



A REPORT  
TO THE  
MONTANA  
LEGISLATURE

FINANCIAL-COMPLIANCE AUDIT

## *State Auditor's Office*

*For the Two Fiscal Years Ended  
June 30, 2010*

OCTOBER 2010

LEGISLATIVE AUDIT  
DIVISION

10-20

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Government Auditing Standards, the Single Audit Act Amendments of 1996 and OMB Circular A-133 require the auditor to issue certain financial, internal control, and compliance reports. This individual agency audit report is not intended to comply with these reporting requirements and is therefore not intended for distribution to federal grantor agencies. The Legislative Audit Division issues a statewide biennial Single Audit Report which complies with the above reporting requirements. The Single Audit Report for the two fiscal years ended June 30, 2009, was issued March 1, 2010. The Single Audit Report for the two fiscal years ended June 30, 2011, will be issued by March 31, 2012. Copies of the Single Audit Report can be obtained by contacting:

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# LEGISLATIVE AUDIT DIVISION

Tori Hunthausen, Legislative Auditor  
Monica Huyg, Legal Counsel



Deputy Legislative Auditors  
James Gillett  
Angie Grove

October 2010

The Legislative Audit Committee  
of the Montana State Legislature:

This is our financial-compliance audit report on the State Auditor's Office (office) for the two fiscal years ended June 30, 2010. Included in this report are recommendations concerning internal control deficiencies, and compliance with state laws. The office's written response to the audit recommendations is included in the audit report beginning on page B-3.

We thank the State Auditor and her staff for their assistance and cooperation during the audit.

Respectfully submitted,

*/s/ Tori Hunthausen*

Tori Hunthausen, CPA  
Legislative Auditor



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## APPOINTED AND ADMINISTRATIVE OFFICIALS

### State Auditor's Office

Monica Lindeen, State Auditor

Walt Schweitzer, Deputy State Auditor

Lynne Egan, Deputy Securities Commissioner

Bob Moon, Deputy Insurance Commissioner

Sharon McCabe, Central Services Administrator

### Insure Montana Board Members

			<u>Term Expires</u>
John Thomas	Helena		January 2012
Jim Edwards	Helena		June 2012
Erin McGowan Fincham	Helena		June 2013
Eve Franklin	Helena		Pleasure*
Betty Beverly	Helena		January 2013
Bob Marsenich	Polson		January 2011
Katherine Buckley-Patton	Helena/Dillon		January 2013
David B. Kendall	Missoula		June 2011
Carol Roy	Helena		Pleasure*

\*Eve Franklin from the Governor's Office and Carol Roy from the State Auditor's Office serve as the nonvoting staff appointments to the board.

For additional information concerning the State Auditor's Office, contact Monica Lindeen:

State Auditor's Office  
P. O. Box 4009  
Helena, MT 59604-4009  
(406) 444-2040  
e-mail: mlindeen@mt.gov



## FINANCIAL-COMPLIANCE

## State Auditor's Office

For the Two Fiscal Years Ended June 30, 2010

OCTOBER 2010

10-20

REPORT SUMMARY

State Auditor's Office (Office) serves as the State Government watchdog for the citizens of Montana in the insurance and securities industries. The office is a criminal justice agency charged with protecting Montana's consumers through insurance and securities regulation and also through informing the public about insurance and securities issues.

### Context

The Insurance Division regulates the insurance industry in Montana. Its duties include resolving insurance consumer inquiries and complaints about agents, coverage, and companies; licensing and reviewing the rates and financial condition of insurance companies; collecting the insurance premium tax; approving forms used by insurance companies; licensing, testing, and administering a continuing education program for insurance agents; and investigating insurance code and rule violations. In total, the office collected \$104,136,222 of Premium Insurance Taxes during fiscal years 2009 and 2010. The office is responsible for distributing a portion of insurance premium taxes to the Montana Public Employees' Retirement Administration, and to fire and police departments in qualifying Montana cities and towns.

The Securities Division is responsible for the administration and enforcement of the Securities Act of Montana. The division is responsible for the registration of securities issuers, salespeople, investment advisers, broker-dealers, and investment adviser representatives. It also investigates instances of unregistered or fraudulent securities transactions.

The office administers the Insure Montana Program, a two-part program that is designed to assist small

businesses with the cost of health insurance, whether they have previously provided health insurance or not. The program has a tax credit program and a purchasing pool, which is responsible for administering monthly assistance payments to qualifying businesses. In total, the office provided \$18,455,496 in assistance during fiscal years 2009 and 2010.

### Results

Sections within our audit report discuss areas where the office should improve controls to ensure proper recognition of premium insurance tax credits, bad debt transfers, and default fines. The audit report also discusses areas where the department should comply with state laws regarding securities fees and insurer deposits.

Recommendation Concurrence	
Concur	2
Partially Concur	0
Do Not Concur	0

Source: Agency audit response included in final report.

For a complete copy of the report or for further information, contact the Legislative Audit Division at 406-444-3122; e-mail to [lad@mt.gov](mailto:lad@mt.gov); or check the website at <http://leg.mt.gov/audit>. Report Fraud, Waste, and Abuse to the Legislative Auditor's FRAUD HOTLINE Call toll-free 1-800-222-4446 or e-mail [lad@mt.gov](mailto:lad@mt.gov).



# Chapter I – Introduction

## General

We performed the financial-compliance audit of the State Auditor’s Office (office) for the two fiscal years ended June 30, 2010. The objectives of the audit were to:

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

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 and correct misstatements on a timely basis. A significant deficiency is one or more control deficiencies that affect 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.

Subject	Significant Deficiency	Material Weakness	Page
Internal Controls - Information and Communication	Yes	Yes	5

This report contains two recommendations to the office. Other areas of concern deemed not to have a significant impact on the successful operations of the programs within the office are not specifically included in the 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.

## **Office Background and Organization**

The office was established by Article VI, Section 1 of the Montana Constitution. The State Auditor is the *ex-officio* Commissioner of Insurance and the *ex-officio* Commissioner of Securities. The State Auditor also serves as a member of the State Land Board and the Crop Hail Insurance Board. The office licenses and regulates insurance companies and agents within the state, and regulates and registers securities dealers. As of June 2010, the office has 76 full-time equivalent (FTE) positions, which include 14 exempt positions.

The office is organized as follows:

**Centralized Management** (17 FTE) is responsible for the administrative, budgeting, personnel, and accounting functions of the office. The division also provides support for the State Auditor as she fulfills her duties on the State Land Board and the Crop Hail Insurance Board.

**Insurance Division** (51 FTE) regulates the insurance industry in Montana. Its duties include resolving insurance consumer inquiries and complaints about agents, coverage, and companies; licensing and reviewing the rates and financial condition of insurance companies; collecting the insurance premium tax; approving forms used by insurance companies; licensing, testing, and administering a continuing education program for insurance agents; and investigating insurance code and rule violations.

The office administers the **Insure Montana Program** (5 FTE), a two-part program that is designed to assist small businesses with the cost of health insurance, whether they have previously provided health insurance or not. The program has a tax credit program and a purchasing pool, which is responsible for administering monthly assistance payments to qualifying businesses. Eligible employers participating in Insure Montana may choose to provide their employees group health insurance through a Qualified Association Health Plan (QAP) or through Insure Montana's purchasing pool. Whichever plan the employer chooses, the employer will receive incentive payments and the employees will receive assistance payments to assist with the cost of coverage. However, if a QAP is chosen and the benefits are less comprehensive than the purchasing pool's standard plan, a reduction is made to assistance and incentive payments.

**Securities Division** (12.5 FTE) is responsible for the administration and enforcement of the Securities Act of Montana. The division is responsible for the registration of securities issuers, salespeople, investment advisers, broker-dealers, and investment adviser representatives. It also investigates instances of unregistered or fraudulent securities transactions.

The office is responsible for distributing a portion of insurance premium taxes to the Montana Public Employees' Retirement Administration, and to fire and police departments in qualifying Montana cities and towns.

### **Prior Audit Recommendations**

The prior financial-compliance audit of the office for the two fiscal years ended June 30, 2008, contained eight recommendations. During the current audit, we determined the office implemented all eight of the recommendations.



## Chapter II – Findings and Recommendations

### **Internal Controls Information and Communication**

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**The office has not complied with state policy requirements for establishing and maintaining internal controls.**

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State accounting policy outlines management's responsibility for establishing and maintaining agency internal controls to safeguard and account for the resources entrusted to them to carry out government programs. State policy requires agencies to implement internal control procedures to ensure all transactions necessary for compliance with generally accepted accounting principles are recorded on the state's accounting records. To assist agencies in the implementation process, the Department of Administration issued an Internal Control Guidebook. The guide includes an internal control evaluation and monitoring plan, which recommends agencies monitor and test their controls and evaluate and report the results of that testing. Internal controls include information and communication, which is the identification, capture, and exchange of information in a form and time frame that enables agency staff to carry out their responsibilities.

During the audit we noted several instances where the office's internal controls related to information and communication were insufficient to properly identify, capture, or exchange information in a form and time to prevent errors. Office management indicated the following errors were the result of incomplete communication in the exchange of key information between divisions.

#### **Premium Insurance Tax Credits**

The office collects Premium Insurance Taxes from insurance companies who write insurance premiums in the state. Annual calculation of Premium Insurance Taxes may result in a Premium Insurance Tax Credit. State accounting policy requires these credits to be recorded as revenue abatements. Revenue abatements are recorded when disbursements of overpayments received from outside parties were previously recorded as revenues. Overpayments must be directly identifiable with the associated revenues from the outside party. In fiscal year 2008-09, the office did not properly record the revenue abatement on the state's accounting records resulting in a \$2,574,190 General Fund overstatement of Tax revenues.

#### **Bad Debt Transfers**

State accounting policy specifies that a current year nonbudgeted expenditure is recorded when transferring an uncollectible receivable, a bad debt, to the Department

of Revenue for collection. In fiscal year 2008-09, the office transferred uncollectable receivables for the Insure Montana program to the Department of Revenue but kept the receivable on the office's accounting records. This resulted in an understatement of nonbudgeted expenditures of \$34,794 in the State Special Revenue Fund.

## **Default Fines**

State accounting policy specifies that recognition of receivables should occur as soon as the underlying transaction occurs even if the resources are not yet received. This includes receivables in which the state has an enforceable legal claim to the resources that have not yet been received. Policy also specifies the corresponding revenue should be recorded in the period when earned, so long as receipt of cash is anticipated within 60 days of fiscal year-end. If receipt is expected to be delayed, the revenue should be deferred. In fiscal year 2009-10, the office did not record \$49,251 of receivables in the General Fund for default fines in which the office had an enforceable claim. Since the office did not anticipate collecting these fines within 60 days of fiscal year-end, deferred revenue entry also should have been recorded.

---

### **RECOMMENDATION #1**

*We recommend the office implement internal controls to properly identify, capture, or exchange information in a form and time to prevent errors.*

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## **Noncompliance with State Law**

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**The department did not comply with state laws regarding securities fees and excess deposits.**

---

### **Securities Fees**

Section 30-10-209, MCA, specifies the various security fees the office is required to collect from brokerage firms, investment advisory firms, and individuals working for those firms. Collectable security fees are defined as series, portfolio, or other subdivisions of an investment company. Currently the office only collects security fees at the series and portfolio levels. Other subdivision fees include classes of securities within each portfolio which the office is required to collect per state law. Noncollection of subdivision fees costs the General Fund an estimated \$750,000 to \$1,000,000 annually.

## Excess Deposits

Section 33-2-609, MCA, limits the amount of assets or securities an insurer may have on deposit to no more than 20 percent or \$50,000 of the required deposit, whichever is the larger amount, for the purpose of absorbing fluctuations in the value of assets and securities deposited, and to facilitate the exchange and substitution of such assets and securities. As of June 30, 2010, two of twelve insurers have deposits exceeding the permitted 20 percent excess threshold resulting in excess liabilities to the state of \$118,774.

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### **RECOMMENDATION #2**

*We recommend the office:*

- A. *Collect security fees at class levels as required by state law.*
  - B. *Retain assets or securities in amounts that do not exceed deposit thresholds as required by state law.*
-



# Independent Auditor's Report and Office 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 State Auditor's Office for each of the fiscal years ended June 30, 2010, and 2009. The information contained in these financial schedules is the responsibility of the office'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, the 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 office's assets, liabilities, and cash flows.

The office made errors in recording Premium Insurance Tax Credits in the General Fund in fiscal year 2008-09. Budgeted Revenues & Transfers-In on the Schedule of Changes in Fund Balances & Property Held in Trust is overstated by \$2,574,190.

In our opinion, except for the effects of the errors as discussed in the preceding paragraph, 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 State Auditor's Office 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

August 23, 2010

STATE AUDITOR'S OFFICE  
SCHEDULE OF CHANGES IN FUND BALANCES & PROPERTY HELD IN TRUST  
FOR THE FISCAL YEAR ENDED JUNE 30, 2010

	General Fund	State Special Revenue Fund	Enterprise Fund	Agency Fund
FUND BALANCE: July 1, 2009	\$ <u>(20,846,201)</u>	\$ <u>9,146,652</u>	\$ <u>440,124</u>	\$ <u>0</u>
PROPERTY HELD IN TRUST: July 1, 2009				\$ <u>11,919,437</u>
<b>ADDITIONS</b>				
Budgeted Revenues & Transfers-In	62,465,127	30,692,470		
Nonbudgeted Revenues & Transfers-In	2,994,974	505,199		
Prior Year Revenues & Transfers-In Adjustments	(499,592)	(413,823)		
Direct Entries to Fund Balance	(45,253,037)	(9,944,829)		
Additions to Property Held in Trust				475,224
Total Additions	<u>19,707,472</u>	<u>20,839,017</u>	<u>0</u>	<u>475,224</u>
<b>REDUCTIONS</b>				
Budgeted Expenditures & Transfers-Out	24,009,084	17,355,937		
Nonbudgeted Expenditures & Transfers-Out		3,079,577	440,124	
Prior Year Expenditures & Transfers-Out Adjustments	(129,571)	(178,962)		
Reductions in Property Held in Trust				1,571,356
Total Reductions	<u>23,879,513</u>	<u>20,256,552</u>	<u>440,124</u>	<u>1,571,356</u>
FUND BALANCE: June 30, 2010	\$ <u>(25,018,242)</u>	\$ <u>9,729,117</u>	\$ <u>0</u>	\$ <u>0</u>
PROPERTY HELD IN TRUST: June 30, 2010				\$ <u>10,823,305</u>

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.

STATE AUDITOR'S OFFICE  
SCHEDULE OF CHANGES IN FUND BALANCES & PROPERTY HELD IN TRUST  
FOR THE FISCAL YEAR ENDED JUNE 30, 2009

	General Fund	State Special Revenue Fund	Enterprise Fund	Agency Fund
FUND BALANCE: July 1, 2008	\$ (19,640,881)	\$ 8,144,670	\$ 389,217	\$ 0
PROPERTY HELD IN TRUST: July 1, 2008				\$ 11,960,371
<b>ADDITIONS</b>				
Budgeted Revenues & Transfers-In	57,444,798	34,339,398		
Nonbudgeted Revenues & Transfers-In	3,193,695	155,786	618,276	
Prior Year Revenues & Transfers-In Adjustments	(35,102)	302,376		
Direct Entries to Fund Balance	(39,435,885)	(15,195,479)	25,454	
Additions to Property Held in Trust				332,667
Total Additions	<u>21,167,506</u>	<u>19,602,081</u>	<u>643,730</u>	<u>332,667</u>
<b>REDUCTIONS</b>				
Budgeted Expenditures & Transfers-Out	22,372,826	15,132,581		
Nonbudgeted Expenditures & Transfers-Out		3,348,192	592,823	
Prior Year Expenditures & Transfers-Out Adjustments		119,326		
Reductions in Property Held in Trust				373,601
Total Reductions	<u>22,372,826</u>	<u>18,600,099</u>	<u>592,823</u>	<u>373,601</u>
FUND BALANCE: June 30, 2009	\$ (20,846,201)	\$ 9,146,652	\$ 440,124	\$ 0
PROPERTY HELD IN TRUST: June 30, 2009				\$ 11,919,437

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.

STATE AUDITOR'S OFFICE  
SCHEDULE OF TOTAL REVENUES & TRANSFERS-IN  
FOR THE FISCAL YEAR ENDED JUNE 30, 2010

	General Fund	State Special Revenue Fund	Total
<b>TOTAL REVENUES &amp; TRANSFERS-IN BY CLASS</b>			
Licenses and Permits	\$ 6,245,802	\$ 9,879,687	\$ 16,125,489
Taxes	54,371,662	9,542,622	63,914,284
Charges for Services		245,109	245,109
Fines and Forfeits	1,347,961		1,347,961
Grants, Contracts, and Donations		64,020	64,020
Transfers-in	2,995,084	11,014,173	14,009,257
Miscellaneous		38,235	38,235
Total Revenues & Transfers-In	64,960,509	30,783,846	95,744,355
Less: Nonbudgeted Revenues & Transfers-In	2,994,974	505,199	3,500,173
Prior Year Revenues & Transfers-In Adjustments	(499,592)	(413,823)	(913,415)
Actual Budgeted Revenues & Transfers-In	62,465,127	30,692,470	93,157,597
Estimated Revenues & Transfers-In	62,170,150	30,634,465	92,804,615
Budgeted Revenues & Transfers-In Over (Under) Estimated	\$ 294,977	\$ 58,005	\$ 352,982
<b>BUDGETED REVENUES &amp; TRANSFERS-IN OVER (UNDER) ESTIMATED BY CLASS</b>			
Licenses and Permits	\$ (98)	\$ (126)	\$ (224)
Taxes	295,214	58,903	354,117
Charges for Services		(386)	(386)
Fines and Forfeits	(39)		(39)
Grants, Contracts, and Donations		(83)	(83)
Transfers-in		(238)	(238)
Miscellaneous	(100)	(65)	(165)
Budgeted Revenues & Transfers-In Over (Under) Estimated	\$ 294,977	\$ 58,005	\$ 352,982

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.

STATE AUDITOR'S OFFICE  
SCHEDULE OF TOTAL REVENUES & TRANSFERS-IN  
FOR THE FISCAL YEAR ENDED JUNE 30, 2009

	General Fund	State Special Revenue Fund	Enterprise Fund	Total
<b>TOTAL REVENUES &amp; TRANSFERS-IN BY CLASS</b>				
Licenses and Permits	\$ 6,563,118	\$ 10,457,967		\$ 17,021,085
Taxes	49,764,560	14,866,037		64,630,597
Charges for Services		106,569	\$ 644,497	751,066
Investment Earnings			(26,221)	(26,221)
Fines and Forfeits	946,884			946,884
Grants, Contracts, and Donations		202,187		202,187
Transfers-in	3,328,829	9,233,136		12,561,965
Miscellaneous		(68,336)		(68,336)
Total Revenues & Transfers-In	60,603,391	34,797,560	618,276	96,019,227
Less: Nonbudgeted Revenues & Transfers-In	3,193,695	155,786	618,276	3,967,757
Prior Year Revenues & Transfers-In Adjustments	(35,102)	302,376		267,274
Actual Budgeted Revenues & Transfers-In	57,444,798	34,339,398	0	91,784,196
Estimated Revenues & Transfers-In	57,448,730	34,345,446		91,794,176
Budgeted Revenues & Transfers-In Over (Under) Estimated	\$ (3,932)	\$ (6,048)	\$ 0	\$ (9,980)
<b>BUDGETED REVENUES &amp; TRANSFERS-IN OVER (UNDER) ESTIMATED BY CLASS</b>				
Licenses and Permits	\$ (3,704)	\$ (4,266)		\$ (7,970)
Taxes	(112)	(745)		(857)
Charges for Services		(771)		(771)
Fines and Forfeits	(16)			(16)
Grants, Contracts, and Donations		(1)		(1)
Transfers-in		(64)		(64)
Intra-entity Revenue		(200)		(200)
Miscellaneous	(100)	(1)		(101)
Budgeted Revenues & Transfers-In Over (Under) Estimated	\$ (3,932)	\$ (6,048)	\$ 0	\$ (9,980)

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.

STATE AUDITOR'S OFFICE  
 SCHEDULE OF TOTAL EXPENDITURES & TRANSFERS-OUT  
 FOR THE FISCAL YEAR ENDED JUNE 30, 2010

PROGRAM (ORG) EXPENDITURES & TRANSFERS-OUT	CENTRAL MANAGEMENT	INSURANCE	LOCAL ASSISTANCE TO COUNTIES	SECURITIES	Total
Personal Services					
Salaries	\$ 719,271	\$ 2,452,076		\$ 487,608	\$ 3,658,955
Employee Benefits	229,705	793,856		159,524	1,183,085
Total	<u>948,976</u>	<u>3,245,932</u>		<u>647,132</u>	<u>4,842,040</u>
Operating Expenses					
Other Services	37,297	722,907		87,540	847,744
Supplies & Materials	26,813	121,808		22,231	170,852
Communications	23,177	131,865		43,392	198,434
Travel	12,900	102,429		30,290	145,619
Rent	66,181	203,622		36,197	306,000
Repair & Maintenance	73	1,321		48	1,442
Other Expenses	19,729	116,993		25,232	161,954
Total	<u>186,170</u>	<u>1,400,945</u>		<u>244,930</u>	<u>1,832,045</u>
Equipment & Intangible Assets					
Equipment	2,800	9,059		1,894	13,753
Total	<u>2,800</u>	<u>9,059</u>		<u>1,894</u>	<u>13,753</u>
Local Assistance					
From other sources			\$ 23,879,513		23,879,513
Total			<u>23,879,513</u>		<u>23,879,513</u>
Benefits & Claims					
To Individuals		925,563			925,563
From State Sources		9,648,066			9,648,066
Total		<u>10,573,629</u>			<u>10,573,629</u>
Transfers-out					
Fund transfers		466,327		2,968,882	3,435,209
Total		<u>466,327</u>		<u>2,968,882</u>	<u>3,435,209</u>
Total Expenditures & Transfers-Out	<u>\$ 1,137,946</u>	<u>\$ 15,695,892</u>	<u>\$ 23,879,513</u>	<u>\$ 3,862,838</u>	<u>\$ 44,576,189</u>
EXPENDITURES & TRANSFERS-OUT BY FUND					
General Fund			\$ 23,879,513		\$ 23,879,513
State Special Revenue Fund	\$ 1,137,946	\$ 15,255,768		\$ 3,862,838	20,256,552
Enterprise Fund		440,124			440,124
Total Expenditures & Transfers-Out	1,137,946	15,695,892	23,879,513	3,862,838	44,576,189
Less: Nonbudgeted Expenditures & Transfers-Out	(119)	487,487		3,032,334	3,519,702
Prior Year Expenditures & Transfers-Out Adjustments	(80)	(178,972)	(129,571)	89	(308,534)
Actual Budgeted Expenditures & Transfers-Out	1,138,145	15,387,377	24,009,084	830,415	41,365,021
Budget Authority	1,333,956	19,647,336	24,884,462	1,180,860	47,046,614
Unspent Budget Authority	<u>\$ 195,811</u>	<u>\$ 4,259,959</u>	<u>\$ 875,378</u>	<u>\$ 350,445</u>	<u>\$ 5,681,593</u>
UNSPENT BUDGET AUTHORITY BY FUND					
General Fund			\$ 875,378		\$ 875,378
State Special Revenue Fund	\$ 195,811	\$ 4,259,959		\$ 350,445	4,806,215
Unspent Budget Authority	<u>\$ 195,811</u>	<u>\$ 4,259,959</u>	<u>\$ 875,378</u>	<u>\$ 350,445</u>	<u>\$ 5,681,593</u>

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.

STATE AUDITOR'S OFFICE  
 SCHEDULE OF TOTAL EXPENDITURES & TRANSFERS-OUT  
 FOR THE FISCAL YEAR ENDED JUNE 30, 2009

	CENTRAL MANAGEMENT	INSURANCE	LOCAL ASSISTANCE TO COUNTIES	SECURITIES	Total
<b>PROGRAM (ORG) EXPENDITURES &amp; TRANSFERS-OUT</b>					
Personal Services					
Salaries	\$ 732,044	\$ 2,191,163		\$ 283,497	\$ 3,206,704
Other Compensation		3,900			3,900
Employee Benefits	221,298	692,468		96,847	1,010,613
Total	<u>953,342</u>	<u>2,887,531</u>		<u>380,344</u>	<u>4,221,217</u>
Operating Expenses					
Other Services	57,668	473,772		70,486	601,926
Supplies & Materials	20,090	53,257		12,777	86,124
Communications	15,457	99,798		41,661	156,916
Travel	13,941	55,404		22,738	92,083
Rent	59,444	158,421		33,849	251,714
Repair & Maintenance	189	1,232		122	1,543
Other Expenses	13,585	624,221		50,694	688,500
Total	<u>180,374</u>	<u>1,466,105</u>		<u>232,327</u>	<u>1,878,806</u>
Equipment & Intangible Assets					
Equipment	5,157	12,141		12,161	29,459
Total	<u>5,157</u>	<u>12,141</u>		<u>12,161</u>	<u>29,459</u>
Local Assistance					
From other sources			\$ 22,372,826		22,372,826
Total			<u>22,372,826</u>		<u>22,372,826</u>
Benefits & Claims					
To Individuals		925,614			925,614
From State Sources		8,808,997			8,808,997
Total		<u>9,734,611</u>			<u>9,734,611</u>
Transfers-out					
Fund transfers		11,304		3,317,525	3,328,829
Total		<u>11,304</u>		<u>3,317,525</u>	<u>3,328,829</u>
Total Expenditures & Transfers-Out	\$ <u>1,138,873</u>	\$ <u>14,111,692</u>	\$ <u>22,372,826</u>	\$ <u>3,942,357</u>	\$ <u>41,565,748</u>
<b>EXPENDITURES &amp; TRANSFERS-OUT BY FUND</b>					
General Fund			\$ 22,372,826		\$ 22,372,826
State Special Revenue Fund	\$ 1,138,873	\$ 13,518,869		\$ 3,942,357	\$ 18,600,099
Enterprise Fund		592,823			592,823
Total Expenditures & Transfers-Out	1,138,873	14,111,692	22,372,826	3,942,357	41,565,748
Less: Nonbudgeted Expenditures & Transfers-Out	(170)	611,637		3,329,547	3,941,014
Prior Year Expenditures & Transfers-Out Adjustments	2,033	(5,834)		123,126	119,325
Actual Budgeted Expenditures & Transfers-Out	1,137,010	13,505,889	22,372,826	489,684	37,505,409
Budget Authority	1,173,857	15,742,959	22,658,120	850,336	40,425,272
Unspent Budget Authority	\$ <u>36,847</u>	\$ <u>2,237,070</u>	\$ <u>285,294</u>	\$ <u>360,652</u>	\$ <u>2,919,863</u>
<b>UNSPENT BUDGET AUTHORITY BY FUND</b>					
General Fund			\$ 285,294		\$ 285,294
State Special Revenue Fund	\$ <u>36,847</u>	\$ <u>2,237,070</u>		\$ <u>360,652</u>	\$ <u>2,634,569</u>
Unspent Budget Authority	\$ <u>36,847</u>	\$ <u>2,237,070</u>	\$ <u>285,294</u>	\$ <u>360,652</u>	\$ <u>2,919,863</u>

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.

**State Auditor's Office**  
**Notes to the Financial Schedules**  
**For the Two Fiscal Years Ended June 30, 2010**

## **1. Summary of Significant Accounting Policies**

### **Basis of Accounting**

The office uses the modified accrual basis of accounting, as defined by state accounting policy, for its Governmental fund category (General, and State Special Revenue Funds). In applying the modified accrual basis, the office 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 office to record the cost of employees' annual and sick leave when used or paid.

The office uses accrual basis accounting for its Proprietary (Enterprise Fund) and Fiduciary (Agency Fund) fund categories. Under the accrual basis, as defined by state accounting policy, the office 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 office 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 office 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. The General Fund includes revenue for securities, premium insurance taxes; fines and penalties, and transfers in from the securities and captives state special revenue funds. The expenditures included in the general fund are transfers of funds to Montana Public

Employees' Retirement Administration and expenditures to each city or town that has a fire department relief association or a police department that is not a participant in the municipal police officers' retirement system.

- ♦ **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. Office State Special Revenue Funds include Insurance and Security Division activity, such as securities and insurance examination fees, insurance industry continuing education programs, Insure Montana activity, and securities portfolio registrations.

### **Proprietary Fund Category**

- ♦ **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 office Enterprise Fund includes activity related to an advisory surplus lines organization for the fiscal year 2009.

### **Fiduciary Fund Category**

- ♦ **Agency Fund** – to account for resources held by the state in a custodial capacity. The office's Agency Fund accounts for cash and securities required to be held in trust by the office for insurance companies licensed in Montana.

## **2. General Fund Balance**

The negative fund balance in the General Fund does not indicate overspent appropriation authority. The office has authority to pay obligations from the statewide General Fund within its appropriation limits. The office expends cash or other assets from the statewide fund when it pays General Fund obligations. The office'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, 2009, and June 30, 2010.

## **3. Direct Entries to Fund Balance**

Direct entries to fund balances in the General and Special Revenue funds include entries generated by SABHRS to reflect the flow of resources within individual funds shared by separate agencies. The material portion of direct entries to fund balance in the General Fund is attributed to Premium Insurance Taxes.

#### **4. Surplus Lines**

Until fiscal year 2010, the office contracted with Montana Surplus Lines Agents Association (MSLAA) to perform the regulatory and supervision duties of surplus lines, including Stamping Fees. During this time the activity was recorded in the Enterprise Fund. On July 1, 2009, the Commissioner of Securities and Insurance terminated the contract with MSLAA and the function was brought in-house. According to §33-2-321(5)(b), MCA, “If a surplus lines advisory organization is not operating as set forth in this section, the stamping fee may be collected by the commissioner and placed in a state special revenue account for the expenses of regulating surplus lines.” During fiscal year 2010, Surplus Lines activity was no longer recorded in the Enterprise Fund, but in the State Special Revenue Fund.

#### **5. Premium Tax Credit Carryover**

Annually the office conducts audits of premium insurance tax returns, which includes calculating premium tax credit carryovers. Insurance companies with an available credit carryover can either receive a refund or carry forward the credit to offset future premium tax obligations. As a result, since fiscal year 2000, credit carryovers were not recorded on the state’s accounting system, resulting in a \$2,574,190 fiscal year 2009 General Fund overstatement of cumulative Tax revenues. In fiscal year 2010 the office estimated the premium tax credit carryover to be \$2,882,919, which was appropriately recorded on the state’s accounting system.



STATE AUDITOR'S  
OFFICE

OFFICE RESPONSE



# COMMISSIONER OF SECURITIES & INSURANCE

B-1

MONICA J. LINDEEN  
COMMISSIONER



OFFICE OF THE MONTANA  
STATE AUDITOR

October 5, 2010

Ms. Tori Hunthausen  
Legislative Auditor  
Office of the Legislative Auditor  
State Capitol  
P.O. Box 201705  
Helena, Mt. 59620-1705

**RECEIVED**  
OCT 06 2010  
LEGISLATIVE AUDIT DIV.

Dear Ms. Hunthausen:

We have received your financial compliance audit for the two fiscal years ending June 30, 2010. Thank you for the opportunity to respond to the recommendations.

## Recommendation #1

We recommend the office implement internal controls to properly identify, capture, or exchange information in a form and time to prevent errors.

## Agency Response:

We concur with this recommendation. We are in the processes of updating the Internal Control Policy to include Communication Procedures between divisions and bureaus. The implementation of these procedures will result in more effective communication of information between divisions and bureaus which will result in the recording of more accurate financial and program information.

## Recommendation #2

We recommend the office:

- a. Collect security fees at class levels as required by state law.

## Agency Response:

We concur with this recommendation. Beginning January 1, 2011, investment company and similar issuers will be required to notice file or register securities at the class level. Procedures have been implemented to begin.

- b. Retain assets or securities in amounts that do not exceed deposit thresholds as required by state law

Ms. Tori Hunthausen  
Legislative Auditor  
Page Two  
October 5, 2010

Agency Response:

We concur with this recommendation. We are requesting a revision in the law to eliminate the thresholds on required deposits of assets or securities of an insurer.

We would like to thank your staff for their time and effort during the audit. They were very professional and helpful addressing the issues and pointing out areas that need improvement.

Sincerely,

A handwritten signature in cursive script, appearing to read "Monica J. Lindeen".

Monica J. Lindeen  
Commissioner of Securities & Insurance  
Office of the Montana State Auditor

