



A REPORT
TO THE
MONTANA
LEGISLATURE

FINANCIAL-COMPLIANCE AUDIT

Department of Military Affairs

*For the Two Fiscal Years Ended
June 30, 2014*

OCTOBER 2014

LEGISLATIVE AUDIT
DIVISION

14-25

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FINANCIAL-COMPLIANCE AUDITS

Financial-compliance audits are conducted by the Legislative Audit Division to determine whether an agency's financial operations are properly conducted, the financial reports are presented fairly, and the agency has complied with applicable laws and regulations. In performing the audit work, the audit staff uses standards set forth by the American Institute of Certified Public Accountants and the United States Government Accountability Office. Financial-compliance audit staff members hold degrees with an emphasis in accounting. Most staff members hold Certified Public Accountant (CPA) licenses.

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, 2013, was issued March 28, 2014. The Single Audit Report for the two fiscal years ended June 30, 2015, will be issued by March 31, 2016. Copies of the Single Audit Report can be obtained by contacting:

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Deborah F. Butler, Legal Counsel



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Cindy Jorgenson
Angus Maciver

October 2014

The Legislative Audit Committee
of the Montana State Legislature:

This is our financial-compliance audit report on the Department of Military Affairs (department) for the two fiscal years ended June 30, 2014. Included in this report are six recommendations related to internal controls, as well as noncompliance with state law, state accounting policy, and administrative rules.

This report includes the department's financial schedules. The financial schedule presentation is intended to provide the legislative body with information necessary for decision-making purposes; it is not intended to conform to the financial reporting requirements established in generally accepted accounting principles (GAAP). The financial schedule presentation has not changed, but audit reporting standards have changed. Auditing standards require us to clearly communicate that the financial schedule presentation is not intended to, and does not, conform to GAAP reporting requirements. The Independent Auditor's Report on page A-1 contains language to this effect in the section titled "Adverse Opinions on U.S. Generally Accepted Accounting Principles." This section does not imply the amounts presented on the department's financial schedules are not fairly stated. Page A-1 also communicates the extent to which the user can rely on the information contained in the financial schedules in the section titled "Qualified Opinions on Regulatory Basis of Accounting" and "Unmodified Opinions on Regulatory Basis of Accounting."

The department's written response to the audit recommendations is included in the audit report at page B-1. We have considered the non-concurring response to Recommendation #6 on page B-2. The department's physical training (PT) program policy states specifically, "The PT program is voluntary..." and the time for PT "...is a privilege." The Department of Military Affairs is not exempt from personnel administration requirements codified under Title 2, Chapter 18; therefore, state policy 202 applies. We maintain our position as reported.

We thank the Adjutant General and his staff for their cooperation and assistance throughout the audit.

Respectfully submitted,

/s/ Tori Hunthausen

Tori Hunthausen, CPA
Legislative Auditor

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APPOINTED AND ADMINISTRATIVE OFFICIALS

Department of Military Affairs

Major General Matthew T. Quinn, Adjutant General

Brad Livingston, Interim Administrator, Disaster and Emergency Services Division

Sundi West, Executive Operations Manager, Director's Office (as of September 2014)

Ed Tinsley, Administrator, Disaster and Emergency Services Division (through July 2014)

Jan Thomson-Rouse, Director, Youth Challenge Program

Wendy Fetcher, Director, Science, Technology, Academy, Reinforcing, Basic, Aviation, and Space Exploration Program (STARBASE)

Joe Foster, Administrator, Veterans Affairs Division

Dan Hubber, Army Facilities Deputy Director

Board of Veterans' Affairs Voting Members

		<u>Term Expires</u>
Bill Willing, Chair	Anaconda	08/01/15
Peter Olson, Vice Chair	Culbertson	08/01/16
Shawn Backbone	Crow Agency	08/01/17
David Boyd	Poplar	08/01/15
Bryon Erickson	Three Forks	08/01/18
Casey Jourdan	Billings	08/01/18
Ron Milam	Missoula	08/01/18
Clancy Sivertson	Belt	08/01/17
Gary Sorenson	Missoula	08/01/15
Brenda York	Belgrade	08/01/18

Nonvoting Members

		<u>Term Expires</u>
Dan Bernhardt	Helena	01/01/17
Trena Bonde	Ft. Harrison	08/01/18

Johnathon Kenneway	Great Falls	08/01/16
Bruce Knutson	Helena	08/01/16
Denny Lenoir	Helena	08/01/16
Matthew Quinn	Ft. Harriosn	01/01/17
Jason Smith	Helena	01/01/17
Kathy Swanson	Anaconda	08/01/18
Joren Underdahl	Columbia	08/01/18

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MONTANA LEGISLATIVE AUDIT DIVISION

FINANCIAL-COMPLIANCE AUDIT

Department of Military Affairs

For the Two Fiscal Years Ended June 30, 2014

OCTOBER 2014

14-25

REPORT SUMMARY

The Department of Military Affairs' operations are funded primarily by federal moneys. In fiscal year 2014, over \$54 million in federal funds were received and approximately \$9 million was spent towards construction of a new armory in Miles City.

Context

The Department of Military Affairs (department) is administered by the Adjutant General and his staff to provide for safety and well-being for citizens of Montana. This is accomplished through mission-ready forces for federal and state activations, emergency services as directed by the Governor, and services to Montana veterans. The department, through the Army and Air National Guard, manages a joint federal-state program to maintain trained and equipped military organizations available to the Governor, in the event of a state emergency, and the President, in the event of a national emergency. The department also manages and coordinates with state and federal agencies in providing services for veterans and their families and manages the state veterans' cemeteries. The department also administers programs such as the Montana National Guard Youth Challenge Program; the Montana Science, Technology, Academy, Reinforcing, Basic, Aviation and Space Exploration Program (STARBASE); the Montana Military Family Relief Fund; and the Montana Guard Scholarship Program.

The recommendation not implemented, related to expenditure accruals, is also a recommendation in this report. The current audit report also contains five other recommendations to the department.

During the audit we found the department is not in compliance with state laws, administrative rules, and policy. The state law is related to determining eligibility for and providing state reenlistment bonuses to National Guard members who meet the criteria outlined in law. We also found internal controls to be insufficient to detect and correct 29 misclassifications of expenses and for reimbursements made to 20 out of 23 subrecipients without evidence of a signed agreement. Furthermore, state accounting policy was not followed when Public Assistance Grants in the amount of \$6 million and \$3 million was recorded.

Results

The department had three recommendations in the prior audit report of which two were implemented and one was not implemented.

Recommendation Concurrence	
Concur	4
Partially Concur	1
Do Not Concur	1
Source: Agency audit response included in final report.	

For a complete copy of the report (14-25) or for further information, contact the Legislative Audit Division at 406-444-3122; e-mail to lad@mt.gov; or check the web site at <http://leg.mt.gov/audit>

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Call toll-free 1-800-222-4446, or e-mail ladhotline@mt.gov.

Chapter I – Introduction

Audit Scope

We performed a financial-compliance audit of the Department of Military Affairs (department) for the two fiscal years ended June 30, 2014. The objectives of the audit were to:

1. 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 improvements in management and internal controls of the department.
2. Determine department compliance with selected laws and regulations.
3. Determine the implementation status of prior audit recommendations.
4. Determine whether the financial schedules present fairly the results of operations and changes in fund equity of the department for each of the fiscal years ended June 30, 2014, and June 30, 2013.

To address objectives #1 and #4, we focused our audit efforts primarily on the federal grants received for the National Guard Military Operations and Maintenance Projects, Disaster Emergency Services, and Disaster Fund. We also tested transactions related to personal services and operating expenditures. This included understanding the department's internal control policies and procedures, performing analytical procedures, and reviewing accounting transactions. We addressed objective #2 by reviewing and testing compliance with state laws.

Auditing standards require us to communicate, in writing, deficiencies in internal control we identified as a result of audit objective #1 above and considered to be significant or material. A deficiency in internal control 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 material weakness is one or more deficiencies in internal control such that there is reasonable possibility that a material misstatement of the entity's financial schedules will not be prevented, or detected and corrected on a timely basis. A significant deficiency is one or more deficiencies in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Table 1 outlines the significant deficiency we identified during this audit.

Our consideration of internal control was not for the purpose of expressing an opinion on the effectiveness of internal

Table 1
Summary of Control Deficiencies

Subject	Type of Deficiency	Page
Internal Controls	Significant Deficiency	7

controls. Therefore, material weaknesses or significant deficiencies may exist that were not identified.

This report contains six recommendations to the department.

Background

The department, through the Army and Air National Guard, manages a joint federal-state program to maintain trained and equipped military organizations in readiness for state and national mobilizations to active duty. The department consists of the following functions and authorized full-time equivalent positions (FTE) for fiscal year 2013-14.

Montana National Guard is authorized approximately 87 FTE that are paid through the state's payroll system. The National Guard has a unique dual mission that consists of both Federal and State roles. The Governor can call the National Guard into action during local or statewide emergencies, such as storms, fires, earthquakes or civil disturbances. In addition, the President of the United States can activate the National Guard for participation in federal missions. The Montana National Guard has two programs – the Army National Guard and the Air National Guard.

The Army National Guard is one component of The Army (which consists of the Active Army, the Army National Guard and the Army Reserve). The Army National Guard is composed primarily of traditional Guardsmen – civilians who serve their country, state and community on a part-time basis.

The Air National Guard maintains units available for prompt mobilization during war and provides assistance during national emergencies. During peacetime, the combat-ready units and support units carry out missions compatible with training, mobilization readiness, humanitarian and contingency operations.

Military Capital Construction provides support to the Army and Air National Guard for the construction of military facilities, real property improvements, design services, and other projects authorized and directed by Congress or the Department of Defense.

Director's Office (formerly Centralized Services Division) (12 FTE) is the primary administrative support organization for the department and provides oversight for budgeting, fiscal management, payroll, human resource management, purchasing, property control, policy development and implementation, and assists with interpretation of rules, regulations and statutes for all programs within the department.

Disaster and Emergency Services Division (DES) (24 FTE) works with local, state, and federal officials to prepare, update, and coordinate emergency preparedness, response and recovery plans. This responsibility includes the administration and disbursement of federal homeland security and emergency management funds to eligible political subdivisions and tribal nations across the state. DES provides technical support for civil defense shelters, exercises, and radiological defense and monitoring. The division also receives, records, and disburses federal funds to eligible government entities.

Disaster Fund Program is administered by the department to provide assistance under an emergency or major disaster declaration. The department works with the Federal Emergency Management Agency and uses the funds to restore its own disaster-damaged facilities and to provide subgrants to local governments.

Montana National Guard Youth Challenge Program (61 FTE) is a 17-month, voluntary, two-phased military modeled training program targeting unemployed, drug-free, and crime-free youth ages 16 to 18 who have stopped attending secondary school before graduating. The program provides values, skills, education, and self-discipline in a quasi-military modeled training environment. Phase I of the program is a 22-week residential stay on the campus of University of Montana Western in Dillon focusing on physical training, classroom instruction, personal development, and life skills. Phase II is a year-long mentoring relationship with a specially-trained member of the community where the youth resides to provide a positive role model and to assist the student in gaining employment or enrolling in postsecondary schooling.

Veterans Affairs Division (30 FTE) manages and cooperates with state and federal agencies in providing statewide services for discharged veterans and their families. It promotes the general welfare of veterans and assists Montana's veterans and dependents in obtaining veterans benefits. The program also administers the veterans' cemeteries located at Miles City, Fort Harrison in Helena, and Missoula.

Montana STARBASE (Science, Technology, Academy, Reinforcing, Basic, Aviation, and Space Exploration) "Big Sky" Program (2 FTE) is for elementary school-aged children. Its goals include raising interest and improving the knowledge and skills of at-risk youth in math, science, and technology by exposing the students and their teachers to real world applications of math and science. The program uses positive role models found on military bases and installations to implement experimental learning, simulations, and experiments in aviation and space-related fields. The department has added a second location in Great Falls.

Montana Military Family Relief Fund provides monetary grants to families of Montana National Guard and Reserve Component members who meet the grant criteria. The grants are intended to help Montana families defray the costs of food, housing, utilities, medical services, and other expenses that become difficult to afford when a wage-earner has temporarily left civilian employment to be placed on active military duty.

Montana Guard Scholarship Program was established to assist in recruiting and retention efforts for the Montana National Guard. The program provides scholarships to eligible Montana National Guard personnel enrolled as undergraduate students at Montana colleges, universities, or in training programs.

Prior Audit Recommendations

The prior audit report for the two fiscal years ended June 30, 2012, contained three recommendations to the department.

The department implemented the recommendation to work with the federal Department of Homeland Security to ensure compliance with the Federal Transparency Act requirements in relation to the Public Assistance Grants. However, the department is still unable to report the sub-awards on the federal system due to technical issues with the federal system. Because the department continues to attempt to submit the required information, we have no further recommendation at this time.

The department also implemented the recommendation to comply with rules for recruitment and selection of employees to provide for equitable and consistent treatment of applicants.

The department did not implement the recommendation related to following control processes to ensure expenditure accrual transactions are recorded and supported in accordance with state accounting policy. This is further discussed on page 6.

Chapter II – Findings and Recommendations

Noncompliance with State Law

The department is not providing National Guard reenlistment bonuses to eligible members.

State law requires the Department of Military Affairs (department) to appoint a secretary to maintain records, establish rules, and to determine whether there are reenlisted National Guard members that are eligible for state bonuses. The department has not appointed a secretary to administer these laws. Furthermore, there has been no appropriation and no payments of state bonuses to eligible members during fiscal years 2013 and 2014. State laws also establish criteria regarding who is eligible for the bonuses. A member is not eligible for a state bonus if they are eligible for any federally funded National Guard bonus for reenlistment. During fiscal year 2014, 400 members of the National Guard reenlisted and 171 received a federal reenlistment bonus. According to state law, the secretary is tasked to determine whether there are any members meeting the criteria for a state bonus and set the amount of the bonus based on the appropriation for that purpose. The department is not in compliance with §10-1-804, 10-1-805, and 10-1-806, MCA.

Department staff stated the law was intended to encourage a greater number of extensions and reenlistments in the Montana National Guard. Furthermore, staff stated the use of federally funded bonuses and other incentives, such as the scholarship fund, make use of a state bonus unnecessary.

Until such time as it is not required by law, the department should appoint a secretary to administer the laws related to National Guard reenlistment bonuses. Depending on the number of eligible members, the cost to implement this law could be substantial.

RECOMMENDATION #1

We recommend the department comply with state law by:

- A. *Appointing a secretary to administer National Guard reenlistment bonuses.*
 - B. *Establishing rules to administer these laws.*
 - C. *Determining eligibility of members.*
 - D. *Implementing procedures to award reenlistment bonuses in accordance with state law.*
-

Accruals

The department did not accrue contract obligations in accordance with state accounting policy.

State accounting policy allows the department to accrue expenditures for commitments related to unperformed legally binding contracts as of the end of the fiscal year. There is separate accounting treatment for these obligations based on the date goods or services are received; before or after fiscal year-end. State accounting policy requires expenditure accruals to be supported by documentation and reviewed before they are recorded. We identified the following accounting errors where state accounting policy was not followed.

- ◆ At fiscal year-end, the Director's Office (DO) sends a letter to all divisions within the department requesting a list of the accruals along with the supporting documentation. In fiscal year 2013 and fiscal year 2014, accruals were approved by the DO without substantiating documentation that the accrual met valid obligation criteria and identifying when the services were received. These accruals totaled \$3,214,926 in fiscal year 2013 and \$1,532,019 in fiscal year 2014. Lack of training resulted in the accrual classification errors according to department personnel.
- ◆ The department was awarded Public Assistance Grants in 2011 and recorded an accrual for the moneys in fiscal year 2012 and fiscal year 2013. However, the department did not record the accrual for the Public Assistance Grants in fiscal year 2014. By not recording the accrual, the expenditures are understated by \$6,436,240 in the federal special revenue fund and by \$3,569,159 in the General Fund. This misstatement led to the modified opinion on page A-1. Department staff stated there was staff turnover and recording this accrual was overlooked.

RECOMMENDATION #2

We recommend the department ensure expenditure accrual transactions are supported and recorded in accordance with state accounting policy.

Recruitment and Selection Rules

The department is not following administrative rules for the recruiting and selection of employees.

State administrative rules require the department to document certain information during the recruitment and selection of employees. This documentation includes the

names and titles of the persons who participated in the design or administration of the selection procedures and a statement of why and how the hiring decision was made. During the audit we reviewed the files of employees hired during fiscal years 2013 and 2014. Of the five files reviewed, two files did not include this required documentation. Lack of this documentation can lead to questions of whether the process was followed and whether the most qualified candidate was selected for the position. Department staff stated they were uncertain as to why the documentation was not in the recruitment files. The department should have processes in place to ensure that administrative rules are followed.

RECOMMENDATION #3

We recommend the department comply with administrative rules governing documentation requirements for recruitment and selection of employees.

Internal Control Deficiencies

Section 17-1-102(4), MCA, requires the department to input all necessary transactions before the end of the fiscal year to present the receipt, use, and disposition of all money and property, for which it is accountable, in accordance with generally accepted accounting principles (GAAP). The Department of Administration develops and establishes state accounting policy to implement this statute. State accounting policy also requires agencies to implement internal control procedures to ensure all transactions necessary for compliance with GAAP are recorded in the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) before fiscal year-end.

The following items describe instances where, due to internal control deficiencies, the department recorded transactions that did not comply with state law or state accounting policy.

Accounting Misclassifications

The department does not have an adequate internal control process to detect and correct accounting misclassifications.

State accounting policy establishes the categories of expenses and accounts that are to be used for financial reporting. During the audit, we identified 29 instances of misclassifications in expense accounts or funds. These misclassifications led to

misstatements totaling \$977,081 between expense categories. Of this total, \$950,068 was related to payments made on behalf of cities and counties by the state to the vendor. These funds are usually sent directly to the cities and counties. These expenses were recorded as Repairs & Maintenance expenses when accrued, and recorded as Grants from Federal Sources when paid. This misclassification led to a negative balance on the fiscal year 2013 Schedule of Total Expenditures & Transfers-Out for Repairs & Maintenance. Department staff stated the coding was entered as written on the invoice and in other cases it was entered incorrectly.

The accounting entry errors that occurred during the audit period indicate there is a significant deficiency in the department's internal controls as the review procedures are not sufficient to prevent or detect and correct accounting errors in a timely manner.

RECOMMENDATION #4

We recommend the department strengthen the internal control process to improve review procedures over transactions to ensure compliance with state accounting policy.

Reimbursement Without Evidence of a Signed Agreement

Internal controls did not detect or prevent reimbursements from being paid to subrecipients without a signed grant award agreement.

The department receives financial assistance from the federal government to support activities to prepare for and respond to terrorist acts, which includes purchasing equipment and provisions for training first responders. The department spent approximately \$12 million during fiscal years 2013 and 2014 from these Homeland Security grant funds.

Department policy states that the Homeland Security agreements are not fully executed until a signed copy of both the award agreement and the policies and procedures agreement are received and that all of the required signatures are obtained. It further states that a subrecipient cannot spend funds without a signed grant award agreement.

The grant award agreements are contracts between the Disaster and Emergency Services Division and the subrecipient which not only specify the amount awarded, but the terms and conditions applicable to the grant for the approved project. During the audit we reviewed 23 files for subrecipients receiving funds in fiscal year 2013 and

fiscal year 2014. Of the 23, there were 20 files related to the 2011 Homeland Security grant that did not have evidence of a signed grant award agreement. Department staff stated there was turnover in the position and they were unable to locate the signed agreements.

The department should follow established internal control policies to obtain signed grant award agreements to ensure the reimbursements are within the scope of those agreements.

RECOMMENDATION #5

We recommend the department follow established internal control policies to obtain signed grant award agreements for Homeland Security grants before reimbursement of funds to sub-recipients.

Exercise Time As Paid Work Time

The department is paying for exercise time as paid work time activities contrary to administrative rule and policy.

The department has a voluntary Physical Training Policy (PT) that allows its employees to exercise up to three hours per week and to record it as regular compensable time. The benefit is optional and meant to be a privilege for the state employees of the department. Out of the 216 state employees at the department, there are 24 currently benefiting from the privilege, which equates up to 3,744 hours per year of time paid for hours not worked. This is equivalent to more than one full-time employee.

The policy states the exercise will be performed in established exercise facilities at the base, unless an exception is granted. State administrative rule recognizes that break periods, running from 5 to about 20 minutes, are common to promote the efficiency of the employee and are customarily paid for as working time. This voluntary physical training time is in addition to a customary break. Exercise time is not separately identifiable when recorded on the time and attendance record. Each employee is responsible to ensure the activity does not extend beyond the three hours per week of official time. There is a roster maintained by the supervisor of the employees participating, however, the department does not track this time and does not have procedures in place to monitor this activity unless the employee is exercising off base.

While department staff indicate the optional privilege creates equity between the federal and state employees working at the department, it creates an inequity issue among Executive Branch employees. Furthermore, the federal employees are required to pass a physical fitness test; the state employees are not. For the 24 state employees who are currently participating, physical training is not required for the principal duties which the individuals are employed to perform. For example, one employee's job profile lists such duties for the job's overall purpose as being responsible for managing office administrative activities; providing support for division operations; monitoring and processing division budget, fiscal, and accounting activities; and other related responsibilities.

State human resource policy, which covers department employees, allows managers to offer paid time during working hours to employees who attend trainings and events sponsored by the Health Care Benefits Division. These events include benefit training, benefit presentations, health screenings, webinars, and wellness services. The policy specifically excludes "anything not listed in the policy, such as Spring Fitness, Hunter's Challenge, Healthy for Life programs, and Weight Management programs." The department's policy is not in compliance with this policy, as this activity is on the employee's own time. The department's policy extends the benefit beyond state policy.

RECOMMENDATION #6

We recommend the department pay work time within the boundaries of state administrative rule and policy.

Independent Auditor's Report and Department Financial Schedules

LEGISLATIVE AUDIT DIVISION

Tori Hunthausen, Legislative Auditor
Deborah F. Butler, Legal Counsel



Deputy Legislative Auditors:
Cindy Jorgenson
Angus Maciver

INDEPENDENT AUDITOR'S REPORT

The Legislative Audit Committee
of the Montana State Legislature:

Introduction

We have audited the accompanying Schedules of Changes in Fund Equity, Schedules of Total Revenues & Transfers-In, and Schedules of Total Expenditures & Transfers-Out of the Department of Military Affairs for each of the fiscal years ended June 30, 2014, and 2013, and the related notes to the financial schedules.

Management's Responsibility for the Financial Schedules

Management is responsible for the preparation and fair presentation of these financial schedules in accordance with the regulatory format prescribed by the Legislative Audit Committee, based on the transactions posted to the state's accounting system without adjustment; this responsibility includes recording transactions in accordance with state accounting policy; and designing, implementing, and maintaining internal controls relevant to the preparation and fair presentation of the financial schedules that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

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 from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial schedules. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial schedules, whether due to fraud or error. In making those risk assessments, the auditor considers internal controls relevant to the department's preparation and fair presentation of the financial schedules in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the department's internal control, and accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as the overall presentation of the financial schedules.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

Basis for Adverse Opinions on U.S. Generally Accepted Accounting Principles

As described in Note 1, the financial schedules are prepared from the transactions posted to the state's primary accounting system without adjustment, in the regulatory format prescribed by the Legislative Audit Committee. This is a basis of accounting other than accounting principles generally accepted in the United States of America. The financial schedules are not intended to, and do not, report assets and liabilities.

The effects on the financial schedules of the variances between the regulatory basis of accounting described in Note 1 and accounting principles generally accepted in the United States of America, although not reasonably determinable, are presumed to be material.

Adverse Opinions on U.S. Generally Accepted Accounting Principles

In our opinion, because of the significance of the matter discussed in the "Basis for Adverse Opinions on U.S. Generally Accepted Accounting Principles" paragraph, the financial schedules referred to above do not present fairly, in accordance with accounting principles generally accepted in the United States of America, the financial position of the department as of June 30, 2014, and June 30, 2013, or changes in financial position for the years then ended.

Basis for Qualified Opinions on Regulatory Basis of Accounting

The department did not record activity for valid expenditure obligations in fiscal year 2014, as required by state accounting policy. The error resulted in the following misstatements in the financial schedules:

FY2014 Schedule	Program/Fund	Account Line	Over (under) Stated
Schedule of Total Expenditures & Transfers-Out	Disaster Fund	Grants from State Sources	(3,569,159)
Schedule of Total Expenditures & Transfers-Out	Disaster Fund	Grants from Federal Sources	(6,436,240)
Schedule of Total Expenditures & Transfers-Out	Disaster Fund	Prior Year Expenditures & Transfers-Out Adjustment	(10,005,399)
Schedule of Changes in Fund Equity	General Fund	Prior Year Expenditures & Transfers-Out Adjustment	(3,569,159)
Schedule of Changes in Fund Equity	Federal Special Revenue Fund	Prior Year Expenditures & Transfers-Out Adjustment	(6,436,240)

Qualified Opinions on Regulatory Basis of Accounting

In our opinion, except for the effects of the matter described in the "Basis for Qualified Opinions on Regulatory Basis of Accounting" paragraph, the Schedule of Changes in Fund Equity and Schedule

of Total Expenditures & Transfers-Out for the fiscal year ended June 30, 2014, present fairly, in all material respects, the results of operations and changes in fund equity of the Department of Military Affairs for the year then ended, in conformity with the basis of accounting described in Note 1.

Unmodified Opinions on Regulatory Basis of Accounting

In our opinion, the Schedule of Changes in Fund Equity, Schedule of Total Revenues & Transfers-In, and Schedule of Total Expenditures & Transfers-Out for the fiscal year ended June 30, 2013, and the Schedule of Total Revenues & Transfers-In for the fiscal year ended June 30, 2014, present fairly, in all material respects, the results of operations and changes in fund equity of the Department of Military Affairs for each of the fiscal years then ended, in conformity with the basis of accounting described in Note 1.

Respectfully submitted,

/s/ Cindy Jorgenson

Cindy Jorgenson, CPA
Deputy Legislative Auditor
Helena, MT

August 27, 2014

DEPARTMENT OF MILITARY AFFAIRS
SCHEDULE OF CHANGES IN FUND EQUITY
FOR THE FISCAL YEAR ENDED JUNE 30, 2014

FUND EQUITY: July 1, 2013					
	General	State Special	Federal Special	Capital	
	Fund	Revenue Fund	Revenue Fund	Projects Fund	
	\$ (4,568,800)	\$ 959,590	\$ (14,830,858)	\$ 0	
ADDITIONS					
Budgeted Revenues & Transfers-In	1,137	1,124,949	55,073,597	10,250,734	
Nonbudgeted Revenues & Transfers-In		140,549	26,602		
Prior Year Revenues & Transfers-In Adjustments	28	26,951	(869,171)		
Direct Entries to Fund Equity	7,722,519	499,065	(461,404)		
Total Additions	<u>7,723,685</u>	<u>1,791,514</u>	<u>53,769,625</u>	<u>10,250,734</u>	
REDUCTIONS					
Budgeted Expenditures & Transfers-Out	6,423,979	1,545,500	58,494,937	10,728,408	
Nonbudgeted Expenditures & Transfers-Out	(2,619)	(813)			
Prior Year Expenditures & Transfers-Out Adjustments	(2,786,641)	4,499	(10,513,575)		
Total Reductions	<u>3,634,718</u>	<u>1,549,187</u>	<u>47,981,361</u>	<u>10,728,408</u>	
FUND EQUITY: June 30, 2014	\$ (479,833)	\$ 1,201,917	\$ (9,042,595)	\$ (477,673)	

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-11.

DEPARTMENT OF MILITARY AFFAIRS
SCHEDULE OF CHANGES IN FUND EQUITY
FOR THE FISCAL YEAR ENDED JUNE 30, 2013

	General Fund	State Special Revenue Fund	Federal Special Revenue Fund	Capital Projects Fund
FUND EQUITY: July 1, 2012	\$ (5,593,015)	\$ 1,048,950	\$ (21,514,692)	\$ 0
ADDITIONS				
Budgeted Revenues & Transfers-In	1,906	964,842	47,146,095	143,878
Nonbudgeted Revenues & Transfers-In		3,577		
Prior Year Revenues & Transfers-In Adjustments		6,290	(890,506)	
Direct Entries to Fund Equity	6,931,923	116,076	(523)	
Total Additions	6,933,829	1,090,786	46,255,067	143,878
REDUCTIONS				
Budgeted Expenditures & Transfers-Out	5,878,616	1,160,435	39,445,233	143,878
Nonbudgeted Expenditures & Transfers-Out	(1,592)	(693)	(346)	
Prior Year Expenditures & Transfers-Out Adjustments	32,589	20,405	126,346	
Total Reductions	5,909,614	1,180,146	39,571,233	143,878
FUND EQUITY: June 30, 2013	\$ (4,568,800)	\$ 959,590	\$ (14,830,858)	\$ 0

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-11.

DEPARTMENT OF MILITARY AFFAIRS
SCHEDULE OF TOTAL REVENUES & TRANSFERS-IN
FOR THE FISCAL YEAR ENDED JUNE 30, 2014

TOTAL REVENUES & TRANSFERS-IN BY CLASS						
	General Fund	State Special Revenue Fund	Federal Special Revenue Fund	Capital Projects Fund	Total	
Taxes						
Charges for Services	\$ 1,165	\$	\$ 26,155	\$	\$	26,155
Investment Earnings		261,653	1,887			264,705
Rentals, Leases and Royalties		695				695
Grants, Contracts, and Donations		420				420
Transfers-in		149,703				149,703
Federal Indirect Cost Recoveries		879,979	192,252	10,250,734		11,322,965
Federal			10,417			10,417
Total Revenues & Transfers-In	1,165	1,292,449	54,000,316			54,000,316
Less: Nonbudgeted Revenues & Transfers-In		54,231,028		10,250,734		65,775,377
Prior Year Revenues & Transfers-In Adjustments		140,549	26,602			167,151
Actual Budgeted Revenues & Transfers-In	28	26,951	(869,171)			(842,191)
Estimated Revenues & Transfers-In	1,137	1,124,949	55,073,597	10,250,734		66,450,417
Budgeted Revenues & Transfers-In Over (Under) Estimated	1,138	1,124,955	55,073,603	10,250,735		66,450,431
	<u>(1)</u>	<u>(6)</u>	<u>(6)</u>	<u>(1)</u>		<u>(14)</u>
	\$	\$	\$	\$		\$
BUDGETED REVENUES & TRANSFERS-IN OVER (UNDER) ESTIMATED BY CLASS						
Taxes	\$ (1)			\$		(1)
Charges for Services			(2)			(5)
Investment Earnings		(3)				(1)
Rentals, Leases and Royalties		(1)				(1)
Grants, Contracts, and Donations		(1)				(1)
Transfers-in		(1)	(1)	(1)		(2)
Federal Indirect Cost Recoveries			(0)			(0)
Federal			(3)			(3)
Budgeted Revenues & Transfers-In Over (Under) Estimated	<u>(1)</u>	<u>(6)</u>	<u>(6)</u>	<u>(1)</u>		<u>(14)</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-11.

DEPARTMENT OF MILITARY AFFAIRS
SCHEDULE OF TOTAL REVENUES & TRANSFERS-IN
FOR THE FISCAL YEAR ENDED JUNE 30, 2013

TOTAL REVENUES & TRANSFERS-IN BY CLASS

	General Fund	State Special Revenue Fund	Federal Special Revenue Fund	Capital Projects Fund	Total
Taxes					
Charges for Services	\$ 1,896	\$ 269,253	1,784	\$	1,784
Investment Earnings		1,283	2,335		273,483
Sale of Documents, Merchandise and Property	11		1,681		1,283
Rentals, Leases and Royalties		610			1,692
Grants, Contracts, and Donations		12,876			610
Transfers-in		690,687	140,626	143,878	12,876
Federal Indirect Cost Recoveries			57,481		975,191
Federal			46,051,682		57,481
Total Revenues & Transfers-In	1,906	974,710	46,255,589	143,878	46,051,682
Less: Nonbudgeted Revenues & Transfers-In		3,577			47,376,083
Prior Year Revenues & Transfers-In Adjustments		6,290	(890,506)		3,577
Actual Budgeted Revenues & Transfers-In	1,906	964,842	47,146,095	143,878	(884,216)
Estimated Revenues & Transfers-In	1,907	844,067	47,146,083	143,878	48,256,722
Budgeted Revenues & Transfers-In Over (Under) Estimated	\$ (1)	\$ 120,775	\$ 12	\$ 0	48,135,935
					\$ 120,786

BUDGETED REVENUES & TRANSFERS-IN OVER (UNDER) ESTIMATED BY CLASS

Charges for Services	\$	(2)	\$ 17	\$	15
Investment Earnings		(1)			(1)
Sale of Documents, Merchandise and Property					(1)
Rentals, Leases and Royalties		(10)			(10)
Grants, Contracts, and Donations					
Transfers-in		120,788	(1)		120,787
Federal Indirect Cost Recoveries					
Federal			(4)		(4)
Budgeted Revenues & Transfers-In Over (Under) Estimated	\$ (1)	\$ 120,775	\$ 12	\$ 0	\$ 120,786

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-11.

DEPARTMENT OF MILITARY AFFAIRS
SCHEDULE OF TOTAL EXPENDITURES & TRANSFERS-OUT
FOR THE FISCAL YEAR ENDED JUNE 30, 2014

	Air National Guard Program	Army National Guard Program	Challenge Program	Director's Office	Disaster & Emergency Services	Disaster Fund	Military Capital Construction	Montana Military Family Relief Fund	Scholarship Program	Starbase	Veterans Affairs Program	Total
PROGRAM (ORG) EXPENDITURES & TRANSFERS-OUT												
Personal Services												
Salaries	\$ 1,905,233	\$ 2,208,836	\$ 1,781,184	\$ 643,762	\$ 1,147,175	\$ 301,829				\$ 147,328	\$ 1,189,000	\$ 9,324,347
Hourly Wages		406										406
Other Compensation	5,976		3,895		6							9,878
Employee Benefits	781,607	771,187	753,819	196,780	408,014	52,185				50,561	472,123	3,486,275
Total	2,692,817	2,980,429	2,538,898	840,542	1,555,195	354,014				197,888	1,661,123	12,820,905
Operating Expenses												
Other Services	697,439	11,112,504	612,862	51,679	39,709	101,779	\$ 87,399			108,212	(66,798)	12,744,786
Supplies & Materials	164,913	305,453	205,561	14,289	159,008	1,047				27,701	95,952	973,923
Communications		225,214	36,222	12,320	38,807	82	80			2,840	37,608	353,173
Travel	8,122	64,709	29,131	7,717	119,259	39,668				2,405	31,316	302,326
Rent	70	342,729	350,927		2,389					1,849	50,126	748,090
Utilities	697,208	2,179,020	2,059								18,409	2,896,697
Repair & Maintenance	51,790	4,746,372	9,239		5,347		886,112			1,763	17,114	5,717,736
Other Expenses	15,990	37,192	97,378	13,353	74,134	8,922			\$ 179,854	1,465	11,476	439,763
Goods Purchased For Resale		140		234								374
Total	1,635,532	19,013,333	1,343,378	99,592	438,654	151,498	973,592		179,854	146,234	195,202	24,176,868
Equipment & Intangible Assets												
Equipment		288,574			22,180							310,755
Total		288,574			22,180							310,755
Capital Outlay												
Buildings							10,856,358				1,147,067	12,003,424
Other Improvements							751					751
Total							10,857,108				1,147,067	12,004,175
Grants												
From State Sources					295,793	(2,197,120)		\$ 28,250			180,000	(1,693,077)
From Federal Sources					11,984,858	(7,462,962)						4,521,896
Total					12,280,651	(9,660,083)		28,250			180,000	2,828,819
Benefits & Claims												
To Individuals				2,280								2,280
Total				2,280								2,280
Transfers-out												
Fund transfers					1,419,354	79,783	9,128,971				1,121,763	11,749,872
Total					1,419,354	79,783	9,128,971				1,121,763	11,749,872
Total Expenditures & Transfers-Out	\$ 4,328,349	\$ 22,282,336	\$ 3,882,276	\$ 942,414	\$ 15,716,034	\$ (9,074,787)	\$ 20,959,671	\$ 28,250	\$ 179,854	\$ 344,122	\$ 4,305,154	\$ 63,893,674
EXPENDITURES & TRANSFERS-OUT BY FUND												
General Fund	\$ 364,261	\$ 1,614,286	\$ 799,460	\$ 601,409	\$ 1,180,249	\$ (2,205,726)			\$ 179,854		\$ 1,100,925	\$ 3,634,718
State Special Revenue Fund		420			78,352	513,259		\$ 28,250			928,906	1,549,187
Federal Special Revenue Fund	3,964,088	20,667,629	3,082,816	341,005	14,457,433	(7,382,320)	\$ 11,353,027			\$ 344,122	1,153,560	47,981,361
Capital Projects Fund							9,606,644				1,121,763	10,728,408
Total Expenditures & Transfers-Out	4,328,349	22,282,336	3,882,276	942,414	15,716,034	(9,074,787)	20,959,671	28,250	179,854	344,122	4,305,154	63,893,674
Less: Nonbudgeted Expenditures & Transfers-Out		(238)	(850)	(270)	(434)	(319)					(1,322)	(3,432)
Prior Year Expenditures & Transfers-Out Adjustments	(17,885)	(13,542)	(156)		(204,160)	(13,024,081)			(35,555)		(340)	(13,295,717)
Actual Budgeted Expenditures & Transfers-Out	4,346,234	22,296,115	3,883,282	942,684	15,920,628	3,949,613	20,959,671	28,250	215,408	344,122	4,306,816	77,192,823
Budget Authority	4,609,597	22,511,579	3,956,659	1,129,498	27,916,588	5,624,368	69,872,349	121,012	215,409	719,460	5,454,905	142,131,426
Unspent Budget Authority	\$ 263,363	\$ 215,464	\$ 73,378	\$ 186,814	\$ 11,995,960	\$ 1,674,754	\$ 48,912,678	\$ 92,762	\$ 1	\$ 375,338	\$ 1,148,089	\$ 64,938,602
UNSPENT BUDGET AUTHORITY BY FUND												
General Fund	\$ 34,629	\$ 10,412	\$ 70,506	\$ 119,959	\$ 44,983	\$ 490,920			\$ 1		\$ 47,315	\$ 818,725
State Special Revenue Fund		1,580			159,685	40		\$ 92,762			1,018,521	1,272,588
Federal Special Revenue Fund	228,734	203,472	2,871	66,855	11,791,292	1,183,794	\$ 45,040,505			\$ 375,338	51,480	58,944,342
Capital Projects Fund							3,872,173				30,773	3,902,946
Unspent Budget Authority	\$ 263,363	\$ 215,464	\$ 73,378	\$ 186,814	\$ 11,995,960	\$ 1,674,754	\$ 48,912,678	\$ 92,762	\$ 1	\$ 375,338	\$ 1,148,089	\$ 64,938,602

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Additional information is provided in the notes to the financial schedules beginning on page A-11.

DEPARTMENT OF MILITARY AFFAIRS
SCHEDULE OF TOTAL EXPENDITURES & TRANSFERS-OUT
FOR THE FISCAL YEAR ENDED JUNE 30, 2013

PROGRAM (ORG) EXPENDITURES & TRANSFERS-OUT	Air National Guard Program	Army National Guard Program	Centralized Services Division	Challenge Program	Disaster & Emergency Services	Disaster Fund	Military Capital Construction	Montana Military Family Relief Fund	Scholarship Program	Starbase	Veterans Affairs Program	Total
Personal Services												
Salaries	\$ 1,936,404	\$ 2,101,647	\$ 689,165	\$ 1,718,028	\$ 1,173,261	\$ 45,327				\$ 160,929	\$ 1,151,275	\$ 8,976,037
Hourly Wages	106											106
Other Compensation				2,194								2,194
Employee Benefits	795,542	717,437	202,859	717,137	426,470	3,518				52,277	437,638	3,352,877
Total	2,732,052	2,819,084	892,025	2,437,358	1,599,731	48,844				213,206	1,588,914	12,331,213
Operating Expenses												
Other Services	750,481	3,028,966	57,817	539,155	303,209	19,903	\$ 16,393			303,933	24,867	5,044,724
Supplies & Materials	212,053	995,273	21,390	173,354	85,706					76,672	55,354	1,619,803
Communications		255,637	13,182	63,687	79,190		470			3,511	43,869	459,546
Travel	1,701	135,183	6,500	47,951	141,139	8,865				12,646	21,818	375,803
Rent	2,191	297,973		345,694	1,860						67,184	714,902
Utilities	663,578	2,002,494	35	5,020	224						15,522	2,686,873
Repair & Maintenance	114,358	4,254,108		10,912	(949,688)	4,425	308,622			3,663	25,982	3,772,383
Other Expenses	4,208	69,729	17,456	91,918	80,772	763			\$ 209,407	2,126	8,014	484,392
Goods Purchased For Resale		3,296										3,296
Total	1,748,570	11,042,658	116,380	1,277,690	(257,587)	33,957	325,485		209,407	402,551	262,611	15,161,721
Equipment & Intangible Assets												
Equipment		209,917			16,914							226,831
Intangible Assets		11,790										11,790
Total		221,707			16,914							238,621
Capital Outlay												
Land & Interest In Land											51,964	51,964
Buildings							1,361,522				488,059	1,849,581
Other Improvements							232					232
Total							1,361,754				540,023	1,901,777
Grants												
From State Sources					338,807	28,515		\$ 95,000				462,322
From Federal Sources					13,488,204	871,731						14,359,935
Total					13,827,012	900,245		95,000				14,822,257
Benefits & Claims												
To Individuals			2,470									2,470
Total			2,470									2,470
Transfers-out												
Fund transfers			1,162		1,844,632	357,140	91,914				51,964	2,346,812
Total			1,162		1,844,632	357,140	91,914				51,964	2,346,812
Total Expenditures & Transfers-Out	\$ 4,480,622	\$ 14,083,449	\$ 1,012,036	\$ 3,715,049	\$ 17,030,701	\$ 1,340,186	\$ 1,779,153	\$ 95,000	\$ 209,407	\$ 615,757	\$ 2,443,512	\$ 46,804,871
EXPENDITURES & TRANSFERS-OUT BY FUND												
General Fund	\$ 380,955	\$ 1,721,052	\$ 641,852	\$ 933,799	\$ 1,048,934	\$ 90,083			\$ 209,407		\$ 883,532	\$ 5,909,614
State Special Revenue Fund		1,740			82,171	759		\$ 95,000			1,000,477	1,180,146
Federal Special Revenue Fund	4,099,667	12,360,657	370,185	2,781,250	15,899,596	1,249,344	\$ 1,687,239			\$ 615,757	507,539	39,571,233
Capital Projects Fund							91,914				51,964	143,878
Total Expenditures & Transfers-Out	4,480,622	14,083,449	1,012,036	3,715,049	17,030,701	1,340,186	1,779,153	95,000	209,407	615,757	2,443,512	46,804,871
Less: Nonbudgeted Expenditures & Transfers-Out	(115)	(291)	(231)	(574)	(428)					(4)	(988)	(2,631)
Prior Year Expenditures & Transfers-Out Adjustments	9,364	1,685		2,675	148,098	17,601		(1,500)		834	584	179,340
Actual Budgeted Expenditures & Transfers-Out	4,471,373	14,082,055	1,012,267	3,712,948	16,883,031	1,322,585	1,779,153	96,500	209,407	614,927	2,443,915	46,628,162
Budget Authority	4,545,277	14,257,843	1,092,371	3,832,492	34,267,728	2,221,798	89,866,653	250,000	209,408	666,146	5,562,440	156,772,157
Unspent Budget Authority	\$ 73,904	\$ 175,788	\$ 80,104	\$ 119,544	\$ 17,384,697	\$ 899,213	\$ 88,087,500	\$ 153,500	\$ 1	\$ 51,219	\$ 3,118,525	\$ 110,143,995
UNSPENT BUDGET AUTHORITY BY FUND												
General Fund	\$ 3,902	\$ 19,087	\$ 21,082	\$ 858	\$ 47,260	\$ 394,454			\$ 1		\$ 682	\$ 487,326
State Special Revenue Fund		3,260			289,349	4,863		\$ 153,500			760,266	1,211,238
Federal Special Revenue Fund	70,002	153,440	59,021	118,686	17,048,089	499,895	\$ 64,238,115		\$ 51,219		1,205,040	83,443,509
Capital Projects Fund							23,849,385				1,152,536	25,001,921
Unspent Budget Authority	\$ 73,904	\$ 175,788	\$ 80,104	\$ 119,544	\$ 17,384,697	\$ 899,213	\$ 88,087,500	\$ 153,500	\$ 1	\$ 51,219	\$ 3,118,525	\$ 110,143,995

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-11.

Department of Military Affairs

Notes to the Financial Schedules

For the Two Fiscal Years Ended June 30, 2014

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 and Capital Projects). 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.

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 was adopted by 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 Veterans Affairs, Veterans Cemeteries, the Military Family Relief Fund, Armory Rental and Disaster and Emergency Services.
- ♦ **Federal Special Revenue Fund** – to account for activities funded from federal revenue sources. Department Federal Special Revenue Funds include Homeland Security, National Guard, and Military Capital Construction.

- ♦ **Capital Projects Fund** – to account for financial resources used for the acquisition or construction of major capital facilities, other than those financed by proprietary funds or trust funds. The department uses this fund for construction related to the Army National Guard and Veteran's Cemeteries.

2. General Fund Equity Balance

The negative fund equity 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, 2013, and June 30, 2014.

3. Direct Entries to Fund Equity and Prior Period Adjustments

Direct entries to fund equity in the General, Special Revenue, and Federal Special Revenue Fund, funds include entries generated by SABHRS to reflect the flow of resources within individual funds shared by separate agencies.

Prior year expenditures in the general fund and federal funds show an increase from other fiscal years due to 2011 flood expenditures. The flood event happened at the end of state fiscal year 2011, but the extent of the damage and expenditure estimates could not be established until fiscal year 2012, and is ongoing causing higher than normal prior year expenditures. The reason the Prior Year Expenditures& Transfers-Out Adjustments line in the Schedule of Changes in Fund Equity is due to the non-accrual explained below.

The department has been recording the approved grant amount for the spring floods of 2011 as an accrual since the inception of the grant. There is approximately \$11 million of grant monies remaining (\$6,436,240 in fund 03022 and \$3,569,159 in fund 01100) and an A Accrual was not recorded in FY2014.

DEPARTMENT OF MILITARY
AFFAIRS

DEPARTMENT RESPONSE

DEPARTMENT OF MILITARY AFFAIRS



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GOVERNOR

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October 24, 2014

Tori Hunthausen
Legislative Auditor
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Helena, MT 59620-1705

RECEIVED

OCT 27 2014

LEGISLATIVE AUDIT DIV.

Dear Ms. Hunthausen,

In reply to the Financial Compliance Audit Report received by this office October 17, 2014 we are submitting the following comments:

Recommendation #1:

We partially concur with your recommendation. This law has been on the books since 1983 and has not been funded/utilized since 1985. Since 9/11, federal reenlistment dollars (averaging between \$10-15k), and the desire of Soldiers and Airmen to serve their state and nation, have made the need for a state reenlistment bonus unnecessary. We still believe that to be the case. However, since the audit determined we are not in compliance with this law, we will appoint a secretary to maintain records, establish rules, and determine the need for state reenlistment bonuses for eligible National Guard members until such time it is no longer in violation of the strict letter of the law. The department will work on an amendment to the Reenlistment Bonus Program statute to update the legislative language this session to bring it more closely in alignment with current Montana National Guard configuration and needs. The department will be in compliance with this recommendation no later than January 1, 2015.

Recommendation #2:

We concur with your recommendation. The department will ensure that expenditure accrual transactions are supported and recorded in accordance with state accounting policy. In addition, the department will have a written procedure in place on the methodology necessary to perform accruals in a manner that is in accordance with state accounting policy. The department will be in compliance with this recommendation no later than January 1, 2015.

Recommendation #3:

We concur with your recommendation. The department will comply with administrative rules governing documentation requirements for recruitment and selection of employees. In addition, the department will hire a new Human Resource specialist, who will review our documentation and may initiate changes to our policies and procedures to ensure we are in accordance with administrative rules. The department will be in compliance with this recommendation no later than January 1, 2015.

Recommendation #4:

We concur with your recommendation. The department will strengthen the internal controls process to improve review procedures over transactions to ensure compliance with state accounting policy. In addition, the department will hire a Quality Assurance Specialist that will audit the department programs for compliance with state accounting policy and improve the department's internal control processes. The department will be in compliance with this recommendation no later than January 1, 2015.

Recommendation #5:

We concur with your recommendation and believe we are currently in compliance. The department will follow established internal control policies to obtain signed grant award agreements for Homeland Security grants before reimbursement of funds to sub-recipients. The grant audited was from 2011 fiscal years and changes have been already put in place to ensure all 2014 award agreements are fully executed.

Recommendation #6:

We do not concur with your recommendation. The department pays work time within the boundaries of state administrative rule and policy and believe it is the prerogative of its managers to develop individual work plans to ensure its employees are trained and ready for any potential work needs.

We believe the citation of State Accounting Policy 202 policy is specifically for Health Care and Benefits Division Sponsored Events and is being incorrectly applied to the DMA policy. The DMA Physical Training Program is not a Health Care and Benefits Division Sponsored Event and so the policy is not applicable. The DMA Physical Training Program Policy has been in effect since at least 2008, before the State Accounting Policy 202 became effective in 2011. Further, the Physical Training Program is neither a benefit nor privilege for state employees but instead is a defined work plan. The finding also states the DMA policy will create inequities among executive branch employees. We do not understand how that leads to a violation of any policy nor are we aware of any policy that mandates equity among all executive branch employees.

Section 2-18-604, MCA gives the Department of Administration authority to administer annual, sick, military leave and jury duty leave. The DMA Physical Training Program is not leave time. It is work time and is not directed by the Department of Administration.

The DMA Physical Training Program Policy is encouraged by DMA management as a work-related task because a healthy and motivated workforce helps DMA to achieve its mission. DMA has managerial discretion to direct the work of its employees during work time to achieve its goals and objectives and the Physical Training Program is a valuable tool. DMA does not view its Physical Training Program as leave time or as a benefit but, instead, as a job duty that is encouraged of every employee. As such DMA has not violated any statute, simply exercised its managerial rights.

The Department of Military Affairs, per MCA 10-1-102 is organized to

- (2) supervise, administer, and coordinate civil defense and disaster control activities
- (3) recruit, mobilize, administer, train, discipline, equip, and supply the organized militia

As such, our DMA employees, as well as our federal full-time employees need to maintain a physical condition that best enables them to support Montana's organized militia as well as DMA's expanded roles and responsibilities, including DES, CFMO, Youth Challenge and Veterans Affairs. This allowance for physical conditioning to be included in DMA's work plans supports the employee mission and goals of the department.

Sincerely,

A handwritten signature in black ink, appearing to read 'MG Quinn', with a stylized flourish at the end.

MG Matthew T. Quinn
Director