



A REPORT
TO THE
MONTANA
LEGISLATURE

FINANCIAL-COMPLIANCE AUDIT

State Auditor's Office
For the Two Fiscal Years Ended
June 30, 2008

OCTOBER 2008

LEGISLATIVE AUDIT
DIVISION

08-20

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Financial-compliance audits are conducted by the Legislative Audit Division to determine if 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) certificates.

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, 2007, was issued January 23, 2008. The Single Audit Report for the two fiscal years ended June 30, 2009, will be issued by March 31, 2010. 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 2008

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, 2008. Included in this report are recommendations concerning inadequate internal controls, compliance with state laws, and accounting issues. The report also contains two disclosure issues regarding the Insure Montana Program. 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 his staff for their assistance and cooperation during the audit.

Respectfully submitted,

/s/ Tori Hunthausen

Tori Hunthausen, CPA
Legislative Auditor

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ELECTED, APPOINTED, AND ADMINISTRATIVE OFFICIALS

State Auditor's Office John Morrison, State Auditor
 Janice VanRiper, Deputy State Auditor
 Lynne Egan, Acting Deputy Securities Commissioner
 Janice VanRiper, Acting Deputy Insurance Commissioner
 Eileen Rose, Central Services Administrator

Insure Montana Board Members

		<u>Term Expires</u>
Gail Briese-Zimmer	Helena	January 2010
Jim Edwards	Helena	June 2009
Erin McGowan Fincham	Helena	June 2010
Anna Whiting Sorrell	Helena	Pleasure*
Betty Beverly	Helena	January 2009
Bob Marsenich	Polson	January 2011
Connie Welsh	Helena	January 2009
David B. Kendall	Missoula	June 2011
Janice VanRiper	Helena	Pleasure *

*Anna Whiting Sorrell from the Governor's Office and Janice VanRiper 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 John Morrison at:

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REPORT SUMMARY

State Auditor’s Office

This report contains the results of our financial-compliance audit of the State Auditor’s Office (office) for the two fiscal years ended June 30, 2008. This report contains eight recommendations directed to the office concerning internal controls, compliance with state laws, and accounting issues. The prior financial-compliance audit of the office for the two fiscal years ended June 30, 2006, contained seven recommendations.

We issued an unqualified opinion on the office’s financial schedules for fiscal years 2007-08 and 2006-07. This means the reader may rely on the financial information presented in the financial schedules and supporting data on the state’s accounting system.

The listing below serves as a means of summarizing the recommendations contained in the report, the office’s response thereto, and a reference to the supporting comments.

Recommendation #1

We recommend the office enhance and implement internal controls over the Insure Montana Program 6

Office Response: Do not Concur..... B-3

Recommendation #2

We recommend the office enhance and monitor revenue coding and reconciliations to ensure the revenue amounts reflected on the state’s accounting system are accurate and supported. 7

Office Response: Concur..... B-4

Recommendation #3

We recommend the office:

- A. Establish written insurance license procedures to ensure refunds are issued when collections exceed legally required payments.
- B. Issue refunds and charge the correct application fees for nonresident producer licenses as required by state law. 8

Office Response: Concur..... B-4

Recommendation #4

We recommend the office implement procedures for monitoring and testing its internal control as required by state policy..... 9

Office Response: Concur..... B-5

Recommendation #5

We recommend the office:

- A. Transfer excess fees to the General Fund as required by state law.
- B. Establish procedures to ensure all excess annual leave is used by employees or forfeited in accordance with state law.
- C. Instruct insurers to return certificates of authority as required by state law.
- D. Charge the appropriate fee for the genetics program in accordance with state law.

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Office Response: Concur.....B-5

Recommendation #6

We recommend the office ensure personnel are paid out of the correct program budget.

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Office Response: Concur.....B-6

Recommendation #7

We recommend the office record contract accruals, and record and have adequate support for accounts receivable balances for the Insure Montana Program, in accordance with state law and policy. 13

Office Response: Concur.....B-6

Recommendation #8

We recommend the office adequately support the revenue estimates recorded on the accounting system. 13

Office Response: Concur.....B-6

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, 2008. 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, 2008.

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

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

Subject	Significant Deficiency	Material Weakness	Page
Insure Montana Program Operations	Yes	No	5
Revenue Coding and Reconciliations	Yes	No	7
Insurance Licenses	Yes	No	8
Monitoring and Testing of Internal Controls	Yes	No	9

This report contains eight 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 section 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 State Auditor's Office licenses and regulates insurance companies and agents within the state, and regulates and registers securities dealers. Total full-time equivalent (FTE) positions of the office as of June 2008 are 78.5, which includes 14 exempt positions.

The office is organized as follows:

The **Centralized Services Division** is responsible for the administrative, budgeting, personnel, and accounting functions of the office. The division also provides support for the State Auditor as he fulfills his duties on the State Land Board and the Crop Hail Insurance Board (10 FTE).

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 (52.5 FTE).

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. 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 (3 FTE).

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 (13 FTE).

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 office also distributed federal forest reserve funds to Montana counties in state fiscal year 2006-07. This responsibility was moved to the Department of Administration during the 2007 Legislative Session.

Prior Audit Recommendations

The prior financial-compliance audit of the office for the two fiscal years ended June 30, 2006, contained seven recommendations. During the current audit, we determined the office implemented all seven of the recommendations.

Chapter II – Findings and Recommendations

Internal Controls

According to state policy, an entity's management is responsible for establishing and maintaining internal control. Internal controls are policies and procedures used by agencies to ensure that their programs operate efficiently and effectively. Internal control policies and procedures are designed to safeguard agency assets, check the accuracy and reliability of financial data, promote operational efficiency, encourage adherence to prescribed managerial policies, and foster compliance with applicable laws and regulations. Management is expected to conduct reviews, tests and analyses of internal controls to ensure their proper operation, and to identify whether controls are being followed before problems occur. Weak or insufficient internal controls can lead to theft, shortages, operational inefficiency, or a breakdown in the control structure.

Listed below are examples of insufficient internal controls at the office concerning Insure Montana, revenue recording, and insurance licenses.

Insure Montana

The Insure Montana Program has established internal control procedures, but the procedures should be improved.

The office operates the Insure Montana Program to assist small businesses and employees with the cost of health insurance. Insure Montana has an insurance purchasing pool and a tax credit program. The tax credit program provides tax credits to employers who currently offer group health insurance to their employees. The purchasing pool program offers group health insurance through a pool of small businesses, and participants and employers in the purchasing pool program receive monthly payments to assist with the cost of coverage.

Through our audit we found the internal controls over the Insure Montana Program could be improved. Weaknesses in internal control include: inadequate documentation of review for changes in applicants' information, reconciliation controls between the state's accounting system and the Insure Montana database, and a lack of written procedures for verification process for applicants' information. Examples and results of these weaknesses are listed below:

- ◆ We tested 20 tax credit files and 20 purchasing pool program files for program eligibility and appropriate calculation of the tax credits, incentive payments, and assistance payments, as applicable. While the files contained evidence that employment changes had taken place, it was not clear when the office

was notified of the change, how the notification was received, which office staff person dealt with the change, or when the change was input to the Insure Montana database. The changes potentially affect program eligibility.

- ◆ In one tax credit file we tested, Insure Montana Program staff were notified of two changes related to eligible employees, and the staff did not make adjustments to the tax credit authorized in the Insure Montana database for tax year 2006. As a result, the company received \$1,480 in excess tax credit.
- ◆ While the Insure Montana Program staff developed procedures for reconciling the purchasing pool information on the Insure Montana database to the state's accounting system, the process was cumbersome and lengthy. The two systems did not balance at state fiscal year-end 2006-07. The state's accounting system was \$90,424 less than the database amount.
- ◆ The office has not verified the reported information on the Insure Montana application forms. The reported information is used to determine eligibility and the monthly assistance or the tax credit amounts.

Without adequate controls, there is significant risk that inappropriate payments will be made with Insure Montana funds, and there is potential for errors on the state's accounting system. There was significant staff turnover with the Insure Montana Program, which contributed to the control issues. The new management has taken steps to correct and improve controls. The office also has plans to improve the Insure Montana database in the upcoming fiscal year with system upgrades. Improving and monitoring these controls could be a significant time cost to the office, depending on the changes management decides to make. Upgrades and improvements to the database require payments to the database contractors, which could also be costly depending on the work requested.

RECOMMENDATION #1

We recommend the office enhance and implement internal controls over the Insure Montana Program.

Office Revenue

The revenues that go through the State Auditor's Office database are not coded correctly and the total revenues do not support the amounts on the state's accounting system.

The office has a database used to record most of the revenues for the office. The database tracks which businesses paid premium insurance tax and which businesses and individuals paid license fees. The office accounting staff created codes to record the revenue in the database. The codes in the database are associated with certain funds and accounts on the state's accounting system. We found that some codes in the database were not matched to the revenue classes that appropriately reflected the type of revenue on the state's records. We also noted that the reconciliation procedure used by the office failed to detect errors and discrepancies between the two systems.

Coding of Revenue

The office has a coding category report, which shows how the state accounting system funds and accounts are associated with the database codes. Some of the codes on the coding category report do not correlate with the correct account and fund on the state's accounting system. The office was unable to determine the dollar effect of the coding errors in fiscal year 2006-07, and it was not efficient for us to review every revenue transaction to determine if the correct coding was used. The current accounting staff at the office did not establish the codes, but said they are aware of the issue and plan to correct it.

Reconciliation of Revenue

The office has procedures for a reconciliation between its database and the state's accounting system. This reconciliation is important to ensure quality information is used for making management decisions. We found the database and the state's accounting system did not reconcile at state fiscal year-end 2006-07. We calculated the state's accounting system as having \$495,621 more than the database.

RECOMMENDATION #2

We recommend the office enhance and monitor revenue coding and reconciliations to ensure the revenue amounts reflected on the state's accounting system are accurate and supported.

Insurance Licenses

There are no written procedures for recording and reviewing data entered for insurance licenses.

In order for insurers to conduct business in the state of Montana, they must complete an application and pay the appropriate application fee to the office. The office records the payment on the database. Of the ten deposits we tested for insurance licenses, three licensees overpaid the application amount and no refund was issued. Section 33-2-708(4), MCA, requires any overpayment of \$10 or more be refunded to the applicant. The total amount that should have been refunded was \$800. According to office personnel, these errors were not detected.

Section 33-2-708(1), MCA, also dictates how much the application fee should be for each type of application. For nonresident insurance producer licenses, the fee is \$100. Of the ten deposits we tested, we noted two where the office collected \$200 for the application fee. According to office personnel, the instructions for the application indicate there is a \$100 fee for each insurance line type the applicant wants to sell, which are life/health insurance or property/casualty insurance. State law does not indicate a \$100 fee is required for each line type, but rather for the application. Therefore, the department collected \$100 in excess of what it should have collected from each applicant, and no refunds were issued. In fiscal year 2006-07, there were 221 producers who obtained licenses for life/health and property/casualty, and 306 in fiscal year 2007-08. Therefore, the office collected \$22,100 in error in fiscal year 2006-07, and \$30,600 in fiscal year 2007-08. Office personnel indicated they have been charging and collecting \$200 in these application situations for years.

RECOMMENDATION #3

We recommend the office:

- A. *Establish written insurance license procedures to ensure refunds are issued when collections exceed legally required payments.*
 - B. *Issue refunds and charge the correct application fees for nonresident producer licenses as required by state law.*
-

Monitoring and Testing of Internal Controls

The office has not fully implemented its internal control procedures in accordance with state accounting policy.

We identified errors that resulted in significant control deficiencies as described in the previous report sections and shown on table 1. The errors in the previous report sections may have been detected by office staff if monitoring and testing procedures for established internal controls had been in place.

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 develop internal control procedures, monitor and test its internal controls, and evaluate and report the results of its testing.

The office has developed and is continuing to develop internal control procedures. However, the office could not produce documentation of monitoring or testing of these established procedures.

RECOMMENDATION #4

We recommend the office implement procedures for monitoring and testing its internal control as required by state policy.

Compliance With State Laws

We tested the office's compliance with selected state laws and regulations applicable to office operations. The following section describes areas where the office's compliance with state laws can be improved.

General Fund Transfers

The office transferred incorrect amounts to the General Fund in fiscal year 2007-08.

Fees deposited in the securities fund are used to pay the cost of the securities division functions and regulatory duties. According to section 30-10-115(2), MCA, any excess

must be deposited in the General Fund. The office has a spreadsheet it uses to track the amounts that have been moved to the General Fund during the year, and how much cash is available to deposit in the General Fund. In state fiscal year 2007-08, the office had \$154,800 remaining in the securities fund. This amount should have been transferred to the General Fund. Current staff are revising the spreadsheet to better track the amounts available that should be deposited in the General Fund.

Excess Leave

The office is not following state law regarding employee excess vacation leave.

Section 2-18-617(1), MCA, limits the amount of annual leave an employee can accumulate and carry forward to the next calendar year to twice the amount an employee earns in a calendar year. Annual leave accumulated above this amount at the end of a calendar year is considered excess and must be used by the employee within the first 90 days of the next calendar year, unless an employee's written request for such leave is denied by the employing agency. If the employing agency denies the request, the excess annual leave is not forfeited if used before the end of that calendar year. State law clearly makes it the employing agency's responsibility to provide reasonable opportunity for an employee to use, rather than forfeit, excess annual leave. We noted one exempt employee who was allowed to carry forward 181.84 hours over the amount allowed in state law, totaling approximately \$6,087. Office personnel indicated there are no office procedures for monitoring or removing excess leave.

Certificates of Authority

The office does not collect certificates of authority as required by state law.

An insurer transacting insurance in Montana must have a certificate of authority (certificate) issued by the commissioner. The certificate outlines the specific kinds of insurance the insurer is authorized to transact in Montana. According to section 33-2-116(3), MCA, the certificate is at all times the property of the state of Montana, and upon expiration, suspension, or termination, the insurer shall return the certificate. The office does not require companies that are in suspended status to return their certificate, and only two out of three terminated companies that we reviewed returned it. According to office personnel, some companies lose or cannot find the certificate, and historically, the office has not required suspended companies to return the certificate.

Genetics Program Fee

During state fiscal year 2007-08, the office charged the incorrect amount for the genetics program fee.

Section 33-2-712, MCA, requires applicable insurers to pay a \$1 fee for each Montana resident insured under any individual or group disability or health insurance policy. Office personnel thought the fee had dropped from \$1 to \$.70 due to changes in legislation, and updated the genetics program fee form to reflect the fee change. This legislation was not passed, and in 2007-08, the insurers only paid \$.70 rather than the \$1 fee. Office management estimate the error cost the genetics program approximately \$300,000 in revenue in state fiscal year 2007-08. Office personnel plan to correct the form and charge the legally required fee in state fiscal year 2008-09.

RECOMMENDATION #5

We recommend the office:

- A. *Transfer excess fees to the General Fund as required by state law.*
 - B. *Establish procedures to ensure all excess annual leave is used by employees or forfeited in accordance with state law.*
 - C. *Instruct insurers to return certificates of authority as required by state law.*
 - D. *Charge the appropriate fee for the genetics program in accordance with state law.*
-

Program Transfers

Office personnel are paid out of incorrect program budgets.

The office has three divisions with personal service costs. The Centralized Services Division is responsible for administrative, personnel, budgeting, and accounting functions of the office. The Insurance Division regulates the insurance industry in Montana. The Securities Division is responsible for the administration and enforcement of the Securities Act of Montana, and for the registration of securities issuers, salespeople, broker-dealers, investment advisers, and investment adviser representatives. For both fiscal years 2006-07 and 2007-08, the office paid employees out of the incorrect budgets. Two employees budgeted within the Securities Division and five employees budgeted within the Insurance

Division perform duties under the Centralized Services Division. Approximately \$79,673 of expenditures should have been moved from the Securities Division to Centralized Services, and \$218,354 of expenditures should have been moved from the Insurance Division to Centralized Services in fiscal year 2007-08.

Section 17-7-139(1), MCA, allows for program transfers approved by the approving authority, the Office of Budget and Program Planning under the Governor's office. The instructions on the program transfer form that is submitted to the Office of Budget and Program Planning states 'program transfer of full-time employees must be completed by April 1, 2008. No program transfers of full-time employees are allowed in the odd numbered fiscal year.' Office personnel caught these errors in April, but given the deadline could not make the needed changes.

RECOMMENDATION #6

We recommend the office ensure personnel are paid out of the correct program budget.

Accounting Issues

The office did not properly accrue contract expenditures and does not have adequate support for accounts receivable balances for the Insure Montana Program.

Section 17-1-102(4), MCA, requires the office to input all necessary transactions before the end of the fiscal year to present the receipt, use, and disposition of all money, for which it is accountable, in accordance with generally accepted accounting principles. The Department of Administration establishes state accounting policy to implement this law. We noted the following instances where the office did not record financial activity for the Insure Montana Program in accordance with state law and policy.

- ◆ The office entered into a contract for the Insure Montana Program, and paid the \$77,500 contract in advance. This payment was made at the end of the 2006-07 fiscal year, and office personnel indicated this was paid in full to use the 2006-07 budget appropriation. Rather than paying for services not yet received, the program should have recorded an accrual at year-end and paid for the services when they were received.
- ◆ The Insure Montana Program establishes accounts receivable when overpayments are made to eligible businesses and employees for monthly assistance payments. In state fiscal year 2006-07, the accounts receivable amount of \$49,210 shown on the state's accounting records is not supported. Insure Montana personnel were not employed with the office during state

fiscal year 2006-07, and could not locate specific supporting documentation for the accounts receivable balance.

- ◆ The Insure Montana Program is funded through tobacco taxes received from the Department of Public Health and Human Services. The office records an account receivable for the amount of revenue owed by, but not yet received from the Department of Public Health and Human Services for unclaimed tax credits. In fiscal year 2006-07, an account receivable was not recorded. The recorded fiscal year 2007-08 revenue amount includes the unrecorded fiscal year 2006-07 amount of \$1,719,100. Therefore, revenue is understated in fiscal year 2006-07 and overstated in fiscal year 2007-08 by \$1,719,100 in the State Special Revenue Fund. Office personnel forgot to make this entry in fiscal year 2006-07.

RECOMMENDATION #7

We recommend the office record contract accruals, and record and have adequate support for accounts receivable balances for the Insure Montana Program, in accordance with state law and policy.

Revenue Estimates

During fiscal year 2006-07, the office recorded a revenue estimate in error.

To prepare a state budget, section 17-7-111(1), MCA, emphasizes the need for consistent and accurate information from executive branch agencies. Necessary information includes estimated receipts by fund type and fund category. On the Schedule of Revenues and Transfers-In for fiscal year 2006-07, the office incorrectly established a \$6,030,756 revenue estimate in the General Fund for the Insure Montana Program. The personnel currently at the office were not employed with the office when the estimates were made, and could not find support for the estimates. As a result, the General Fund revenue estimates are inflated on the Schedule of Revenues and Transfers-In for fiscal year 2006-07, by \$6,030,756.

RECOMMENDATION #8

We recommend the office adequately support the revenue estimates recorded on the accounting system.

Chapter III – Disclosure Issues

Insure Montana

Conflict of Interest

The State Auditor, who is the Insurance Commissioner for Montana, is responsible for the regulation of the insurance industry. The State Auditor's Office (office) is a criminal justice agency charged with protecting Montana's consumers through insurance regulation and informing the public about insurance issues.

The office also administers the Insure Montana Program. The 2005 Legislature passed the laws that created this program, and placed the operations and administration at the office. The Insure Montana Program is a two-part program that is designed to assist small businesses with the cost of health insurance, whether they have provided health insurance previously or not. Small businesses with 2-9 employees that are currently providing health insurance to their employees are eligible for refundable tax credits. For businesses that were previously unable to afford health insurance for their employees, Insure Montana provides health insurance coverage through a small business purchasing pool.

As the administrator of the Insure Montana Program, and the regulator of the insurance industry in Montana, the office appears to have a conflicting role by regulating the insurance carrier from which it facilitates the purchase of the insurance plan for the purchasing pool. We present this as a disclosure issue and make no recommendation at this time.

Insurance Premiums

Insure Montana participants received a 12.6 percent increase in insurance premiums between 2007 and 2008. To address the increase in premiums, Insure Montana had the option of holding participants' premium subsidy level at the 2007 rates or increasing subsidy levels to offset premium increases. The decision was made to keep subsidies level at the 2007 rates. This meant participants are paying more in insurance premiums, but are not receiving an increase in employee assistance and employer incentive payments.

Insure Montana's health plan benefits also changed in 2008. Changes included increased deductibles and member coinsurance. If these increases continue along with increases in insurance premiums, and incentive and assistance payments stay constant, it may be less desirable for employers to offer health insurance to their employees because insurance may no longer be affordable. We present this as a disclosure issue and make no recommendation at this time.

Independent Auditor's Report and Office Financial Schedules

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, 2008, and 2007. The information contained in these financial schedules is the responsibility of the office's management. Our responsibility is to express an opinion 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 opinion.

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.

In our opinion, the financial schedules referred to above present fairly, in all material respects, the results of operations and changes in fund balances and property held in trust of the State Auditor's Office for each of the fiscal years ended June 30, 2008, and 2007, in conformity with the basis of accounting described in note 1.

Respectfully submitted,

/s/ James Gillett

James Gillett, CPA
Deputy Legislative Auditor

September 2, 2008

STATE AUDITOR'S OFFICE
SCHEDULE OF CHANGES IN FUND BALANCES & PROPERTY HELD IN TRUST
FOR THE FISCAL YEAR ENDED JUNE 30, 2008

	<u>General Fund</u>	<u>State Special Revenue Fund</u>	<u>Enterprise Fund</u>	<u>Agency Fund</u>
FUND BALANCE: July 1, 2007	\$ (17,270,977)	\$ 2,586,846	\$ 447,799	\$ 0
PROPERTY HELD IN TRUST: July 1, 2007				<u>\$ 11,853,845</u>
 ADDITIONS				
Budgeted Revenues & Transfers-In	70,738,736	23,986,181		
Nonbudgeted Revenues & Transfers-In	3,309,251	82,485	733,785	
Prior Year Revenues & Transfers-In Adjustments		34,422		
Direct Entries to Fund Balance	(55,189,538)	(450,536)		
Additions to Property Held in Trust				273,038
Total Additions	<u>18,858,449</u>	<u>23,652,552</u>	<u>733,785</u>	<u>273,038</u>
 REDUCTIONS				
Budgeted Expenditures & Transfers-Out	21,228,353	15,557,113		
Nonbudgeted Expenditures & Transfers-Out		3,435,382	792,367	
Prior Year Expenditures & Transfers-Out Adjustments		(897,767)		
Reductions in Property Held in Trust				166,512
Total Reductions	<u>21,228,353</u>	<u>18,094,728</u>	<u>792,367</u>	<u>166,512</u>
FUND BALANCE: June 30, 2008	<u>\$ (19,640,881)</u>	<u>\$ 8,144,670</u>	<u>\$ 389,217</u>	<u>\$ 0</u>
PROPERTY HELD IN TRUST: June 30, 2008				<u>\$ 11,960,371</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.

STATE AUDITOR'S OFFICE
SCHEDULE OF CHANGES IN FUND BALANCES & PROPERTY HELD IN TRUST
FOR THE FISCAL YEAR ENDED JUNE 30, 2007

	General Fund	State Special Revenue Fund	Federal Special Revenue Fund	Enterprise Fund	Agency Fund
FUND BALANCE: July 1, 2006	\$ (775,155)	\$ 4,982,365	\$ 0	\$ 366,530	\$ 0
PROPERTY HELD IN TRUST: July 1, 2006					\$ 10,141,733
ADDITIONS					
Budgeted Revenues & Transfers-In	67,598,074	15,400,168	12,934,779		
Nonbudgeted Revenues & Transfers-In	2,997,268	93,425		919,916	
Prior Year Revenues & Transfers-In Adjustments	602,876	25,835	3,165	(295,984)	
Direct Entries to Fund Balance	(53,148,592)	(490,318)	(0)		
Additions to Property Held in Trust					1,895,261
Total Additions	<u>18,049,626</u>	<u>15,029,110</u>	<u>12,937,944</u>	<u>623,932</u>	<u>1,895,261</u>
REDUCTIONS					
Budgeted Expenditures & Transfers-Out	18,830,996	14,100,720	12,934,779		
Nonbudgeted Expenditures & Transfers-Out		3,031,911		542,663	
Prior Year Expenditures & Transfers-Out Adjustments	15,714,452	291,998	3,165		
Reductions in Property Held in Trust					183,149
Total Reductions	<u>34,545,448</u>	<u>17,424,629</u>	<u>12,937,944</u>	<u>542,663</u>	<u>183,149</u>
FUND BALANCE: June 30, 2007	\$ (17,270,977)	\$ 2,586,846	\$ 0	\$ 447,799	\$ 0
PROPERTY HELD IN TRUST: June 30, 2007					\$ 11,853,845

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.

STATE AUDITOR'S OFFICE
SCHEDULE OF TOTAL REVENUES & TRANSFERS-IN
FOR THE FISCAL YEAR ENDED JUNE 30, 2008

	<u>General Fund</u>	<u>State Special Revenue Fund</u>	<u>Enterprise Fund</u>	<u>Total</u>
TOTAL REVENUES & TRANSFERS-IN BY CLASS				
Licenses and Permits	\$ 6,582,397	\$ 9,292,676		\$ 15,875,073
Taxes	63,935,552	11,610		63,947,162
Charges for Services		389,997	\$ 722,721	1,112,718
Investment Earnings			11,064	11,064
Fines, Forfeits and Settlements	220,787			220,787
Miscellaneous		98,805		98,805
Grants, Contracts, Donations and Abandonments		86,259		86,259
Other Financing Sources	<u>3,309,251</u>	<u>14,223,741</u>		<u>17,532,992</u>
Total Revenues & Transfers-In	<u>74,047,987</u>	<u>24,103,088</u>	<u>733,785</u>	<u>98,884,860</u>
Less: Nonbudgeted Revenues & Transfers-In	3,309,251	82,485	733,785	4,125,521
Prior Year Revenues & Transfers-In Adjustments		34,422		34,422
Actual Budgeted Revenues & Transfers-In	<u>70,738,736</u>	<u>23,986,181</u>	<u>0</u>	<u>94,724,917</u>
Estimated Revenues & Transfers-In	<u>70,702,782</u>	<u>24,008,983</u>		<u>94,711,765</u>
Budgeted Revenues & Transfers-In Over (Under) Estimated	<u>\$ 35,954</u>	<u>\$ (22,802)</u>	<u>\$ 0</u>	<u>\$ 13,152</u>
BUDGETED REVENUES & TRANSFERS-IN OVER (UNDER) ESTIMATED BY CLASS				
Licenses and Permits	\$ (2,603)	\$ (5,360)		\$ (7,963)
Taxes	(1,230)	(3,767)		(4,997)
Charges for Services		(6,701)		(6,701)
Fines, Forfeits and Settlements	39,887			39,887
Miscellaneous	(100)	(1,974)		(2,074)
Grants, Contracts, Donations and Abandonments		(1,000)		(1,000)
Other Financing Sources		(4,000)		(4,000)
Budgeted Revenues & Transfers-In Over (Under) Estimated	<u>\$ 35,954</u>	<u>\$ (22,802)</u>	<u>\$ 0</u>	<u>\$ 13,152</u>

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STATE AUDITOR'S OFFICE
SCHEDULE OF TOTAL REVENUES & TRANSFERS-IN
FOR THE FISCAL YEAR ENDED JUNE 30, 2007

	<u>General Fund</u>	<u>State Special Revenue Fund</u>	<u>Federal Special Revenue Fund</u>	<u>Enterprise Fund</u>	<u>Total</u>
TOTAL REVENUES & TRANSFERS-IN BY CLASS					
Licenses and Permits	\$ 6,079,780	\$ 8,733,806			\$ 14,813,586
Taxes	61,400,026	5			61,400,031
Charges for Services		772,941		\$ 613,191	1,386,132
Investment Earnings				10,741	10,741
Fines, Forfeits and Settlements	428,605				428,605
Miscellaneous	300	(41,072)			(40,772)
Grants, Contracts, Donations and Abandonments		144,000			144,000
Other Financing Sources	3,289,507	5,909,748	\$ 3,165		9,202,420
Federal			12,934,779		12,934,779
Total Revenues & Transfers-In	<u>71,198,218</u>	<u>15,519,428</u>	<u>12,937,944</u>	<u>623,932</u>	<u>100,279,522</u>
Less: Nonbudgeted Revenues & Transfers-In	2,997,268	93,425		919,916	4,010,609
Prior Year Revenues & Transfers-In Adjustments	602,876	25,835	3,165	(295,984)	335,892
Actual Budgeted Revenues & Transfers-In	<u>67,598,074</u>	<u>15,400,168</u>	<u>12,934,779</u>	<u>0</u>	<u>95,933,021</u>
Estimated Revenues & Transfers-In	<u>72,448,821</u>	<u>29,490,621</u>	<u>12,550,000</u>		<u>114,489,442</u>
Budgeted Revenues & Transfers-In Over (Under) Estimated	<u>\$ (4,850,747)</u>	<u>\$ (14,090,453)</u>	<u>\$ 384,779</u>	<u>\$ 0</u>	<u>\$ (18,556,421)</u>
BUDGETED REVENUES & TRANSFERS-IN OVER (UNDER) ESTIMATED BY CLASS					
Licenses and Permits	\$ 87,972	\$ 2,231			\$ 90,203
Taxes	831,476				831,476
Charges for Services		(176,970)			(176,970)
Fines, Forfeits and Settlements	260,352				260,352
Miscellaneous	209				209
Other Financing Sources	(6,030,756)	(13,915,714)			(19,946,470)
Federal			\$ 384,779		384,779
Budgeted Revenues & Transfers-In Over (Under) Estimated	<u>\$ (4,850,747)</u>	<u>\$ (14,090,453)</u>	<u>\$ 384,779</u>	<u>\$ 0</u>	<u>\$ (18,556,421)</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.

STATE AUDITOR'S OFFICE
 SCHEDULE OF TOTAL EXPENDITURES & TRANSFERS-OUT
 FOR THE FISCAL YEAR ENDED JUNE 30, 2008

PROGRAM (ORG) EXPENDITURES & TRANSFERS-OUT	CENTRAL MANAGEMENT	INSURANCE	LOCAL ASSISTANCE TO COUNTIES	SECURITIES	Total
Personal Services					
Salaries	\$ 430,345	\$ 2,285,249		\$ 358,940	\$ 3,074,534
Hourly Wages		220			220
Employee Benefits	65,847	759,229		139,511	964,587
Total	<u>496,192</u>	<u>3,044,698</u>		<u>498,451</u>	<u>4,039,341</u>
Operating Expenses					
Other Services	28,203	588,482		158,496	775,181
Supplies & Materials	24,593	127,138		20,252	171,983
Communications	9,784	97,709		12,935	120,428
Travel	16,534	81,070		11,754	109,358
Rent	26,721	157,710		35,627	220,058
Repair & Maintenance	225	1,106		270	1,601
Other Expenses	11,221	827,227		46,359	884,807
Total	<u>117,281</u>	<u>1,880,442</u>		<u>285,693</u>	<u>2,283,416</u>
Local Assistance					
From Other Income Sources			\$ 21,228,353		21,228,353
Total			<u>21,228,353</u>		<u>21,228,353</u>
Benefits & Claims					
To Individuals		824,173			824,173
From State Sources		8,430,913			8,430,913
Total		<u>9,255,086</u>			<u>9,255,086</u>
Transfers					
Accounting Entity Transfers		23,102		3,286,150	3,309,252
Total		<u>23,102</u>		<u>3,286,150</u>	<u>3,309,252</u>
Total Expenditures & Transfers-Out	<u>\$ 613,473</u>	<u>\$ 14,203,328</u>	<u>\$ 21,228,353</u>	<u>\$ 4,070,294</u>	<u>\$ 40,115,448</u>
EXPENDITURES & TRANSFERS-OUT BY FUND					
General Fund			\$ 21,228,353		\$ 21,228,353
State Special Revenue Fund	\$ 613,473	\$ 13,410,961		\$ 4,070,294	18,094,728
Enterprise Fund		792,367			792,367
Total Expenditures & Transfers-Out	<u>613,473</u>	<u>14,203,328</u>	<u>21,228,353</u>	<u>4,070,294</u>	<u>40,115,448</u>
Less: Nonbudgeted Expenditures & Transfers-Out		815,468		3,412,281	4,227,749
Prior Year Expenditures & Transfers-Out Adjustments		(897,768)			(897,768)
Actual Budgeted Expenditures & Transfers-Out	<u>613,473</u>	<u>14,285,628</u>	<u>21,228,353</u>	<u>658,013</u>	<u>36,785,467</u>
Budget Authority	720,936	15,751,817	21,441,871	987,244	38,901,868
Unspent Budget Authority	<u>\$ 107,463</u>	<u>\$ 1,466,189</u>	<u>\$ 213,518</u>	<u>\$ 329,231</u>	<u>\$ 2,116,401</u>
UNSPENT BUDGET AUTHORITY BY FUND					
General Fund			\$ 213,518		\$ 213,518
State Special Revenue Fund	\$ 107,463	\$ 1,466,189		\$ 329,231	1,902,883
Unspent Budget Authority	<u>\$ 107,463</u>	<u>\$ 1,466,189</u>	<u>\$ 213,518</u>	<u>\$ 329,231</u>	<u>\$ 2,116,401</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.

STATE AUDITOR'S OFFICE
 SCHEDULE OF TOTAL EXPENDITURES & TRANSFERS-OUT
 FOR THE FISCAL YEAR ENDED JUNE 30, 2007

PROGRAM (ORG) EXPENDITURES & TRANSFERS-OUT	CENTRAL MANAGEMENT	FOREST RESERVE TO COUNTIES	INSURANCE	LOCAL ASSISTANCE TO COUNTIES	SECURITIES	TOTAL
Personal Services						
Salaries	\$ 412,842		\$ 1,911,468		\$ 348,144	\$ 2,672,454
Employee Benefits	113,902		611,940		126,389	852,231
Total	<u>526,744</u>		<u>2,523,408</u>		<u>474,533</u>	<u>3,524,685</u>
Operating Expenses						
Other Services	19,919		923,518		59,162	1,002,599
Supplies & Materials	14,748		97,298		15,517	127,563
Communications	11,643		90,760		16,476	118,879
Travel	6,768		43,521		17,583	67,872
Rent	30,954		178,703		41,239	250,896
Repair & Maintenance	100		577		133	810
Other Expenses	3,575		(1,094,337)		2,155	(1,088,607)
Total	<u>87,707</u>		<u>240,040</u>		<u>152,265</u>	<u>480,012</u>
Local Assistance						
From Federal Sources		\$ 12,934,779				12,934,779
From Other Income Sources				\$ 34,545,448		34,545,448
Total		<u>12,934,779</u>		<u>34,545,448</u>		<u>47,480,227</u>
Grants						
From State Sources			(573,215)			(573,215)
Total			<u>(573,215)</u>			<u>(573,215)</u>
Benefits & Claims						
To Individuals		3,165	1,146,430			1,149,595
From State Sources			10,099,281			10,099,281
Total		<u>3,165</u>	<u>11,245,711</u>			<u>11,248,876</u>
Transfers						
Accounting Entity Transfers			592		3,289,507	3,290,099
Total			<u>592</u>		<u>3,289,507</u>	<u>3,290,099</u>
Total Expenditures & Transfers-Out	\$ 614,451	\$ 12,937,944	\$ 13,436,536	\$ 34,545,448	\$ 3,916,305	\$ 65,450,684
EXPENDITURES & TRANSFERS-OUT BY FUND						
General Fund				\$ 34,545,448		\$ 34,545,448
State Special Revenue Fund	\$ 614,451		\$ 12,893,873		\$ 3,916,305	17,424,629
Federal Special Revenue Fund		\$ 12,937,944				12,937,944
Enterprise Fund			542,663			542,663
Total Expenditures & Transfers-Out	614,451	12,937,944	13,436,536	34,545,448	3,916,305	65,450,684
Less: Nonbudgeted Expenditures & Transfers-Out	(498)		548,563		3,026,510	3,574,575
Prior Year Expenditures & Transfers-Out Adjustments		3,165	(566)	15,714,452	292,564	16,009,615
Actual Budgeted Expenditures & Transfers-Out	614,949	12,934,779	12,888,539	18,830,996	597,231	45,866,494
Budget Authority	655,042	12,935,000	14,545,188	19,027,464	846,842	48,009,536
Unspent Budget Authority	<u>\$ 40,093</u>	<u>\$ 221</u>	<u>\$ 1,656,649</u>	<u>\$ 196,468</u>	<u>\$ 249,611</u>	<u>\$ 2,143,042</u>
UNSPENT BUDGET AUTHORITY BY FUND						
General Fund				\$ 196,468		\$ 196,468
State Special Revenue Fund	\$ 40,093		\$ 1,656,649		\$ 249,611	1,946,353
Federal Special Revenue Fund		\$ 221				221
Unspent Budget Authority	<u>\$ 40,093</u>	<u>\$ 221</u>	<u>\$ 1,656,649</u>	<u>\$ 196,468</u>	<u>\$ 249,611</u>	<u>\$ 2,143,042</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.

State Auditor's Office
Notes to the Financial Schedules
For the Two Fiscal Years Ended June 30, 2008

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, State Special Revenue, Federal 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. General Fund includes operations for securities, premium insurance taxes, and transfers of funds to Montana Public Employees' Retirement Administration.
- ◆ **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.

- ♦ **Federal Special Revenue Fund** – to account for activities funded from federal revenue sources. The office Federal Special Revenue Fund includes the receipt and disbursement of federal forest reserve funds to Montana counties. This fund was only at the office during state fiscal year 2007. This activity was transferred to the Department of Administration for state fiscal year 2008.

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.

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, 2007 and June 30, 2008.

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. Montana Comprehensive Health Association

On the Schedule of Total Expenditures & Transfers-Out for the fiscal year ended June 30, 2007, the Grants - from state sources in the Insurance column shows a credit amount of \$573,215. In fiscal year 2005-06, the office recorded expenditures as grants – from state sources which should have been recorded as a benefit & claim – to individuals. In fiscal year 2006-07, the office made correcting entries which resulted in the \$573,215 credit balance reported in the Grants – from state sources on the Schedule of Total Expenditures & Transfers-Out for the fiscal year ended June 30, 2007.

5. Local Assistance to Counties

In state fiscal year 2006-07 the transfer of funds to the Montana Public Employees' Retirement Administration was not recorded. This entry was recorded in fiscal year 2006-07, and therefore approximately \$15.8 million on the Schedule of Expenditures & Transfers-Out for fiscal year 2006-07 is attributed to the entry that should have been recorded in the previous year.

STATE
AUDITOR'S
OFFICE

OFFICE RESPONSE

MONTANA STATE AUDITOR

B-3

JOHN MORRISON
STATE AUDITOR



COMMISSIONER OF INSURANCE
COMMISSIONER OF SECURITIES

October 10, 2008

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

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OCT 14 2008

LEGISLATIVE AUDIT DIV.

Dear Ms. Hunthausen:

We have reviewed your financial compliance audit for the two fiscal years ending June 30, 2008. Thank you for the opportunity to respond. Our response to each audit recommendation follows:

Recommendation #1:

We recommend the office enhance and implement internal controls over the Insure Montana Program.

Agency Response:

We do not concur in part.

- "... inadequate documentation of review for changes in applicants' information ..." The agency already requires all information changes be provided to program staff on a Change Report form. All Change Report forms are date stamped or contain a date from the facsimile machine. The program director has access to information on the database system that is "behind the scenes" where the user identification number and date is stored for any changes that were entered on the system.
- "... reconciliation controls between the state's accounting system and the Insure Montana database ..." The agency's original process of reconciling the state's accounting system and the program's database was cumbersome, lengthy and error prone. In May 2008 the database contractor completed a system enhancement that automates an immediate reconciliation between the two systems eliminating the time and effort spent on the former process as well as the possibility of human error.

Ms. Tori Hunthausen
October 10, 2008
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- "... lack of written procedures for verification process for applicants' information ..."
The program's existing policy manual (Section 104-1 'Audits') outlines the process of verifying applicant information for case file audits. New case file audits may also reveal internal security issues. The director will closely monitor the audits and review a portion of the case files for appropriate verifications, such as wage verification of employees and health insurance statements for businesses. The proper verifications will provide proof of a credible case and appropriate expenditure of program funds. A request for a full time employee (FTE) has been submitted via the Executive Planning Process (EPP) to continue to complete case file audits. A third FTE would not only make ongoing, frequent case file audits possible, but would also aid in some level of separation of duties.

Recommendation #2:

We recommend the office enhance and monitor revenue coding and reconciliations to ensure the revenue amounts reflected on the state's accounting system are accurate and supported.

Agency Response:

We concur. The office has developed and implemented procedures to insure all deposits are recorded when received, recorded properly on the state's accounting system, are accurate, and properly documented.

Recommendation #3:

We recommend the office:

- A. Establish written insurance license procedures to ensure refunds are issued when collections exceed legally required payments.
- B. Issue refunds and charge the correct application fees for nonresident producer licenses as required by state law.

Agency Response:

We concur.

- A. The office has implemented a written procedure to ensure all insurance license applications are reviewed at the time they are received and if the payment exceeds the collection amount legally required a refund is processed.

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- B. The office has determined the nonresident producers that are due refunds and are in the processing refunds.

Recommendation #4:

We recommend the office implement procedures for monitoring and testing its internal control as required by state policy.

Agency Response:

We concur. The office is the process of developing methods to monitor and test its internal control as required by state policy.

Recommendation #5:

We recommend the office:

- A. Transfer excess fees to the General Fund as required by state law.
- B. Establish procedures to ensure all excess annual leave is used by employees or forfeited in accordance with state law.
- C. Instruct insurers to return certificates of authority as required by state law.
- D. Charge the appropriate fee for the genetics program in accordance with state law.

Agency Response:

We concur.

- A. The office has transferred the omitted fiscal year 08 \$154,800 to the General Fund from the Securities Fund.
- B. The agency has amended our procedure for monitoring excess leave to incorporate an additional step to forfeit unused excess leave by March 31 or December 31 as required by state law.
- C. The office procedures require companies to return the certificate. The office will ensure the certificates are received as required by state law or document why they are not returned.
- D. During the audit the office reported this error to the audit staff and the office mailed letters to companies on September 8, 2008 requesting payment of the additional fee as required by state law by September 29, 2008. As of September 30, 2008 the agency has collected 77% of the additional fees.

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October 10, 2008
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Recommendation #6:

We recommend the office ensure personnel are paid out of the correct program budget.

Agency Response:

We concur. The office is requesting modified positions to temporarily move the current positions into the correct program until the Legislature has an opportunity to authorize the move permanently.

Recommendation #7:

We recommend the office record contract accruals, and record and have adequate support for accounts receivable balances for the Insure Montana Program, in accordance with state law and policy.

Agency Response:

We concur.

The office has taken steps to correct the procedures recording accruals at fiscal year end.

- The office will comply with state law and policy by recording a contracts balance as an accrual at fiscal year end and make subsequent payments when services are received. The office has taken steps to correct the procedures to record accruals at fiscal year end.
- The program's overpayment file has been updated and will accurately record and support payments and outstanding balances of overpayments according to the correct fiscal year the claim was established. A system enhancement will be completed in the near future to automate the information and tracking of overpayment balances.
- While attempting to record fiscal years 06, 07, and 08 tax credit receivables due from DPHHS the office did record all the revenue as fiscal year 08. A correcting entry has been made so the fiscal year 08 revenue is not overstated.

Recommendation #8:

We recommend the office adequately support the revenue estimates recorded on the accounting system.

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Agency Response:

We concur. The office has amended its fiscal year end procedures to review and adjust revenue estimates prior to the fiscal year closing.

The agency also wishes to address the Disclosure Issues discussed in the audit.

Insure Montana

Conflict of Interest

The State Auditor's Office (SAO) disagrees that there is a conflict of interest as the administrator of the Insure Montana Program and the regulator of the insurance industry in Montana. The Insure Montana Program is not an insurance product that would fall under the area of insurance industry regulated by the SAO. The Insure Montana Program, using the same process as the Montana Comprehensive Health Association (MCHA), determines eligibility for premium incentive and assistance payments for businesses and its employees. The program also submits a Request for Proposal (RFP) for offers from insurance carriers to provide an insurance product to the participants of the program. The Insure Montana Program follows the State's RFP processes and procedures when choosing an insurance carrier. The Insure Montana Board chooses the successful bidding insurance carrier, which carrier is then subject to regulation by SAO.

Insurance Premiums

The premium increase for 2008 did increase 12.6%, which was consistent with industry-wide average increases. Note, however, that a major reason for that size rate increase had to do with previously uninsured Insure Montana members coming off their mandatory 12-month waiting periods for pre-existing conditions and thereby seeking deferred health care. That caused very high loss ratios during 2007, which negatively impacts rates for the following year. With a more stable claims picture in 2008, the likely rate increase for year 2008, however, is significantly smaller. That trend should continue, absent unanticipated large claims or upward cost-driving developments in the health insurance industry. The State Auditor's Office has requested an increase to the Insure Montana budget in part to help subsidy levels keep up with expected rate increases so that small employers will be more likely to continue being able to afford coverage through the Insure Montana.

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

Sincerely,

Janice S. VanLiper, Deputy State Auditor, for

John Morrison
State Auditor

JM/emr