retained by the Fish and Game Department. Since 1966, the Common School and Montana Tech trusts have not been compensated for the use of trust land as part of Madison Buffalo Jump State Park.
- **Lewis & Clark Caverns State Park** – boundaries originally included Common School trust land, which was exchanged with Jefferson County in 1937. When the land exchange was ruled contrary to the constitution in 1947, the original land transactions were reversed by executing two quitclaim deeds. However, the quitclaim deed giving the original land back to the state included a restriction that the land only be used by the state for park or recreational purposes. Because Jefferson County did not have a valid interest in the land, the county did not have the authority to create a restriction on the land use. The Common School trust was not compensated for the restricted use of its land, and since acquisition, the trust has not received compensation for use of the land as part of Lewis & Clark Caverns State Park.

In each situation, there was significant interest in acquiring specific land for preservation and parks purposes. Documentation we reviewed suggests trust interests were not considered when the transactions took place. Because the lands are currently under the control of the Department of Fish, Wildlife and Parks, resolution requires the participation and cooperation of both departments.

Had the department entered into permanent easements for the use of surface area for the Madison Buffalo Jump and Lewis & Clark Caverns state parks, we estimate the loss to the trusts ranges from $7,150 to $14,100. Grazing leases provide another method to estimate the losses to the trusts. Grazing leases on sections of state trust lands near Madison Buffalo Jump State Park and Lewis & Clark Caverns State Park have earned approximately $17,800 and $10,470, respectively, for the most recent 20-year period. If easements for the use of these trust lands are completed in the future, the agreements should reflect current fair market value for the land.

RECOMMENDATION #1

We recommend the department:

A. *Maximize trust revenues for land utilized by First Peoples Buffalo Jump State Park.*

B. *Ensure fair market value is reflected in the final easement transaction for land utilized by First Peoples Buffalo Jump State Park.*

C. *Quantify and seek full compensation on behalf of the Common School and Montana Tech trust funds for historical use of trust lands for Madison Buffalo Jump State Park and Lewis & Clark Caverns State Park.*

D. *Enter into agreements necessary to ensure proper and full compensation to the Common School and Montana Tech trust funds in the future.*

Cabin Site Leases

Trusts are not being compensated to the fullest extent, as required by state law and the Montana constitution.

State trust lands generate revenue for the trust beneficiaries in a variety of ways, one of which is cabin site leases. For cabin site leases, the department enters into a contract to lease the surface area of the land, allowing the lessee to build a residence on the property. The state maintains ownership of the land, but the lessee owns the land improvements. Cabin site leases are generally for a 15-year period, and the lease rate is reviewed and updated at the end of each five-year period. In any given year, the department renews or revises the leases for about 20 percent of its cabin sites.

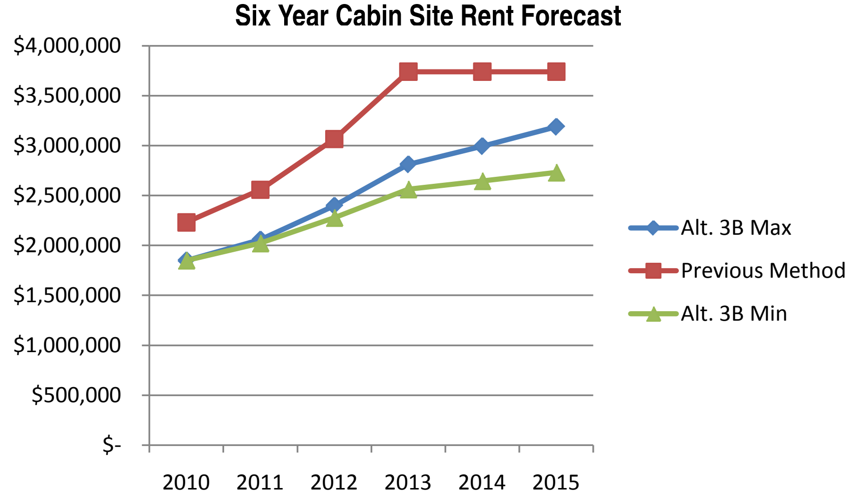
In accordance with state law, every six years the Department of Revenue assigns a current value to the land. Section 77-1-208, MCA, includes a requirement that the Board of Land Commissioners (board) to achieve full market value for the cabin sites based on appraisal conducted by the Department of Revenue.

Prior to 2009, the board defined full market value for cabin site leases as five percent of the most recent appraisal conducted by the Department of Revenue. In 2009, the Department of Revenue appraisals were substantially higher, in most cases, than in previous years, which led to lessee complaints over the lease rate increases. In response to these concerns, the department studied cabin site values and proposed alternative lease rate methods to the board. In May 2010, the department recommended and the board adopted an alternative lease rate methodology called Alternative 3B. As a result, lease holders may choose either the 2009 Department of Revenue appraised value or the property value calculated under Alternative 3B as the basis for the five percent annual lease payment.

Under Alternative 3B, the department increases the 2003 Department of Revenue appraised value by 6.53 percent annually through 2009, which becomes the base property value. For each subsequent year the base property value is increased between 3.25 and 6.5 percent, depending on the average of appreciation in cabin site appraisals over a period of time, including the 2009 values, and the annual consumer price index.

The department provided the following projection of annual lease payments under the various methodologies:

Figure 1
Six Year Cabin Site Rent Forecast



Source: Compiled by Department of Natural Resources and Conservation.

Leases due for renewal or revisions in lease values in calendar year 2009 continued to be based on the 2003 appraised value while the department conducted its study. These leases, as well as leases due for renewal or revision in calendar year 2010 have been given the option to use Alternative 3B to reduce their annual lease payments.

Because Alternative 3B uses property values lower than the 2009 appraised values, and property values calculated under Alternative 3B will not reach the 2009 appraised value, by the time the next Department of Revenue appraisal is conducted, the annual lease revenues earned by trust beneficiaries are permanently reduced. By adopting Alternative 3B, the board is not maximizing revenues to the trusts, as required by state law.

Recommendation #2

We recommend the department provide the Board of Land Commissioners with cabin site lease methodologies that will maximize trust revenues, as required by state law.

Trust Administration Costs

The department did not compensate the trusts for amounts inappropriately withheld from various trusts and their beneficiaries, and continued to record inappropriate administrative costs to trust accounts in fiscal year 2008-09.

Under Montana law, the department has a duty of complete loyalty to each trust, solely in the interest of that trust's beneficiaries. In a letter dated September 13, 2005, the Attorney General indicated that in the absence of a specific restriction, the department, as trustee, has a right to reimbursement for expenses incurred in administering each trust. Administrative costs are required to be reasonable, incurred in perpetuating the purpose of that trust, and not for other unrelated purposes.

Table 2
Administrative Cost Over-Allocations
For FY 2006-07 and FY 2007-08

	Total
Common School	996,704
State Reform School	14,453
School for the Deaf & Blind	402,673
MSU- Morrill	3,321
MSU - 2nd Grant	125,803
Total	**1,542,954**

Source: Compiled by the Legislative Audit Division.

Prior to fiscal year 2009-10, administrative costs were charged or allocated to trust lands based on trust revenues, a practice established through department policy. Various administration account costs were charged or allocated to the trusts, as described in our financial-compliance audit (08-17) of the department. Our prior audit report quantified overcharges to the trust accounts, as summarized by Table 2.

At our request, the department performed a comparison of administrative costs charged to each trust versus costs incurred for the benefit of each trust for fiscal year 2008-09. Table 3 summarizes the department's analysis.

Table 3
Comparison of Administrative Cost Allocations
For FY 2008-09

Trust	Amount Charged Based on 2009 State Laws	Analysis Using New Methodology	Difference
Common School	$8,208,234	$7,655,446	$552,788
University of Montana	3,676	19,401	(15,725)
Montana Tech	27,013	407,191	(380,178)
State Normal School	12,043	109,772	(97,729)
State Reform School	8,767	148,093	(139,326)
School for the Deaf & Blind	350,088	162,782	187,306
MSU - 2nd Grant	95,323	216,496	(121,173)
MSU-Morrill	22,677	182,133	(159,456)
Veterans Home	289	72	217
Capitol Building	816,772	643,681	173,091
Sir Estate	243	58	185
Total	**$9,545,125**	**$9,545,125**	**$ -**

Source: Department of Natural Resources and Conservation records.

The analysis indicates the Common School, Montana School for the Deaf and Blind, Veterans Home, Capitol Building, and Sir Estate trusts were each overcharged for administrative costs. Total over charges were $913,587 for fiscal year 2008-09. An analysis of costs incurred on behalf of each trust prior to fiscal year 2006-07 has not been conducted. However, the department should also quantify and compensate the trusts for amounts inappropriately withheld from trust revenues and trust beneficiaries for fiscal years ending prior to June 30, 2007.

According to department personnel, they made no change in the methods administrative costs were allocated to the trust accounts for fiscal year 2008-09 because by doing so the department would violate state law in effect at that time. However, the department did not consider alternatives available to them, such as paying the costs from existing appropriation authority not funded by assessments to the trusts.

In legislation passed during the 2009 Legislative Session, effective as of July 1, 2009, the department addressed several prior audit recommendations regarding trust

administrative costs. We analyzed the process used for fiscal year 2009-10, and determined the department has properly accounted for administrative costs by trust.

RECOMMENDATION #3

We recommend the department compensate the trusts for the $2,456,541 inappropriately withheld from Common School, State Reform School, MSU-Morrill, MSU-second grant, Montana School for the Deaf and Blind, Veterans Home, Capitol Building, and Sir Estate trust revenues and their beneficiaries.

Consistency in Revenue Recognition

The department did not consistently account for activity related to a court ordered settlement.

In June 2008, courts ordered a company to pay approximately $41 million to the state for a portion of the revenue generated from the use of riverbeds. The department addressed a prior audit recommendation to record the $41 million receivable on the state's accounting records. The decision has been appealed to the U.S. Supreme Court. Until payment is received or the court decisions are overturned, state law specifies simple interest of ten percent per year is also payable to the department.

State accounting policy specifies revenue should be recorded in the period when earned, so long as payment is anticipated within 60 days of fiscal year-end. If payment is expected to be delayed, the revenue should be deferred in the ledger that supports the department's financial schedules.

For fiscal year 2008-09, the department did not consider and did not record interest accrued on the settlement amount. For fiscal year 2009-10, the department calculated and recorded $8,550,303 in interest on the settlement. At the time the transactions were recorded, the department believed payment ordered in the court decision, plus interest, would be received within 60 days of fiscal year-end, and recorded the interest as revenue. However, the department did not consider the $41 million settlement recorded as deferred revenue in a previous fiscal year, which resulted in inconsistent revenue recognition related to the court decision.

Recommendation #4

We recommend the department apply consistent treatment in recording revenue and deferred revenue transactions related to the court decision.

Meal Allowance Rates

The department adopted new meal allowance policy contrary to state law.

Section 2-18-501, MCA, in part, specifies employees are authorized allowances for meals while the employee is conducting state business away from the employee's designated headquarters. The statute also specifies monetary amounts for each breakfast, lunch, and dinner. Section 2-18-502, MCA, further defines an employee's travel status and clarifies time periods that an employee qualifies for meal allowances.

Two of our past three audit reports (08-17 and 04-17) of the department have included recommendations related to meal rates paid for employees in travel status due to fire activities. As previously reported, meals for department employees assigned to fire activities are generally provided by a fire camp or field kitchen, or are served via sack lunch on the fire line. However, employees directly involved in the suppression of an ongoing fire or employees who are readied for anticipated fires are entitled to meals even when meals are not provided through those methods.

During the current audit period, the department modified their fire meal policy, specifically including meal rates in excess of those amounts allowed by state law. The department cited §76-13-104(2)(a), MCA, which directs the department to adopt rules to protect the state's natural resources from destruction by fire and allows the department to incur other expenses during declared emergencies, as authority for the increased meal reimbursement rates. This section of state law is specific to declared emergency situations. During the past two fiscal years, there were 706 fire incidents, none of which were declared emergencies.

The department cannot adopt rules to override the provisions of law, and does not have authority to increase meal rates for general fire activities.

Recommendation #5

We recommend the department:

A. *Revise its fire meal policy to reflect rates specified in state law.*

B. *Ensure meal costs are paid at rates allowed by state law for employees in travel status.*

Policy Documentation

Department policies do not address employee travel and fitness costs.

The state's purchasing card program provides state employees with a method of paying for and managing purchases for state business. To obtain a purchasing card, a department employee must read the purchasing card users' manual, and then submit a completed application to their supervisor for approval.

The department's purchasing card users' manual specifies compliance with departmental procurement and expenditures policies as a responsibility of the cardholder. The purchasing card users' manual also prohibits splitting charges in order to avoid exceeding the card's individual transaction limit.

During the audit, we reviewed 51 charges from various cardholders, and identified the following two instances where department employees did not comply with cardholder requirements.

- Two purchasing cards were used a total of three times to complete a $4,300 transaction to charter an aircraft to transport an employee from a fire assignment back to his home office. The limit on each purchasing card was $2,000 per transaction, or $5,000 per month. The department's policy and procedure manuals do not specifically address emergency employee travel.
- In January 2009, purchasing card was used by a land office employee to acquire exercise equipment for approximately $1,150. The equipment was used for fire fighter fitness. Department staff indicated fitness related expenses have been prohibited under past practices of the department; however, fitness costs are not expressively prohibited in the department's various policy and procedures manuals. Staff also indicated they attempted to return the equipment, but were not successful in doing so.

After we discussed the exercise equipment with the department in June 2010, the department sold the equipment in July 2010.

Recommendation #6

We recommend the department incorporate emergency employee travel and fitness costs into the appropriate policy manual.

Fire Expenditures

The previous section discussed purchasing card transactions made by employees who circumvented established controls. When controls are not documented, as required by state accounting policy, or overlooked either inadvertently or intentionally, the department risks substantial improper expenditures activity. The next two sections discuss how the department's internal controls for fire expenditures can be improved.

Proper Authorization

The department paid fire expenditures that were not approved by authorized staff.

Centralized Services Division (CSD) maintains a list of staff authorized to approve expenditures for various department functions. In February 2008, CSD was notified that all expenditures for one land office were to be authorized by a single individual. Prior to that time, multiple staff within the office were authorized to approve payments. During the audit, we noted expenditures totaling $145,669 were paid without proper authorization. We determined all expenditures were valid and properly supported, but all were signed by an employee whose payment approval authorization had been revoked. We identified the following internal control errors:

- The land office's authorized approver did not sign the documents prior to submission to CSD.
- CSD did not utilize the authorization list when processing the documents for payment.
- CSD did not communicate to their accounting technicians that updates were made to the authorization list.

Prior audits of the department have reported payments made despite the lack of necessary supporting documentation, including proper authorization.

Recommendation #7

We recommend the department enhance internal controls to ensure costs submitted for payment are properly authorized.

Year-End Accrual Procedures

The department has not documented the process to generate the fiscal year-end fire accrual.

The department estimates fire costs incurred at the end of each fiscal year and records transactions on the state's accounting records. This estimate includes allocating state and federal shares of fire costs. Between fiscal years 2006-07 and 2009-10, the federal share of fire costs has ranged from approximately $370,000 to over $29 million. The department has not documented the process to generate this accrual transaction, as recommended in our prior audit.

Recommendation #8

We recommend the department document the process used to calculate and record the fiscal year-end fire accrual.

Recording Donated Assets

The federal Department of Defense donates certain equipment to various state and local governments. The federal government asks receiving entities to track equipment at the original acquisition cost. However, at the time the equipment is provided to other governmental entities, the fair value of the equipment is considerably less than the acquisition amount. State accounting policy requires gifts and donations be recorded at their fair value at the time of receipt. For fiscal year 2009-10, we identified equipment on the accounting records that was overvalued by $257,208.

Our last audit reported the department had recorded donated equipment at its acquisition cost rather than fair market value, which resulted in overvalued equipment on the state's accounting records. Our current audit did not identify internal controls that would prevent the types of errors identified by the previous audit.

Recommendation #9

We recommend the department establish and document procedures to ensure property donated from the federal Department of Defense is recorded in accordance with state law and policy.

State Compliance

The following two sections discuss how the department can enhance compliance with state law.

Fire Protection Tax Assessment

The department did not prepare required reports or submit required certifications regarding the fire protection tax assessment.

Section 76-13-207, MCA, in part, requires the department prepare an annual operation assessment plan to determine fire costs, and to assess a certain portion of the cost to land owners for the cost of wildland fire protection. This section also requires the department to certify to the Department of Revenue, by the first Tuesday in September of each year, amounts due from land owners.

During the audit, the department indicated they had not prepared an annual operation assessment plan for presentation to the legislature since 2006. Instead, the department uses base budget information, and presents additional details regarding new funding sources.

We also noted the report to the Department of Revenue was submitted late in each fiscal year 2009 and 2008. The department pointed to untimely data received from the Department of Revenue, on which the certification is based, as the reason the September deadline was missed.

Recommendation #10

We recommend the department prepare the annual operation assessment plan to determine fire costs, and submit timely certification to the Department of Revenue, as required by state law.

Montana – Bureau of Land Management Water Rights Compact Report

The department has not submitted an annual report for the last five years.

Section 85-20-501, MCA, Article III G (2), requires the department to produce an annual report detailing its actions in administering the available water supply requirements specified in the Reserved Water Rights Compact with the federal Bureau of Land Management (BLM). The department indicated they have not submitted this report in the past five years, and are working towards a more automated process to accumulate the data necessary for the report. The department also represented contact with the BLM regarding the statues of the compact takes place on an annual basis.

Recommendation #11

We recommend the department submit the annual report for the Reserved Water Rights Compact as required by state law.

Chapter III – Disclosure Issues

Board of Land Commissioners Resolutions

The court decision discussed on page 11 was upheld by the Montana Supreme Court, except that the revenues belong to the public land trust rather than the public school trust.

Deposit and Use of Court Ordered Payment

In May 2010, the State Board of Land Commissioners (board) adopted a resolution to deposit the court ordered payment and related interest to the state special revenue fund, and to use the monies to acquire additional land to be held in trust for the support of education in the state's public schools. The board further declared that revenue generated from the use of newly acquired land would be deposited to the school facility and technology account. The resolution was based on the department's position that the court ordered payment is nonstate money which can be used at the discretion of the board in managing the public land trust to provide long-term support for education. However, the board may purchase trust lands through the land banking program (Title 77, Chapter 2, Part 3, MCA) or when authorized by the legislature. Because neither of these methods apply to the court ordered payment, the board does not have the authority to purchase trust lands with money received as the result of the court decision. We make no recommendation at this time, but plan to follow-up after the U.S. Supreme Court decides whether to accept the appeal of the judgment.

Revenue Disposition

The board adopted another resolution in May 2010, directing the deposit of rents and other income from the use of riverbeds on navigable waterways in a manner consistent with Article X, Section 5 of the Montana Constitution, which specifies 95 percent of all rent received for the leasing of school lands be distributed in support of public schools with the remaining five percent vested in the corpus of the public school trust fund. Beginning in January 2012, state law directs power site rents be deposited in the school facility and technology account. Absent requirements outlined in state law, the board may have the authority to determine whether the court ordered payment and rents and other income generated from the use of riverbeds on navigable waterways are distributed to the beneficiaries of the public land trust, or held for investment on their behalf. This information is offered for disclosure purposes only, and we make no recommendation at this time.

Independent Auditor's Report and Department Financial Schedules

LEGISLATIVE AUDIT DIVISION

Tori Hunthausen, Legislative Auditor
Monica Huyg, Legal Counsel

Deputy Legislative Auditors
James Gillett
Angie Grove

Independent Auditor's Report

The Legislative Audit Committee
of the Montana State Legislature:

We have audited the accompanying Schedules of Changes in Fund Balances & Property Held in Trust, Schedules of Total Revenues & Transfers-In, and Schedules of Total Expenditures & Transfers-Out of the Department of Natural Resources and Conservation for each of the fiscal years ended June 30, 2010, and 2009. The information contained in these financial schedules is the responsibility of the department's management. Our responsibility is to express opinions on these financial schedules based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial schedules are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial schedules. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial schedule presentation. We believe that our audit provides a reasonable basis for our opinions.

As described in note 1, these financial schedules are prepared on the basis of Montana state accounting policy, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America. The schedules are not intended to be a complete presentation and disclosure of the department's assets, liabilities and cash flows.

In our opinion, the financial schedules referred to above present fairly, in all material respects, the results of operations and changes in fund balances and property held in trust of the Department of Natural Resources and Conservation for each of the fiscal years ended June 30, 2010, and 2009, in conformity with the basis of accounting described in note 1.

Respectfully submitted,

/s/ James Gillett

James Gillett, CPA
Deputy Legislative Auditor

September 2, 2010

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DEPARTMENT OF NATURAL RESOURCES AND CONSERVATION
SCHEDULE OF CHANGES IN FUND BALANCES & PROPERTY HELD IN TRUST
FOR THE FISCAL YEAR ENDED JUNE 30, 2010

	General Fund	State Special Revenue Fund	Federal Special Revenue Fund	Debt Service Fund	Enterprise Fund	Internal Service Fund	Agency Fund	Private Purpose Trust Fund	Permanent Fund
FUND BALANCE: July 1, 2009	$ (4,265,154)	$ 387,900,733	$ (6,567,579)	$ 25,030,336	$ (33,206)	$ 245,741	$ 0	$ 0	$ 447,471,363
PROPERTY HELD IN TRUST: July 1, 2009							$ 1,760,336		
ADDITIONS									
Budgeted Revenues & Transfers-In	142,176	219,349,027	19,734,001		643,516	1,817,292			
Nonbudgeted Revenues & Transfers-In	39,129	113,947,159	954	21,147,172	26	1,236		1,001,393	268,066,289
Prior Year Revenues & Transfers-In Adjustments	(14,674)	4,301,429	13,394	(13,854)					4,594,906
Direct Entries to Fund Balance	24,541,633	(124,445,813)	337,007	428,328	8,895				38,754
Additions to Property Held in Trust							2,964,664		
Total Additions	24,708,264	213,151,802	20,085,356	21,561,646	652,437	1,818,528	2,964,664	1,001,393	272,699,949
REDUCTIONS									
Budgeted Expenditures & Transfers-Out	22,225,762	44,930,232	14,738,145		729,580	1,922,484			
Nonbudgeted Expenditures & Transfers-Out	185	127,559,753	(16,759,772)	17,567,677	14,229	53,000			223,086,455
Prior Year Expenditures & Transfers-Out Adjustments	(21,263)	168,857	83,583	100,000					4,504,790
Reductions in Property Held in Trust							3,001,766		
Total Reductions	22,204,684	172,658,842	(1,938,044)	17,667,677	743,809	1,975,484	3,001,766	0	227,591,245
FUND BALANCE: June 30, 2010	$ (1,761,574)	$ 428,393,693	$ 15,455,821	$ 28,924,305	$ (124,578)	$ 88,785	$ 0	$ 1,001,393	$ 492,580,067
PROPERTY HELD IN TRUST: June 30, 2010							$ 1,723,234		

This schedule is prepared from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) without adjustment.
Additional information is provided in the notes to the financial schedules beginning on page A-9.

DEPARTMENT OF NATURAL RESOURCES AND CONSERVATION
SCHEDULE OF CHANGES IN FUND BALANCES & PROPERTY HELD IN TRUST
FOR THE FISCAL YEAR ENDED JUNE 30, 2009

	General Fund	State Special Revenue Fund	Federal Special Revenue Fund	Debt Service Fund	Enterprise Fund	Internal Service Fund	Agency Fund	Permanent Fund
FUND BALANCE: July 1, 2008	$ (10,319,537)	$ 386,886,824	$ (25,195,465)	$ 29,886,641	$ 26,304	$ 201,993	$ 0	$ 450,166,929
PROPERTY HELD IN TRUST: July 1, 2008							$ 2,013,219	
ADDITIONS								
Budgeted Revenues & Transfers-In	201,554	126,995,388	28,238,715		506,968	1,873,236		
Nonbudgeted Revenues & Transfers-In	664,852	64,748,322	10,259	26,490,488	33	880		123,260,526
Prior Year Revenues & Transfers-In Adjustments	2,386	513,441	(6,816,090)	164,634	10,530	(2,626)		1,459,428
Direct Entries to Fund Balance	27,210,988	(52,865,748)	8,028,768	455,318				(422,019)
Additions to Property Held in Trust							2,666,891	
Total Additions	28,079,780	139,391,403	29,461,652	27,110,440	517,531	1,871,490	2,666,891	124,297,935
REDUCTIONS								
Budgeted Expenditures & Transfers-Out	22,131,223	48,804,068	10,746,681		538,147	1,784,495		
Nonbudgeted Expenditures & Transfers-Out	2,980	86,172,151		31,966,745	24,659	35,757		125,220,393
Prior Year Expenditures & Transfers-Out Adjustments	(108,806)	3,401,275	87,085		14,235	7,490		1,773,108
Reductions in Property Held in Trust							2,919,774	
Total Reductions	22,025,397	138,377,494	10,833,766	31,966,745	577,041	1,827,742	2,919,774	126,993,501
FUND BALANCE: June 30, 2009	$ (4,265,154)	$ 387,900,733	$ (6,567,579)	$ 25,030,336	$ (33,206)	$ 245,741	$ 0	$ 447,471,363
PROPERTY HELD IN TRUST: June 30, 2009							$ 1,760,336	

This schedule is prepared from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) without adjustment.
Additional information is provided in the notes to the financial schedules beginning on page A-9.

DEPARTMENT OF NATURAL RESOURCES AND CONSERVATION
SCHEDULE OF TOTAL REVENUES & TRANSFERS-IN
FOR THE FISCAL YEAR ENDED JUNE 30, 2010

	General Fund	State Special Revenue Fund	Federal Special Revenue Fund	Debt Service Fund	Enterprise Fund	Internal Service Fund	Private-Purpose Trust Fund	Permanent Fund	Total
TOTAL REVENUES & TRANSFERS-IN BY CLASS									
Licenses and Permits		$ 254,208						$ 1,432,057	$ 1,686,265
Taxes	$ 4,261	3,301,961	$ 951		$ 26	$ 1,236			3,308,435
Charges for Services	145,809	2,607,675		$ 4,362		598,902			3,356,748
Investment Earnings	511	2,354,736		9,309,261			$ 1,393	62,309,811	73,975,712
Fines and Forfeits	(6,894)	18,898							12,004
Capital Contributions					3,600				3,600
Sale of Documents, Merchandise and Property	12	906,617		3,435,029	623,816			8,387,644	13,353,118
Rentals, Leases and Royalties	18,747	112,049						142,924,578	143,055,374
Grants, Contracts, and Donations		346,609							346,609
Transfers-in		315,504,611		8,384,666		1,218,390	1,000,000	54,718,159	380,825,826
Bond Proceeds		4,119,153							4,119,153
Capital Asset Sale Proceeds	600	20,300						2,888,946	2,909,846
Proceeds of Refunding Bonds		8,050,000							8,050,000
Federal Indirect Cost Recoveries			191,260						191,260
Miscellaneous	3,585	798			16,100				20,483
Federal			19,556,138						19,556,138
Total Revenues & Transfers-In	166,631	337,597,615	19,748,349	21,133,318	643,542	1,818,528	1,001,393	272,661,195	654,770,571
Less: Nonbudgeted Revenues & Transfers-In	39,129	113,947,159	954	21,147,172	26	1,236	1,001,393	268,066,289	404,203,358
Prior Year Revenues & Transfers-In Adjustments	(14,674)	4,301,429	13,394	(13,854)				4,594,906	8,881,201
Actual Budgeted Revenues & Transfers-In	142,176	219,349,027	19,734,001	0	643,516	1,817,292	0	0	241,686,012
Estimated Revenues & Transfers-In	142,237	219,351,225	19,734,302		643,520	1,817,291			241,688,575
Budgeted Revenues & Transfers-In Over (Under) Estimated	$ (61)	$ (2,198)	$ (301)	$ 0	$ (4)	$ 1	$ 0	$ 0	$ (2,563)
BUDGETED REVENUES & TRANSFERS-IN OVER (UNDER) ESTIMATED BY CLASS									
Licenses and Permits		$ (2)							$ (2)
Taxes		(1)							(1)
Charges for Services	$ 4	(585)				$ 2			(579)
Investment Earnings		(297)	$ (4)						(301)
Fines and Forfeits		(2)							(2)
Monetary Settlements	(25)								(25)
Sale of Documents, Merchandise and Property		(3)			$ (4)				(7)
Transfers-in		(1,267)				(1)			(1,268)
Bond Proceeds		(41)							(41)
Federal Indirect Cost Recoveries			(74)						(74)
Miscellaneous	(40)								(40)
Federal			(223)						(223)
Budgeted Revenues & Transfers-In Over (Under) Estimated	$ (61)	$ (2,198)	$ (301)	$ 0	$ (4)	$ 1	$ 0	$ 0	$ (2,563)

This schedule is prepared from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) without adjustment.
Additional information is provided in the notes to the financial schedules beginning on page A-9.

DEPARTMENT OF NATURAL RESOURCES AND CONSERVATION
SCHEDULE OF TOTAL REVENUES & TRANSFERS-IN
FOR THE FISCAL YEAR ENDED JUNE 30, 2009

	General Fund	State Special Revenue Fund	Federal Special Revenue Fund	Debt Service Fund	Enterprise Fund	Internal Service Fund	Permanent Fund	Total
TOTAL REVENUES & TRANSFERS-IN BY CLASS								
Licenses and Permits		$ 250,500					$ 1,375,211	$ 1,625,711
Taxes	$ 6,762	3,500,591			$ 33	$ 880		3,508,266
Charges for Services	149,290	2,816,870		$ (994,907)		893,259		2,864,512
Investment Earnings	2,025	3,630,831		10,380,032			18,284,578	32,297,466
Fines and Forfeits	48,439	19,691						68,130
Capital Contributions					14,400			14,400
Sale of Documents, Merchandise and Property	2,800	767,352		3,189,507	502,983		7,937,217	12,399,859
Rentals, Leases and Royalties	20,218	145,248					72,240,304	72,405,770
Grants, Contracts, and Donations		456,032						456,032
Transfers-in	607,935	180,653,671		14,080,490		977,351	19,412,391	215,731,838
Capital Asset Sale Proceeds	24,850	11,950					5,470,253	5,507,053
Federal Indirect Cost Recoveries			$ 178,369					178,369
Miscellaneous	6,473	4,415	10,245		115			21,248
Federal			21,244,270					21,244,270
Total Revenues & Transfers-In	868,792	192,257,151	21,432,884	26,655,122	517,531	1,871,490	124,719,954	368,322,924
Less: Nonbudgeted Revenues & Transfers-In	664,852	64,748,322	10,259	26,490,488	33	880	123,260,526	215,175,360
Prior Year Revenues & Transfers-In Adjustments	2,386	513,441	(6,816,090)	164,634	10,530	(2,626)	1,459,428	(4,668,297)
Actual Budgeted Revenues & Transfers-In	201,554	126,995,388	28,238,715	0	506,968	1,873,236	0	157,815,861
Estimated Revenues & Transfers-In	201,600	126,997,890	28,240,898		506,967	1,873,236		157,820,591
Budgeted Revenues & Transfers-In Over (Under) Estimated	$ (46)	$ (2,502)	$ (2,183)	$ 0	$ 1	$ 0	$ 0	$ (4,730)
BUDGETED REVENUES & TRANSFERS-IN OVER (UNDER) ESTIMATED BY CLASS								
Taxes		$ (8)						$ (8)
Charges for Services	$ (4)							(4)
Investment Earnings		(2,452)	$					(2,452)
Fines and Forfeits	(31)							(31)
Sale of Documents, Merchandise and Property								0
Grants, Contracts, and Donations		1						1
Transfers-in		(43)						(43)
Federal Indirect Cost Recoveries								0
Miscellaneous	(11)				$ 1			0
Federal			(2,183)					(2,183)
Budgeted Revenues & Transfers-In Over (Under) Estimated	$ (46)	$ (2,502)	$ (2,183)	$ 0	$ 1	$ 0	$ 0	$ (4,730)

This schedule is prepared from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) without adjustment.
Additional information is provided in the notes to the financial schedules beginning on page A-9.

DEPARTMENT OF NATURAL RESOURCES AND CONSERVATION
SCHEDULE OF TOTAL EXPENDITURES & TRANSFERS-OUT
FOR THE FISCAL YEAR ENDED JUNE 30, 2010

	CENTRALIZED SERVICES DIVISION	CONSERVATION & RESOURCE DEVELOPMENT DIVISION	FORESTRY & TRUST LANDS	OIL & GAS CONSERVATION DIVISION	RESERVED WATER RIGHTS COMPACT COMMISSION	TRUST FUNDS	WATER RESOURCES DIVISION	Total
PROGRAM (ORG) EXPENDITURES & TRANSFERS-OUT								
Personal Services								
Salaries	$ 2,030,176	$ 1,263,827	$ 12,970,052	$ 805,808	$ 313,022		$ 6,915,573	$ 24,298,458
Hourly Wages	682		3,144,127					3,144,809
Other Compensation		880		7,280	2,728		317	11,205
Employee Benefits	618,075	409,917	5,119,353	260,938	89,652		2,315,806	8,813,741
Personal Services-Other			22,767					22,767
Total	2,648,933	1,674,624	21,256,299	1,074,026	405,402		9,231,696	36,290,980
Operating Expenses								
Other Services	318,475	7,010,251	6,634,545	1,052,448	61,434		4,205,289	19,282,442
Supplies & Materials	184,263	102,827	2,586,725	57,632	10,862		414,684	3,356,995
Communications	89,888	40,999	487,639	46,539	10,048		211,002	886,115
Travel	26,281	66,922	395,647	42,013	22,925		131,079	684,867
Rent	198,118	80,695	2,661,110	20,611	46,878		758,306	3,765,719
Utilities	19,178	5,276	228,071	14,480	4,568		11,048	282,622
Repair & Maintenance	714	6,468	798,143	12,617	550		39,836	858,327
Other Expenses	74,895	79,636	567,744	49,997	1,536	$ 5,756	256,284	1,035,849
Goods Purchased For Resale			8,777					8,777
Total	911,812	7,393,074	14,368,401	1,296,337	158,801	5,756	6,027,530	30,161,713
Equipment & Intangible Assets								
Equipment		25,623	1,003,178	48,075			66,333	1,143,208
Capital leases - equipment							(535)	(535)
Total		25,623	1,003,178	48,075			65,798	1,142,672
Capital Outlay								
Land & Interest In Land			119,204				3,000	122,204
Total			119,204				3,000	122,204
Grants								
From State Sources		5,338,339		3,000				5,341,339
From Federal Sources			8,776,224					8,776,224
Total		5,338,339	8,776,224	3,000				14,117,563
Benefits & Claims								
Other Financing Uses/Deduction		8,579,579						8,579,579
Total		8,579,579						8,579,579
Transfers-out								
Fund transfers		97,187,851	2,681,525			238,191,645	2,064,139	340,125,161
Intra-Entity Expense			72,894			2,910,420		2,983,314
Total		97,187,851	2,754,419			241,102,066	2,064,139	343,108,475
Debt Service								
Bonds		6,453,598						6,453,598
Loans		484,085					385,453	869,539
Capital Leases			3,675					3,675
Total		6,937,683	3,675				385,453	7,326,811
Other Post Employment Benefits								
Other Post Employment Benefits			53,700					53,700
Total			53,700					53,700
Total Expenditures & Transfers-Out	$ 3,560,745	$ 127,136,773	$ 48,335,100	$ 2,421,438	$ 564,203	$ 241,107,822	$ 17,777,616	$ 440,903,697
EXPENDITURES & TRANSFERS-OUT BY FUND								
General Fund	$ 2,502,705	$ 1,565,215	$ 9,775,483		$ 516,663		$ 7,844,618	$ 22,204,684
State Special Revenue Fund	593,856	124,068,162	23,364,798	$ 2,313,888	47,540	$ 13,516,577	8,754,021	172,658,842
Federal Special Revenue Fund	464,184	(16,158,428)	12,475,526	107,550			1,173,124	(1,938,044)
Debt Service Fund		17,661,824					5,853	17,667,677
Enterprise Fund			743,809					743,809
Internal Service Fund			1,975,484					1,975,484
Permanent Fund						227,591,245		227,591,245
Total Expenditures & Transfers-Out	3,560,745	127,136,773	48,335,100	2,421,438	564,203	241,107,822	17,777,616	440,903,697
Less: Nonbudgeted Expenditures & Transfers-Out	56,176	111,060,289	1,608,699	1,926	165	236,603,032	2,191,239	351,521,526
Prior Year Expenditures & Transfers-Out Adjustments	1,040	(460,131)	808,263	(422)	182	4,504,790	(17,754)	4,835,968
Actual Budgeted Expenditures & Transfers-Out	3,503,529	16,536,615	45,918,138	2,419,934	563,856	0	15,604,131	84,546,203
Budget Authority	3,667,493	63,144,820	70,330,314	4,009,038	17,117,290		24,477,215	182,746,170
Unspent Budget Authority	$ 163,964	$ 46,608,205	$ 24,412,176	$ 1,589,104	$ 16,553,434	$ 0	$ 8,873,084	$ 98,199,967
UNSPENT BUDGET AUTHORITY BY FUND								
General Fund	$ 122,963	$ 133,672	$ 465,486		$ 40,974		$ 171,148	$ 934,243
State Special Revenue Fund		26,058,513	12,491,502	$ 1,534,962	16,512,460		7,048,588	63,646,025
Federal Special Revenue Fund	41,001	20,416,020	10,971,143	54,142			1,653,348	33,135,654
Enterprise Fund			129,285					129,285
Internal Service Fund			354,760			$		354,760
Unspent Budget Authority	$ 163,964	$ 46,608,205	$ 24,412,176	$ 1,589,104	$ 16,553,434	0	$ 8,873,084	$ 98,199,967

DEPARTMENT OF NATURAL RESOURCES AND CONSERVATION
SCHEDULE OF TOTAL EXPENDITURES & TRANSFERS-OUT
FOR THE FISCAL YEAR ENDED JUNE 30, 2009

	CENTRALIZED SERVICES DIVISION	CONSERVATION/RESOURCE DEVELOPMENT DIVISION	FORESTRY & TRUST LANDS	OIL & GAS CONSERVATION DIVISION	RESERVED WATER RIGHTS COMPACT COMMISSION	TRUST FUNDS	WATER RESOURCES DIVISION	Total
PROGRAM (ORG) EXPENDITURES & TRANSFERS-OUT								
Personal Services								
Salaries	$ 2,050,527	$ 1,201,434	$ 12,665,740	$ 824,132	$ 403,850		$ 7,246,980	$ 24,392,663
Hourly Wages			3,928,174				267	3,928,441
Other Compensation		690		8,028	3,765		410	12,893
Employee Benefits	610,536	376,947	5,024,091	258,788	104,924		2,389,125	8,764,411
Personal Services-Other			15,437					15,437
Total	2,661,063	1,579,071	21,633,442	1,090,948	512,539		9,636,782	37,113,845
Operating Expenses								
Other Services	439,639	2,441,739	10,331,365	913,709	662,607		4,776,553	19,565,612
Supplies & Materials	103,544	56,379	3,041,551	80,484	34,906		262,288	3,579,152
Communications	72,305	45,419	382,094	44,829	8,021		173,201	725,869
Travel	29,570	87,411	526,865	49,811	30,605		179,113	903,375
Rent	189,004	79,730	2,288,867	20,270	44,896		755,942	3,378,709
Utilities	22,238	6,088	255,657	13,709	5,297		8,126	311,115
Repair & Maintenance	2,179	13,777	832,211	26,767			122,550	997,484
Other Expenses	23,238	123,350	544,089	43,395	3,160	$ 5,594	223,094	965,920
Goods Purchased For Resale			2,764					2,764
Total	881,717	2,853,893	18,205,463	1,192,974	789,492	5,594	6,500,867	30,430,000
Equipment & Intangible Assets								
Equipment	21,560		1,924,469	83,681	13,792		42,554	2,086,056
Capital leases - equipment			89				6,604	6,693
Intangible Assets			8,895					8,895
Total	21,560		1,933,453	83,681	13,792		49,158	2,101,644
Capital Outlay								
Land & Interest In Land			(31,386)			6,401,000	3,000	6,372,614
Total			(31,386)			6,401,000	3,000	6,372,614
Grants								
From State Sources		9,899,555	81,806	3,200				9,984,561
From Federal Sources			3,493,857					3,493,857
From Other Sources			32,130					32,130
Total		9,899,555	3,607,793	3,200				13,510,548
Transfers-out								
Fund transfers		86,085,127	1,398,681			141,179,261	0	228,663,069
Intra-Entity Expense			90,984			3,582,409		3,673,393
Total		86,085,127	1,489,665			144,761,670	0	232,336,462
Debt Service								
Bonds		10,240,946						10,240,946
Loans		45,619					378,199	423,818
Capital Leases			4,837					4,837
Total		10,286,565	4,837				378,199	10,669,601
Other Post Employment Benefits								
Other Post Employment Benefits			66,972					66,972
Total			66,972					66,972
Total Expenditures & Transfers-Out	$ 3,564,340	$ 110,704,211	$ 46,910,239	$ 2,370,803	$ 1,315,823	$ 151,168,264	$ 16,568,006	$ 332,601,686
EXPENDITURES & TRANSFERS-OUT BY FUND								
General Fund	$ 2,593,396	$ 1,306,456	$ 9,291,796		$ 760,228		$ 8,073,521	$ 22,025,397
State Special Revenue Fund	865,277	77,148,721	26,854,431	$ 2,198,563	555,595	$ 24,174,763	6,580,144	138,377,494
Federal Special Revenue Fund	105,667	288,142	8,359,229	172,240			1,908,488	10,833,766
Debt Service Fund		31,960,892					5,853	31,966,745
Enterprise Fund			577,041					577,041
Internal Service Fund			1,827,742					1,827,742
Permanent Fund						126,993,501		126,993,501
Total Expenditures & Transfers-Out	3,564,340	110,704,211	46,910,239	2,370,803	1,315,823	151,168,264	16,568,006	332,601,686
Less: Nonbudgeted Expenditures & Transfers-Out	(446)	93,492,857	516,648			149,395,157	18,471	243,422,687
Prior Year Expenditures & Transfers-Out Adjustments	(13,494)	(236,049)	3,668,045	234	732	1,773,107	(18,185)	5,174,390
Actual Budgeted Expenditures & Transfers-Out	3,578,280	17,447,403	42,725,546	2,370,569	1,315,091	0	16,567,720	84,004,609
Budget Authority	3,609,656	59,921,992	85,911,072	3,837,015	16,268,224		26,188,715	195,736,674
Unspent Budget Authority	$ 31,376	$ 42,474,589	$ 43,185,526	$ 1,466,446	$ 14,953,133	$ 0	$ 9,620,995	$ 111,732,065
UNSPENT BUDGET AUTHORITY BY FUND								
General Fund	$ 15,145	$ 4,999	$ 1,103,671		$ 51,603		$ 190,817	$ 1,366,235
State Special Revenue Fund	0	42,469,590	34,671,695	$ 1,439,696	14,901,530		8,582,463	102,064,974
Federal Special Revenue Fund	16,231		7,193,219	26,750			847,715	8,083,915
Enterprise Fund			81,853					81,853
Internal Service Fund			135,088					135,088
Unspent Budget Authority	$ 31,376	$ 42,474,589	$ 43,185,526	$ 1,466,446	$ 14,953,133	$ 0	$ 9,620,995	$ 111,732,065

This schedule is prepared from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) without adjustment. Additional information is provided in the notes to the financial schedules beginning on page A-9.

Department of Natural Resources and Conservation

Notes to the Financial Schedules
For the Two Fiscal Years Ended June 30, 2010

1. Summary of Significant Accounting Policies

Basis of Accounting

The department uses the modified accrual basis of accounting, as defined by state accounting policy, for its Governmental fund category (General, State Special Revenue, Federal Special Revenue, Debt Service, and Permanent) and certain liabilities of defined benefit pension plans and certain post employment healthcare plans. In applying the modified accrual basis, the department records:

- Revenues when it receives cash or when receipts are realizable, measurable, earned, and available to pay current period liabilities.
- Expenditures for valid obligations when the department incurs the related liability and it is measurable, with the exception of the cost of employees' annual and sick leave. State accounting policy requires the department to record the cost of employees' annual and sick leave when used or paid.

The department uses accrual basis accounting for its Proprietary (Enterprise and Internal Service) and Fiduciary (Private-Purpose Trust and Agency) fund categories. Under the accrual basis, as defined by state accounting policy, the department records revenues in the accounting period when realizable, measurable, and earned, and records expenses in the period incurred when measurable.

Expenditures and expenses may include: entire budgeted service contracts even though the department receives the services in a subsequent fiscal year; goods ordered with a purchase order before fiscal year-end, but not received as of fiscal year-end; and equipment ordered with a purchase order before fiscal year-end.

Basis of Presentation

The financial schedule format is in accordance with the policy of the Legislative Audit Committee. The financial schedules are prepared from the transactions posted to the state's accounting system without adjustment.

The department uses the following funds:

Governmental Fund Category

- **General Fund** – to account for all financial resources except those required to be accounted for in another fund.

- **State Special Revenue Fund** – to account for proceeds of specific revenue sources (other than private-purpose trusts or major capital projects) that are legally restricted to expenditures for specific state program purposes. Department State Special Revenue Funds include Forestry operations, Wastewater and Drinking Water Projects, and the Renewable Resource grants and Loans Program.
- **Federal Special Revenue Fund** – to account for activities funded from federal revenue sources. The department's fire operations and suppression efforts are financed in part by federal funds.
- **Debt Service Fund** – to account for accumulated resources for the payment of general long-term debt principal and interest. The department accounts for Renewable Resources, Coal Severance Tax, and State Revolving Fund bond payments in this fund.
- **Permanent Fund** – to account for financial resources that are permanently restricted to the extent that only earnings, and not principal, may be used for purposes that support the department's programs. The department uses this fund for the Common School Trust, university and college trusts, Morrill Trust, School for the Deaf and Blind Trust, Pine Hills School Trust, Montana Development Center Trust, Montana State Hospital Trust, Veteran's Home Trust, Capital Building Trust, and the Trust and Legacy Account.

Proprietary Fund Category

- **Internal Service Fund** – to account for the financing of goods or services provided by one department or agency to other departments or agencies of state government or to other governmental entities on a cost-reimbursement basis. The Department's Internal Service Fund contains the Forestry Division's Air Operations Bureau. The Air Operations Bureau maintains and operates aircraft to aid in fire suppression.
- **Enterprise Fund** – to account for operations (a) financed and operated in a manner similar to private business enterprises, where the Legislature intends that the department finance or recover costs primarily through user charges; (b) where the Legislature has decided that periodic determination of revenues earned, expenses incurred or net income is appropriate; (c) where the activity is financed solely by a pledge of the net revenues from fees and charges of the activity; or (d) when laws or regulations require that the activities' cost of providing services, including capital costs, be recovered with fees and charges rather than with taxes or similar revenues. The department accounts for the State Nursery Program in this fund.

Fiduciary Fund Category

- **Private-Purpose Trust Fund** – to account for activity of any trust arrangement not properly reported in a pension fund or an investment trust fund where the principal and income benefit individuals, private organizations, or other governments. The department's private-purpose trust fund is used to account for Fort Belknap Peoples Creek Minimum Flow funds set aside for the Fort Belknap-Montana Water Rights Compact, per section 85-20-1007, MCA.

- **Agency Fund** – to account for resources held by the state in a custodial capacity. Agency funds may be used on a limited basis for internal (to the State) clearing account activity but these must have a zero balance at fiscal year-end. The department's agency funds account for activity such as contractual bonds and hazard reduction.

2. General Fund Balance (negative balances)

The negative fund balance in the General Fund does not indicate overspent appropriation authority. The department has authority to pay obligations from the statewide General Fund within its appropriation limits. The department expends cash or other assets from the statewide fund when it pays General Fund obligations. The department's outstanding liabilities exceed the assets it has placed in the fund, resulting in negative ending General Fund balances for each of the fiscal years ended June 30, 2010 and June 30, 2009.

3. Direct Entries to Fund Balance

Direct entries to fund balances in the General, State Special Revenue, Federal Special Revenue, Debt Service, and Permanent funds include entries generated by SABHRS to reflect the flow of resources within individual funds shared by separate agencies.

4. Long-Term Debt

During prior fiscal years, the state of Montana issued General Obligation bonds for the Drinking Water State Revolving Fund and Water Pollution Control State Revolving Fund programs. These bonds were used for Drinking Water and Water Pollution Control project loans. At June 30, 2010, the department had a total of $21,520,000 in General Obligation bonds outstanding for these programs.

During prior fiscal years, the state of Montana issued General Obligation bonds for the Renewable Resource Loan program. These bonds were used for private loans for irrigation projects. At June 30, 2010, the department had a total of $1,510,000 of General Obligation bonds outstanding for this program.

During prior fiscal years, the department issued Coal Severance Tax bonds for the Renewable Resource Loan program. These bonds were used for public loans for irrigation, water, sewer and dam projects. At June 30, 2010, the department had a total of $20,685,000 of Coal Severance Tax bonds outstanding.

The department has a loan from the U.S. Bureau of Reclamation to fund the Middle Creek Dam project. The unpaid loan principal and interest during construction balance as of June 30, 2010, was $2,586,368.

The Northern Cheyenne Tribe and the department entered into an agreement on July 1, 1994, in which the tribe agreed to loan the state up to $11,500,000 of federal funds appropriated as part of the Northern Cheyenne Indian Reserved Water Rights Settlement. The noninterest bearing loan was used to help finance the costs of the Tongue River Dam Project. The actual amount of the loan was $11,300,000. The outstanding loan balance at June 30, 2010, was $8,112,821. In March 2005, the department issued Coal Severance Tax bond to the tribe for $9,851,282 as security for the loan. The bond, which is noninterest bearing, provides a means of prepayment to the tribe in the event pledged revenues are insufficient for loan repayment.

5. Transfers-In

The Schedule of Total Revenues and Transfers-In contain the following activity in the transfers-in class:

- **General Fund** – This activity represents the proceeds from the sale of fixed assets and the Coal Severance Tax sweep from the State Special Revenue Fund.
- **State Special Revenue Fund** – A portion of this activity is the transfer of Common School Permanent Trust Fund earnings to the Guarantee Account for distribution to school districts. Transfers-In activity also includes the movement of loans receivable from other funds and the transfer of federal funds from the Department of Environmental Quality for the Clean Water and Drinking Water State Revolving Funds.
- **Debt Service Fund** – This activity is comprised of the movement of loans receivable from other funds.
- **Permanent Fund** – This activity represents the allocation of interest and income within the trust funds administered by the department.

6. Permanent Fund Revenues

In fiscal year 2009-10, the department received an $86 million bonus payment related to the Otter Creek coal lease on school trust lands, bringing total permanent fund bonus payments to approximately $93.2 million for the year. In fiscal year 2008-09, total permanent fund bonus payments totaled approximately $12 million.

7. Revenue Estimates

As part of the fiscal year-end procedures, the department adjusts revenue estimates to closely reflect actual revenues for each year. Significant revenue estimate adjustments for fiscal year 2009-10 were $81 million increase for the Guarantee Fund related to the Otter Creek bonus payment, $6 million increase for Water Pollution Control State Revolving Fund Loan Account, and $4.7 million decrease in Nonconsolidated Federal Grants. Significant adjustments for fiscal year 2008-09 included $18 million

increase for Federal Reimbursements for Fire Suppression, $11 million increase for Water Pollution Control State Revolving Fund Loan Account, and $8 million increase for the Guarantee Fund.

8. Unspent Budget Authority

The table below summarizes significant unspent budget authority by program.

	FY 2009-10	FY 2008-09
Conservation and Resource Development Division		
Treasure State Endowment	13,508,845	24,531,500
Natural Resource Operations	11,461,123	17,095,240
Water Pollution Control ARRA	9,962,983	
Drinking Water ARRA	10,034,112	
Forestry/Trust Lands Division		
Fire Suppression	10,453,037	31,972,800
Reserved Water Rights Compact Commission		
Black feet Mitigation	14,512,460	14,901,530
Water Resources Division		
State Hydro Project Earnings	3,408,008	5,673,816

For fiscal year 2009-10, most amounts are related to biennial appropriations and the budget authority extends to fiscal year 2010-11.

9. American Recovery and Reinvestment Act

The American Recovery and Reinvestment Act (ARRA) was enacted by the United States Congress to preserve and create jobs and promote economic recovery.

The department expects to receive federal funding from ARRA totaling approximately $29,585,998, all of which was appropriated in House Bill 645 of the 2009 Legislative Session. Of this amount, $12,677,992 was spent by June 30, 2010. The amount spent includes $416,200 in loans forgiven for the Water Pollution Control and Drinking Water State Revolving Fund programs. Loans outstanding related to these programs total approximately $16.4 million, and are expected to be forgiven in fiscal year 2010-11.

In addition, the department was awarded $525,000 through other competitive or noncompetative grants, of which $54,081 was spent by June 30, 2010.

10. Contingencies

PPL Montana, LLC v. State of Montana: In June 2008, the district court decided in favor of the state, ordering PPL Montana, LLC to pay $40,956,180 in rent for hydroelectric dams located on state-owned riverbeds. The decision recognizes rent from year 2000 through 2007, the time period PPL Montana owned and operated the dams. In March 2010, the Montana Supreme Court upheld the district court decision. In August 2010, PPL Montana, LLC, appealed to the U. S. Supreme Court.

Department of Natural Resources and Conservation

Department Response

DEPARTMENT OF NATURAL RESOURCES AND CONSERVATION

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October 21, 2010

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Tori Hunthausen
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RE: DNRC Written Response to the Legislative Audit Division Financial-Compliance Audit for the Two Fiscal Years Ended June 30, 2010

RECOMMENDATION #1

We recommend the department:

A. Maximize trust revenues for land utilized by First Peoples Buffalo Jump State Park.

B. Ensure fair market value is reflected in the final easement transaction for land utilized by First Peoples Buffalo Jump State Park

Response to both A and B:
Partially concur: In 2007, the department purchased 897.82 acres from the Eustance Ranch for $800 per acre. The appraised value for the property was $1,080 per acre. The Land Board approved the disposition of an interest in state land (under a five-year option agreement) for park purposes to DFWP for $800 per acre for 418 acres. This was the same price that DNRC paid for the land, but was $280 less per acre than the appraised value.

Per the DNRC Financial-Compliance Audit for the two fiscal years ended June 30, 2008, recommendation #8B, the Department approached DFWP and the Land Board staff to ascertain their interest in revisiting the option agreement that was previously approved by DFWP and the Land Board. There was no interest in adjusting the $800 per acre price that was previously negotiated.

In accordance with the option agreement, the Department of Fish Wildlife and Parks made annual payments of approximately $11,704 per year for two years. The department received an easement application per the option agreement for the park easement application in January 2010. The easement application will be processed and taken to the November 15, 2010 Land Board for final approval.

Additionally, after the last audit, the department discussed the potential for issuing a grazing lease on the site prior to the final approval of the conservation easement (currently slated for

November 2010). The department did not attempt to let a bid for a grazing lease due to the pending completion of the easement. The proposed easement allows the Grantee to "make exclusive use of the surface for a State Park."

C. **Quantify and seek full compensation on behalf of the Common School and Montana Tech trust funds for historical use of trust lands for Madison Buffalo Jump State Park and Lewis & Clark Caverns State Park.**
D. **Enter into agreements necessary to ensure proper and full compensation to the Common School and Montana Tech trust funds in the future.**

Response to both C and D:
Concur: The department will meet with the Department of Fish, Wildlife and Parks (DFWP) regarding the historic use of these properties. As mentioned in the audit, the department will discuss with DFWP compensation of $7,150 and $14,100 for the loss in revenue to the trusts if the department had entered into an easement for the Madison Buffalo Jump and Lewis and Clark Caverns state parks, respectively. The department will also discuss with DFWP the potential for the sale of an easement or lease for both properties going forward.

RECOMMENDATION #2
We recommend the department provide the Board of Land Commissioners with cabin site lease methodologies that will maximize trust revenues, as required by state law.

Partially concur: The department provided documentation, information, and five alternatives, which included a no action alternative (Alternative 1) in the development and approval of the methodology for securing full market value for cabin and homesite leases to the Land Board at their October 19, 2009 meeting. The Land Board chose the methodology referred to as Alternative 3B asking the DNRC to commence drafting rules in order to implement Alternative 3B. The administrative rules were adopted by the Land Board and filed with the Secretary of State in May 2010.

The components of Alternative 3B are supported by market evidence from the state leases, and local and regional markets, including average appreciation of land values statewide using Department of Revenue appraisals. The base rental is calculated using a 5% rate, which is consistent with the findings of the negotiated rulemaking committee of the early 2000s and consistent with the specification by the Supreme Court ruling that a rental rate of 3.5% of appraised value was too low.

Vacancies will likely occur as some lessees reach the upper limit of their ability to afford the lease rents. Alternative 3B, with its slightly diminished lease rental amounts, has the strong potential to reduce vacancies, thereby preserving rental incomes in the short term. Alternative 3B projected a vacancy rate of 3 - 8 percent and Alternative 1 projected a vacancy rate of 3 – 10 percent (cabinsite report Sept 2009). As of mid-October 2010, 38 vacancies (approximately a 5 percent vacancy rate) have occurred.

In light of the aforementioned analysis, the department believes that the methodology described in Alternative 3B achieves full market value for the trust beneficiaries.

RECOMMENDATION #3

We recommend the department compensate the trust for the $2,456,541 inappropriately withheld from Common School, State Reform School, MSU-Morrill, MSU-second grant, Montana School for the Deaf and Blind, Veterans Home, Capitol Building, and Sir Estate trust revenues and their beneficiaries.

Do not concur: Per the DNRC Financial-Compliance Audit for the two fiscal years ended June 30, 2008, recommendation #6B, the department sought a change in legislation to establish an expenditure allocation method that results in reasonable and appropriate cost allocations to each individual trust. In 2009, SB 65 was passed by the Legislature and signed by the Governor, and addressed the prior audit recommendations. SB 65 became effective in and was implemented in FY10. Regarding FY10 expenditures, the audit noted, "We analyzed the process used for fiscal year 2009-2010, and determined the department has properly accounted for administrative costs by trust."

Administrative expenses in FY07 through FY09 were determined using different methods than in FY10 (post SB 65). Expenses for the various trusts (pre SB 65) were assessed as a percentage of revenue generated by that trust as opposed to current methods of assessing work planned for and completed on a trust. Given the differences in accounting methods during those fiscal years, we would expect different results for the allocation of administrative expenses.

If DNRC were to have implemented the new methods to account for administrative expenses prior to the passage of SB 65, maximum expenditure caps established in 77-1-109 would have been exceeded for a number of the smaller trusts in FY07, FY08, and FY09. Current funding mechanisms that existed at that time limited the division's ability to charge management costs to a trust when those costs exceeded statutory caps.

Repayment of the $2,456,541 to the various trusts would require an appropriation by the Legislature.

RECOMMENDATION #4

We recommend the department apply consistent treatment in recording revenue and deferred revenue transactions related to the court decision.

Concur: The department will apply consistent treatment in recording revenue and deferred revenue transactions related to the court decision.

RECOMMENDATION #5

We recommend the department:

A. Revise its fire meal policy to reflect rates specified in state law.

B. Ensure meal costs are paid at rates allowed by state law for employees in travel status.

Response to both A and B:
Do Not Concur: 76-13-104(2)(a), MCA, requires the Department to adopt rules to protect the natural resources of state from destruction by fire. The Department's initial attack

strategy treats all fires DNRC responds to as exigencies or emergencies. Providing high calorie meals is imperative for the health and safety of firefighters and the ultimate success of DNRC's firefighting mission. Any additional costs of those meals beyond the standard state meal rates logically falls within the scope of MCA 76-13-104(2)(a) and 76-13-111, MCA.

RECOMMENDATION #6
We recommend the department incorporate emergency employee travel and fitness costs into the appropriate policy manual.

Concur: The department will incorporate emergency employee travel and fitness-related expenditure guidelines into policy.

RECOMMENDATION #7
We recommend the department enhance internal controls to ensure costs submitted for payment are properly authorized.

Concur: The department has enhanced internal controls to ensure costs submitted for payment are properly authorized. The process was implemented July 1, 2010.

RECOMMENDATION #8
We recommend the department document the process used to calculate and record the fiscal year-end fire accrual.

Concur: The department will document the process used to calculate and record the fiscal year-end fire accrual.

RECOMMENDATION #9
We recommend the department establish and document procedures to ensure property donated from the federal Department of Defense is recorded in accordance with state law and policy.

Concur: The department will establish internal controls to ensure property donated from the Department of Defense is recorded at fair market value.

RECOMMENDATION #10
We recommend the department prepare the annual operation assessment plan to determine fire costs, and submit timely certification to the Department of Revenue, as required by state law.

Concur: The department will prepare an annual operation assessment plan to determine fire protection costs and certify to the Department of Revenue, by the first Tuesday in September of each year.

RECOMMENDATION #11
We recommend the department submit the annual report for the Reserved Water Rights Compact as required by state law.

Concur: The report program is being finalized this fall and the annual report will be submitted to Bureau of Land Management in January 2011.

Sincerely:

Mary Sexton
Director