



MICHIGAN

OFFICE OF THE AUDITOR GENERAL

AUDIT REPORT



THOMAS H. MCTAVISH, C.P.A.
AUDITOR GENERAL

The auditor general shall conduct post audits of financial transactions and accounts of the state and of all branches, departments, offices, boards, commissions, agencies, authorities and institutions of the state established by this constitution or by law, and performance post audits thereof.

– Article IV, Section 53 of the Michigan Constitution

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Michigan
Office of the Auditor General
REPORT SUMMARY

Financial Audit

Including the Provisions of the Single Audit Act

Report Number:
251-0100-07

Department of History, Arts and Libraries

October 1, 2004 through September 30, 2006

Released:
June 2007

A Single Audit is designed to meet the needs of all financial report users, including an entity's federal grantor agencies. The audit determines if the financial schedules and/or financial statements are fairly presented; considers internal control over financial reporting and internal control over federal program compliance; determines compliance with State compliance requirements material to the financial schedules and/or financial statements; and assesses compliance with direct and material requirements of the major federal programs.

Financial Schedules:

Auditor's Report Issued

We issued an unqualified opinion on the Department of History, Arts and Libraries' (HAL's) financial schedules.

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Internal Control Over Financial Reporting

We identified a reportable condition related to internal control over financial reporting. (Finding 1) We do not consider this reportable condition to be a material weakness.

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**Noncompliance and Other Matters
Material to the Financial Schedules**

We identified an instance of noncompliance or other matters applicable to the financial schedules that is required to be reported under *Government Auditing Standards* (Finding 2). In addition, we noted a reportable condition (Finding 3).

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Federal Awards:

Auditor's Reports Issued on Compliance

We audited 3 programs as major programs and identified known questioned costs of approximately \$1.4 million. HAL expended a total of approximately \$13.6 million in federal awards during the two-year period ended September 30, 2006. We issued 2 unqualified opinions and 1 adverse opinion. The opinions issued by major program are identified on the back of this summary.

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Internal Control Over Major Programs

We identified a reportable condition related to internal control over major programs (Finding 4). We consider Finding 4 to be a material weakness.

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Required Reporting of Noncompliance

We identified an instance of noncompliance that is required to be reported in accordance with U.S. Office of Management and Budget (OMB) Circular A-133 (Finding 4).

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Systems of Accounting and Internal Control:

We determined that HAL was in substantial compliance with Sections 18.1483 - 18.1487 of the *Michigan Compiled Laws*.

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We audited the following programs as major programs:

<u>CFDA Number</u>	<u>Program Title</u>	<u>Compliance Opinion</u>
15.904	Historic Preservation Fund Grants-In-Aid	Adverse
45.025	Promotion of the Arts - Partnership Agreements	Unqualified
45.310	Grants to States	Unqualified

A copy of the full report can be obtained by calling 517.334.8050 or by visiting our Web site at: <http://audgen.michigan.gov>



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Thomas H. McTavish, C.P.A.
Auditor General

Scott M. Strong, C.P.A., C.I.A.
Deputy Auditor General



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THOMAS H. MCTAVISH, C.P.A.
AUDITOR GENERAL

June 29, 2007

Dr. William M. Anderson, Director
Department of History, Arts and Libraries
702 West Kalamazoo Street
Lansing, Michigan

Dear Dr. Anderson:

This is our report on the financial audit, including the provisions of the Single Audit Act, of the Department of History, Arts and Libraries (HAL) for the period October 1, 2004 through September 30, 2006.

This report contains our report summary, our independent auditor's report on the financial schedules, and the HAL financial schedules and schedule of expenditures of federal awards. This report also contains our independent auditor's report on internal control over financial reporting and on compliance and other matters, our independent auditor's report on compliance with requirements applicable to each major program and on internal control over compliance in accordance with U.S. Office of Management and Budget Circular A-133, and our schedule of findings and questioned costs. In addition, this report contains HAL's summary schedule of prior audit findings, its corrective action plan, and a glossary of acronyms and terms.

Our findings and recommendations are contained in Section II and Section III of the schedule of findings and questioned costs. The agency preliminary responses are contained in the corrective action plan. The *Michigan Compiled Laws* and administrative procedures require that the audited agency develop a formal response within 60 days after release of the audit report.

We appreciate the courtesy and cooperation extended to us during this audit.

AUDITOR GENERAL

TABLE OF CONTENTS

DEPARTMENT OF HISTORY, ARTS AND LIBRARIES

	<u>Page</u>
Report Summary	1
Report Letter	3
INDEPENDENT AUDITOR'S REPORT AND FINANCIAL SCHEDULES	
Independent Auditor's Report on the Financial Schedules	8
Department of History, Arts and Libraries Financial Schedules	
Schedule of General Fund Revenues	10
Schedule of Sources and Disposition of General Fund Authorizations	11
Notes to the Financial Schedules	12
SUPPLEMENTAL FINANCIAL SCHEDULE	
Schedule of Expenditures of Federal Awards	18
INDEPENDENT AUDITOR'S REPORTS ON INTERNAL CONTROL AND COMPLIANCE	
Independent Auditor's Report on Internal Control Over Financial Reporting and on Compliance and Other Matters	22
Independent Auditor's Report on Compliance With Requirements Applicable to Each Major Program and on Internal Control Over Compliance in Accordance With OMB Circular A-133	24

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

Section I: Summary of Auditor's Results	27
Section II: Findings Related to the Financial Schedules	28
1. Internal Control Over Financial Reporting	28
2. Use of State General Fund/General Purpose Appropriations	29
3. State Aid to Libraries	31
Section III: Findings and Questioned Costs Related to Federal Awards	34
4. Historic Preservation Fund Grants-In-Aid, <i>CFDA</i> 15.904	34

OTHER SCHEDULES

Summary Schedule of Prior Audit Findings	39
Corrective Action Plan	42

GLOSSARY

Glossary of Acronyms and Terms	52
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INDEPENDENT AUDITOR'S REPORT AND
FINANCIAL SCHEDULES



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AUDITOR GENERAL

Independent Auditor's Report on the Financial Schedules

Dr. William M. Anderson, Director
Department of History, Arts and Libraries
702 West Kalamazoo Street
Lansing, Michigan

Dear Dr. Anderson:

We have audited the accompanying financial schedules of the Department of History, Arts and Libraries for the fiscal years ended September 30, 2006 and September 30, 2005, as identified in the table of contents. These financial schedules are the responsibility of the Department'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 and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. 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 the 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 present only the revenues and the sources and disposition of authorizations for the Department of History, Arts and Libraries' General Fund accounts, presented using the current financial resources measurement focus and the modified accrual basis of accounting. Accordingly, these financial schedules do not purport to, and do not, constitute a complete financial presentation of either the Department or the State's General Fund in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial schedules referred to in the first paragraph present fairly, in all material respects, the revenues and the sources and disposition of authorizations of the Department of History, Arts and Libraries for the fiscal years ended September 30, 2006 and September 30, 2005 on the basis of accounting described in Note 1.

In accordance with *Government Auditing Standards*, we have also issued our report dated April 17, 2007 on our consideration of the Department's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The schedule of expenditures of federal awards, required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, is presented for purposes of additional analysis and is not a required part of the Department's financial schedules referred to in the first paragraph. Such information has been subjected to the auditing procedures applied in the audit of the financial schedules and, in our opinion, is fairly stated, in all material respects, in relation to the financial schedules taken as a whole.

AUDITOR GENERAL

April 17, 2007

DEPARTMENT OF HISTORY, ARTS AND LIBRARIES
Schedule of General Fund Revenues
Fiscal Years Ended September 30

	<u>2006</u>	<u>2005</u>
REVENUES		
From federal agencies:		
Institute of Museum and Library Services	\$ 4,536,526	\$ 6,028,288
U.S. Department of the Interior	783,082	821,373
National Endowment for the Arts	673,745	706,550
Other federal funds	54,200	(1,883)
Total from federal agencies	<u>\$ 6,047,553</u>	<u>\$ 7,554,328</u>
From services	254	118
Miscellaneous revenues	<u>2,085,710</u>	<u>1,791,279</u>
Total revenues	<u><u>\$ 8,133,517</u></u>	<u><u>\$ 9,345,725</u></u>

The accompanying notes are an integral part of the financial schedules.

DEPARTMENT OF HISTORY, ARTS AND LIBRARIES
Schedule of Sources and Disposition of General Fund Authorizations
Fiscal Years Ended September 30

	<u>2006</u>	<u>2005</u>
SOURCES OF AUTHORIZATIONS (Note 2)		
General purpose appropriations	\$ 41,821,900	\$ 45,176,700
Balances carried forward	1,352,520	1,660,553
Restricted financing sources	9,440,601	10,543,368
Less: Interfund expenditure reimbursements	<u>(1,318,040)</u>	<u>(1,258,047)</u>
 Total	 <u>\$ 51,296,981</u>	 <u>\$ 56,122,574</u>
 DISPOSITION OF AUTHORIZATIONS (Note 2)		
Gross expenditures and transfers out	\$ 51,380,500	\$ 56,005,797
Less: Interfund expenditure reimbursements	<u>(1,318,040)</u>	<u>(1,258,047)</u>
Net expenditures and transfers out	<u>\$ 50,062,460</u>	<u>\$ 54,747,750</u>
 Balances carried forward:		
Encumbrances	\$ 51,341	\$ 106,638
Restricted revenues - authorized	1,117,552	781,435
Restricted revenues - not authorized or used	<u>35,224</u>	<u>464,448</u>
Total balances carried forward	<u>\$ 1,204,117</u>	<u>\$ 1,352,520</u>
Balances lapsed	<u>\$ 30,404</u>	<u>\$ 22,303</u>
 Total	 <u>\$ 51,296,981</u>	 <u>\$ 56,122,574</u>

The accompanying notes are an integral part of the financial schedules.

Notes to the Financial Schedules

Note 1 Significant Accounting Policies

a. Reporting Entity

The accompanying financial schedules report the results of the financial transactions of the Department of History, Arts and Libraries (HAL) for the fiscal years ended September 30, 2006 and September 30, 2005. The financial transactions of HAL are accounted for principally in the State's General Fund and are reported on in the *State of Michigan Comprehensive Annual Financial Report (SOMCAFR)*.

The notes accompanying these financial schedules relate directly to HAL. The *SOMCAFR* provides more extensive disclosures regarding the State's significant accounting policies; budgeting, budgetary control, and legal compliance; and pension benefits and other postemployment benefits.

The mission of HAL is to enrich the quality of life for Michigan residents by providing access to information, preserving and promoting Michigan's heritage, and fostering cultural creativity.

The financial schedules do not include the financial activities related to the microfilm funds, which are accounted for in the Office Services Revolving Fund, an internal service fund. This Fund is audited separately.

The Mackinac Island State Park Commission (MISPC) is a component unit of the State of Michigan and is reported on in the *SOMCAFR*. MISPC is funded by the Mackinac Island State Park Fund, airport and park operation fees, and General Fund support received through HAL. A portion of MISPC's financial transactions are recorded in the State's accounting system within HAL's accounts. These financial transactions are the responsibility of MISPC. HAL receives an annual interfund expenditure reimbursement from MISPC for the portion of MISPC expenditures contained in HAL's accounts that are funded by the Mackinac Island State Park Fund and airport and park operation fees.

b. Measurement Focus, Basis of Accounting, and Presentation

The financial schedules contained in this report are presented using the current financial resources measurement focus and the modified accrual basis of accounting, as provided by accounting principles generally accepted in the United States of America. Under the modified accrual basis of accounting, revenues are recognized as they become susceptible to accrual, generally when they are both measurable and available. Revenues are considered to be available when they are collected within the current period or soon enough thereafter to pay liabilities of the current period. Expenditures generally are recorded when a liability is incurred; however, certain expenditures related to long-term obligations are recorded only when payment is due and payable.

The accompanying financial schedules present only the revenues and the sources and disposition of authorizations for HAL's General Fund accounts. Accordingly, these financial schedules do not purport to, and do not, constitute a complete financial presentation of either HAL or the State's General Fund in conformity with accounting principles generally accepted in the United States of America.

Note 2 Schedule of Sources and Disposition of General Fund Authorizations

The various elements of the schedule of sources and disposition of General Fund authorizations are defined as follows:

- a. General purpose appropriations: Original appropriations and any supplemental appropriations that are financed by General Fund/general purpose revenues. HAL's General Fund/general purpose appropriations decreased by approximately \$3.4 million from fiscal year 2004-05 to fiscal year 2005-06.
- b. Balances carried forward: Authorizations for multi-year projects, encumbrances, restricted revenues - authorized, and restricted revenues - not authorized or used that were not spent as of the end of the prior fiscal year. These authorizations are available for expenditure in the current fiscal year for the purpose of the carry-forward without additional legislative authorization, except for the restricted revenues - not authorized or used. Significant balances carried forward into HAL in fiscal year 2005-06 included \$368,093 from Grants to States (CFDA 45.310)

federal grants; \$329,079 from Library of Michigan user fees; \$175,461 from Heritage Publications magazine subscriptions; and \$118,374 from History, Arts and Libraries Service Fund. Significant balances carried forward into HAL in fiscal year 2004-05 included \$469,544 from Library of Michigan user fees; \$443,118 from Heritage Publications magazine subscriptions; \$249,507 from Museum Store operations; and \$182,585 from arts grant application fees.

- c. Restricted financing sources: Collections of restricted revenues and restricted transfers, net of restricted interfund expenditure reimbursements, to finance programs as detailed in the appropriations act. These financing sources are authorized for expenditure up to the amount appropriated. Depending upon program statute, any amounts received in excess of the appropriation are, at year-end, either converted to general purpose financing sources and made available for general appropriation in the next fiscal year or carried forward to the next fiscal year as either restricted revenues - authorized or restricted revenues - not authorized or used. HAL's significant restricted financing sources for fiscal year 2005-06 included \$4,536,526 from the Grants to States federal grants; \$1,187,679 from the Mackinac Island State Park Fund; \$783,082 from Historic Preservation Fund federal grants; \$673,745 from National Endowment for the Arts funds; \$624,882 from Heritage Publications magazine subscriptions; and \$477,391 from Museum Store operations. HAL's significant restricted financing sources for fiscal year 2004-05 included \$6,028,288 from Grants to States federal grants; \$1,038,817 from the Mackinac Island State Park Fund; \$821,373 from Historic Preservation Fund federal grants; \$706,550 from National Endowment for the Arts funds; \$522,389 from Heritage Publications magazine subscriptions; and \$455,939 from Museum Store operations.
- d. Interfund expenditure reimbursements: Repayments from the funds responsible for particular expenditures or expenses to the funds that initially paid for them. Significant expenditure reimbursements of \$1,187,679 and \$1,038,817 were received from the Mackinac Island State Park Fund for fiscal years 2005-06 and 2004-05, respectively.
- e. Encumbrances: Authorizations carried forward to finance payments for goods or services ordered during the fiscal year but not received by fiscal

year-end. These authorizations are generally limited to obligations funded by general purpose appropriations.

- f. Restricted revenues - authorized: Revenues that, by statute or the State Constitution, are restricted and authorized for use to a particular program or activity. Generally, these revenues may be expended upon receipt without additional legislative authorization. Significant restricted revenues - authorized for HAL in fiscal year 2005-06 included \$465,445 from Library of Michigan user fees; \$286,773 from the History, Arts and Libraries Service Fund; and \$238,956 from Heritage Publications magazine subscriptions. Significant restricted revenues - authorized for HAL in fiscal year 2004-05 included \$329,079 from Library of Michigan user fees; \$172,794 from Heritage Publications magazine subscriptions; and \$118,374 from the History, Arts and Libraries Service Fund.
- g. Restricted revenues - not authorized or used: Revenues that, by statute, are restricted for use to a particular program or activity. Generally, the expenditure of the restricted revenues is subject to annual legislative appropriation. Significant restricted revenues - not authorized or used for HAL in fiscal year 2004-05 included \$368,093 from Grants to States federal grants.
- h. Balances lapsed: Authorizations that were unexpended and unobligated at the end of the fiscal year. These amounts are available for legislative appropriation in the subsequent fiscal year.

Note 3 Compliance With the Management and Budget Act and the State Aid to Public Libraries Act

The Office of the Auditor General concluded that, as of September 30, 2006, HAL was not in compliance with the Management and Budget Act (specifically, Section 18.1460 of the *Michigan Compiled Laws*), which requires that State agencies establish an indirect cost rate and charge indirect costs to all grants, contracts, and awards (Finding 2). The amounts potentially recoverable as indirect cost revenues could not be estimated because HAL had not established an indirect cost rate and also because HAL had not charged all eligible payroll-related expenditures to federal programs.

Also, the Office of the Auditor General questioned whether HAL was in compliance with the State Aid to Public Libraries Act (specifically, Section 397.566(2) of the *Michigan Compiled Laws*) during the audit period (Finding 3). HAL distributed \$7.9 million in State aid to public libraries under this section during fiscal years 2005-06 and 2004-05.

SUPPLEMENTAL
FINANCIAL SCHEDULE

DEPARTMENT OF HISTORY, ARTS AND LIBRARIES
Schedule of Expenditures of Federal Awards (1)
For the Period October 1, 2004 through September 30, 2006

Federal Agency/Program	CFDA (2) Number	Pass-Through Identification Number	For the Fiscal Year Ended September 30, 2005		
			Directly Expended	Distributed to Subrecipients	Total Expended and Distributed
<u>U.S. Department of the Interior</u>					
Direct Programs:					
Historic Preservation Fund Grants-In-Aid	15.904		\$ 733,989	\$ 77,896	\$ 811,885
Save America's Treasures	15.929				0
Total U.S. Department of the Interior			\$ 733,989	\$ 77,896	\$ 811,885
<u>U.S. Department of Transportation</u>					
Pass-Through Program:					
Michigan Department of Transportation Highway Planning and Construction	20.205	ENH200300067	\$	\$ 41,752	\$ 41,752
Total U.S. Department of Transportation			\$ 0	\$ 41,752	\$ 41,752
<u>National Endowment for the Arts</u>					
Direct Programs:					
Promotion of the Arts - Grants to Organizations and Individuals	45.024		\$	\$ 30,000	\$ 30,000
Promotion of the Arts - Partnership Agreements	45.025			676,550	676,550
Total National Endowment for the Arts			\$ 0	\$ 706,550	\$ 706,550
<u>National Endowment for the Humanities</u>					
Direct Program:					
Promotion of the Humanities - Federal/State Partnership	45.129		\$ 14,423	\$	\$ 14,423
Total National Endowment for the Humanities			\$ 14,423	\$ 0	\$ 14,423
<u>Institute of Museum and Library Services</u>					
Direct Program:					
Grants to States	45.310		\$ 5,122,718	\$ 537,423	\$ 5,660,141
Total Institute of Museum and Library Services			\$ 5,122,718	\$ 537,423	\$ 5,660,141
<u>National Archives and Records Administration</u>					
Direct Program:					
National Historical Publications and Records Grants	89.003		\$ 430	\$	\$ 430
Total National Archives and Records Administration			\$ 430	\$ 0	\$ 430
Total Expenditures of Federal Awards			\$ 5,871,560	\$ 1,363,621	\$ 7,235,181

(1) Basis of Presentation: This schedule presents the federal grant activity for the Department of History, Arts and Libraries on the modified accrual basis of accounting and in accordance with the requirements of U.S. Office of Management and Budget (OMB) Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the financial schedules.

(2) CFDA is defined as *Catalog of Federal Domestic Assistance*.

<u>For the Fiscal Year Ended September 30, 2006</u>			Total Expended and Distributed
<u>Directly Expended</u>	<u>Distributed to Subrecipients</u>	<u>Total Expended and Distributed</u>	<u>for the Two-Year Period</u>
\$ 718,526	\$ 74,044	\$ 792,570	\$ 1,604,455
26,815		26,815	26,815
\$ 745,341	\$ 74,044	\$ 819,385	\$ 1,631,270

\$	\$ 1,980	\$ 1,980	\$ 43,732
\$ 0	\$ 1,980	\$ 1,980	\$ 43,732

\$ 8,000	\$ 15,000	\$ 23,000	\$ 53,000
	650,745	650,745	1,327,295
\$ 8,000	\$ 665,745	\$ 673,745	\$ 1,380,295

\$	\$	\$ 0	\$ 14,423
\$ 0	\$ 0	\$ 0	\$ 14,423

\$ 4,904,619	\$	\$ 4,904,619	\$ 10,564,760
\$ 4,904,619	\$ 0	\$ 4,904,619	\$ 10,564,760

\$	\$ 4,237	\$ 4,237	\$ 4,667
\$ 0	\$ 4,237	\$ 4,237	\$ 4,667

<u>\$ 5,657,960</u>	<u>\$ 746,006</u>	<u>\$ 6,403,966</u>	<u>\$ 13,639,147</u>
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INDEPENDENT AUDITOR'S REPORTS ON
INTERNAL CONTROL AND COMPLIANCE



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Independent Auditor's Report on Internal Control Over Financial Reporting and on Compliance and Other Matters

Dr. William M. Anderson, Director
Department of History, Arts and Libraries
702 West Kalamazoo Street
Lansing, Michigan

Dear Dr. Anderson:

We have audited the financial schedules of the Department of History, Arts and Libraries for the fiscal years ended September 30, 2006 and September 30, 2005, as identified in the table of contents, and have issued our report thereon dated April 17, 2007. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Department's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial schedules and not to provide an opinion on the internal control over financial reporting. However, we noted a matter involving the internal control over financial reporting and its operation that we consider to be a reportable condition. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the Department's ability to initiate, record, process, and report financial data consistent with the assertions of management in the financial schedules. The reportable condition is described in the accompanying schedule of findings and questioned costs as Finding 1.

A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial schedules being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and,

accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we believe that the reportable condition identified in the previous paragraph is not a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Department's financial schedules are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial schedule amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed an instance of noncompliance or other matters that is required to be reported under *Government Auditing Standards* and which is described in the accompanying schedule of findings and questioned costs as Finding 2. In addition, we noted a reportable condition, as described in Finding 3.

This report is intended solely for the information and use of the State's management, the Legislature, federal awarding agencies, and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

AUDITOR GENERAL

April 17, 2007



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Independent Auditor's Report on Compliance With
Requirements Applicable to Each Major Program
and on Internal Control Over Compliance in
Accordance With OMB Circular A-133

Dr. William M. Anderson, Director
Department of History, Arts and Libraries
702 West Kalamazoo Street
Lansing, Michigan

Dear Dr. Anderson:

Compliance

We have audited the compliance of the Department of History, Arts and Libraries with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) *Circular A-133 Compliance Supplement* that are applicable to each major federal program for the two-year period ended September 30, 2006. The Department's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each major federal program is the responsibility of the Department's management. Our responsibility is to express an opinion on the Department's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to in the previous paragraph that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Department's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of the Department's compliance with those requirements.

As described in Finding 4 in the accompanying schedule of findings and questioned costs, the Department did not comply with requirements regarding allowable costs/cost principles; matching, level of effort, and earmarking; and reporting that are applicable to its Historic Preservation Fund Grants-In-Aid. Compliance with such requirements is necessary, in our opinion, for the Department to comply with the requirements applicable to that program.

In our opinion, because of the effects of the noncompliance described in the previous paragraph, the Department of History, Arts and Libraries did not comply, in all material respects, with the requirements referred to in the first paragraph that are applicable to its Historic Preservation Fund Grants-In-Aid. Also, in our opinion, the Department of History, Arts and Libraries complied, in all material respects, with the requirements referred to in the first paragraph that are applicable to each of its other major federal programs for the two-year period ended September 30, 2006.

Internal Control Over Compliance

The management of the Department is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the Department's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on the internal control over compliance in accordance with OMB Circular A-133.

We noted a matter involving the internal control over compliance and its operation that we consider to be a reportable condition. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over compliance that, in our judgment, could adversely affect the Department's ability to administer a major federal program in accordance with the applicable requirements of laws, regulations, contracts, and grants. The reportable condition is described in the accompanying schedule of findings and questioned costs as Finding 4.

A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with the applicable requirements of laws, regulations, contracts, and grants caused by error or fraud that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we consider the reportable condition identified in the previous paragraph to be a material weakness.

This report is intended solely for the information and use of the State's management, the Legislature, federal awarding agencies, and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

AUDITOR GENERAL

April 17, 2007

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

Section I: Summary of Auditor's Results

Financial Schedules

Type of auditor's report issued: Unqualified*

Internal control* over financial reporting:

Material weaknesses* identified? No

Reportable conditions* identified that are not considered to be material weaknesses? Yes

Noncompliance or other matters material to the financial schedules? Yes

Federal Awards

Internal control over major programs:

Material weaknesses identified? Yes

Reportable conditions identified that are not considered to be material weaknesses? None reported

Type of auditor's report issued on compliance for major programs:

Unqualified for all major programs except for Historic Preservation Fund Grants-In-Aid, which is adverse*.

Any audit findings disclosed that are required to be reported in accordance with U.S. Office of Management and Budget (OMB) Circular A-133, Section 510(a)? Yes

Identification of major programs:

<u>CFDA Number</u>	<u>Name of Federal Program</u>
15.904	Historic Preservation Fund Grants-In-Aid
45.025	Promotion of the Arts - Partnership Agreements
45.310	Grants to States

* See glossary at end of report for definition.

Dollar threshold used to distinguish between type A and type B programs: \$409,174

Auditee qualified as a low-risk auditee*? No

Section II: Findings Related to the Financial Schedules

FINDING (2510701)

1. Internal Control Over Financial Reporting

The Department of History, Arts and Libraries' (HAL's) internal control over financial reporting did not ensure that transactions were accurately recorded. As a result, federal revenues in HAL's financial schedules were overstated by \$377,582 in fiscal year 2005-06 and understated by \$377,635 in fiscal year 2004-05.

The Management and Budget Act (specifically, Sections 18.1485(1) and 18.1485(2)(c) of the *Michigan Compiled Laws*) requires HAL to establish and maintain an effective system of internal accounting and administrative control over its assets, liabilities, revenues, and expenditures.

During fiscal year 2004-05, HAL earned federal revenues for the Grants to States Program (CFDA 45.310) and the Historic Preservation Fund Grants-In-Aid Program (CFDA 15.904) based on eligible federal expenditures of approximately \$6.8 million. HAL recorded this amount in the State's accounting system as federal revenue. However, at fiscal year-end, HAL reclassified \$377,635 of the previously claimed federally eligible expenditures as State General Fund/general purpose expenditures, without a corresponding adjustment for earned federal revenues. As a result, HAL's federal revenues were overstated by \$377,635 at September 30, 2005 and understated by \$377,582 at September 30, 2006.

HAL offset the \$377,635 federal revenue overstatement from fiscal year 2004-05 by not recording \$377,582 in federal revenue that was earned, based on expenditures, during the subsequent fiscal year (i.e., fiscal year 2005-06). As a result, HAL's federal revenues were understated by \$377,582 at September 30, 2006.

* See glossary at end of report for definition.

RECOMMENDATION

WE AGAIN RECOMMEND THAT HAL IMPROVE ITS INTERNAL CONTROL OVER FINANCIAL REPORTING TO ENSURE THAT TRANSACTIONS ARE ACCURATELY RECORDED.

FINDING (2510702)

2. Use of State General Fund/General Purpose Appropriations

HAL did not maximize its use of federal sources of financing by billing for indirect costs and by expending federal funds before using State General Fund/general purpose appropriations. As a result, HAL used State General Fund/general purpose appropriations to pay for indirect, administrative, and direct federal program costs that could have been paid for with federal funds.

HAL is responsible under the Management and Budget Act (specifically, Sections 18.1460 and 18.1395 of the *Michigan Compiled Laws*) to ensure that it maximizes the use of federal and other restricted funds by recovering indirect costs when applicable and by expending all available federal funds and other restricted funds before using State General Fund/general purpose appropriations.

Our review of HAL's use of federal funding sources disclosed:

- a. HAL did not establish an indirect cost rate and did not charge indirect costs to grants, contracts, and awards, including those received from the federal government.

Section 18.1460 of the *Michigan Compiled Laws* requires each State agency to establish an indirect cost rate and to charge indirect costs to all grants, contracts, and awards. Appendix A of Title 2, Part 225 of the *Code of Federal Regulations* (OMB Circular A-87*) allows grant recipients to recover indirect costs from the federal grant funds received.

Indirect costs are generally recovered for departmental overhead; Statewide expenditures under the Statewide Cost Allocation Plan; agency direct billed costs, such as retirement and vehicle charges; and agency central support costs, such as accounting, payroll, and information systems.

* See glossary at end of report for definition.

During our audit period, HAL expended approximately \$13.6 million from 8 separate federal programs, including payroll-related expenditures of approximately \$1.5 million for 3 federal programs.

Our prior audit recommended that HAL establish an indirect cost rate. In its corrective action plan sent to the Office of the State Budget, HAL stated that it would establish and apply an indirect cost rate if federal funds were available and if it did not cost more to revise and maintain an indirect cost rate than would be recovered from applying such a rate. However, HAL had not determined what its indirect cost rate would be or how much it would cost to revise and maintain an indirect cost rate.

- b. HAL used State General Fund/general purpose appropriations when federal funds were available.

Section 18.1395 of the *Michigan Compiled Laws* requires that, in an appropriation financed by multiple sources, any State General Fund/general purpose appropriation shall be used only after the available federal funds have been expended.

Our review disclosed:

- (1) As stated in Finding 1, during fiscal year 2004-05, HAL reclassified expenditures totaling \$377,635 as State General Fund/general purpose expenditures that had originally been charged against two federally funded programs. By reclassifying these expenditures, HAL avoided the lapsing of these General Fund appropriations.
- (2) HAL charged \$107,500 in eligible Grants to States (*CFDA* 45.310) direct program costs as administrative costs. As a result, HAL had reached its 4% cap on administrative costs and was unable to charge any more administrative (including indirect) costs to the grant. If HAL had charged all its direct costs as direct charges, HAL could have charged an additional \$107,500 in administrative (including indirect) costs incurred to the federal grant.
- (3) HAL did not charge all eligible payroll-related expenditures to Grants to States (*CFDA* 45.310) and did not charge any payroll-related

expenditures to Promotion of the Arts - Partnership Agreements grants (CFDA 45.025).

Federal regulations for the Grants to States Program and the Promotion of the Arts - Partnership Agreements Program allowed HAL to charge the grant awards for payroll-related expenditures. However, HAL instead funded these payroll costs with State General Fund/general purpose sources.

RECOMMENDATIONS

WE AGAIN RECOMMEND THAT HAL ESTABLISH AN INDIRECT COST RATE AND CHARGE INDIRECT COSTS TO GRANTS, CONTRACTS, AND AWARDS AS REQUIRED BY STATE LAW.

We also recommend that HAL expend federal funds before using State General Fund/general purpose appropriations as required by State law.

FINDING (2510703)

3. State Aid to Libraries

HAL should obtain a formal Attorney General opinion to determine whether State aid payments to public libraries under Section 397.566(2) of the *Michigan Compiled Laws* were distributed in accordance with State law. HAL distributed approximately \$7.9 million to public libraries under this section during fiscal years 2005-06 and 2004-05.

During our audit period, HAL distributed State aid payments under the following sections of the State Aid to Public Libraries Act (Sections 397.551 - 397.576 of the *Michigan Compiled Laws*):

- Cooperative library 50 cents per capita payments (Section 397.563 of the *Michigan Compiled Laws*).
- Public library belonging to a cooperative library 50 cents per capita payments (Section 397.566(4) of the *Michigan Compiled Laws*).

- Cooperative library density payments (Section 397.566(4) of the *Michigan Compiled Laws*).
- County library reimbursable salary payments (Section 397.566(5) of the *Michigan Compiled Laws*).
- Public library 50 cents per capita payments (Section 397.566(2) of the *Michigan Compiled Laws*).

However, our review disclosed that Section 397.566(2) provided that a public library shall receive a 50 cents per capita payment only during fiscal year 1978-79:

A public library shall receive 50 cents per capita from state aid **during the fiscal year 1978-79** if in the prior year the public library received local support equal to that required by this act, the library has not reduced its local support by an amount equal to or larger than the state aid from the previous year without the approval of the department, and the library meets the minimum standards established by the department and this act. [Emphasis added.]

Even though this section specifically states that it applies to only fiscal year 1978-79, HAL continued to make payments under this section. In fiscal years 2005-06 and 2004-05, HAL paid \$7.9 million to libraries under this section.

Because HAL made State aid payments under Section 397.566(2) of the *Michigan Compiled Laws*, HAL did not have sufficient legislative appropriations to fully fund all of the State aid payment funding components. Consequently, HAL prorated its State aid payments to libraries in both fiscal years 2005-06 and 2004-05 based on the amount of funding that was available.

HAL's distribution of State aid, by funding component, was as follows:

Funding Component	Section of the <i>Michigan Compiled Laws</i>	Fiscal Years 2005-06 and 2004-05		
		Amount of State Aid Paid	Amount of State Aid That Would Have Been Paid Excluding Section 397.566(2) Payments	Difference
Cooperative library - 50 cents per capita	397.563	\$ 8,669,060	\$ 9,319,271	\$ (650,211)
Public library belonging to a cooperative library - 50 cents per capita	397.566(4)	7,876,827	9,893,902	(2,017,075)
Cooperative library - Density	397.566(4)	630,553	678,004	(47,451)
County library - Reimbursable salaries	397.566(5)	95,396	118,400	(23,004)
Public library - 50 cents per capita (fiscal year 1978-79)	397.566(2) *	7,882,364		7,882,364
Total		<u>\$25,154,200</u>	<u>\$ 20,009,576</u>	<u>\$ 5,144,623</u>

* Includes a distribution of \$6,727 to three public libraries that did not belong to a cooperative library.

HAL informed us that it believed the payments made under Section 397.566(2) of the *Michigan Compiled Laws* since fiscal year 1978-79 were consistent with its interpretation of the intent of the Legislature and in accordance with its *State Aid Guidelines for Michigan Public Libraries*.

RECOMMENDATION

We recommend that HAL obtain a formal Attorney General opinion to determine whether State aid payments to public libraries under Section 397.566(2) of the *Michigan Compiled Laws* were distributed in accordance with State law.

The status of the findings related to the financial schedules that were reported in prior Single Audits* is disclosed in the summary schedule of prior audit findings.

* See glossary at end of report for definition.

Section III: Findings and Questioned Costs* Related to Federal Awards

FINDING (2510704)

4. Historic Preservation Fund Grants-In-Aid, CFDA 15.904

U.S. Department of the Interior	CFDA 15.904 Historic Preservation Fund Grants-In-Aid
Award Number: 26-04-19323 26-05-20424 26-06-21525	Award Period: 10/01/2003 - 09/30/2005 10/01/2004 - 09/30/2006 10/01/2005 - 09/30/2007
	Questioned Costs: \$1,400,758

HAL had not established internal control over the Historic Preservation Fund Grants-In-Aid Program to ensure compliance with federal laws and regulations regarding allowable costs/cost principles; matching, level of effort, and earmarking; and reporting. Our review disclosed material weaknesses in internal control and material noncompliance regarding allowable costs/cost principles; matching, level of effort, and earmarking; and reporting. As a result, we issued an adverse opinion on compliance with federal laws and regulations for the Historic Preservation Fund Grants-In-Aid Program.

Internal control that does not ensure compliance with federal laws and regulations could result in sanctions, disallowances, and/or future reductions of Historic Preservation Fund Grants-In-Aid Program awards.

Expenditures for the Historic Preservation Fund Grants-In-Aid Program totaled approximately \$1.6 million for the two-year period ended September 30, 2006. We identified known questioned costs of \$1,400,758.

* See glossary at end of report for definition.

Our exceptions, by compliance area, are as follows:

a. Allowable Costs/Cost Principles

HAL did not adhere to applicable allowable costs and cost principles in accordance with OMB Circular A-87. Our review disclosed:

- (1) HAL did not obtain a semiannual certification for any of the employees (8 for fiscal year 2005-06 and 9 for fiscal year 2004-05) who were charged 100% to the Historic Preservation Fund Grants-In-Aid Program. Charges to the Program for employees who were charged 100% to the Program were approximately \$1.2 million during the two-year audit period.

In addition, HAL did not obtain these certifications for any of the employees whose payroll costs were used in meeting the matching requirement for the Historic Preservation Fund Grants-In-Aid Program.

OMB Circular A-87 requires employees who are charged 100% to a single grant program or cost objective to certify, at least semiannually, that they worked solely on that single grant program or cost objective. Also, OMB Circular A-87 requires that the salaries and wages of employees that are used to meet cost sharing or matching requirements must be supported in the same manner as those claimed as allowable costs under federal awards.

HAL staff informed us that they believed that the State's payroll time and attendance system, the Data Collection and Distribution System (DCDS), could be used to meet the semiannual certification requirements specified in OMB Circular A-87. However, our review disclosed that DCDS does not provide HAL with sufficient documentation to properly support the certifications required by OMB Circular A-87. In addition, Part 3.4, question 3-19 of the Implementation Guide for OMB Circular A-87 provides that, in order for payroll time and attendance systems to be used to meet certification requirements, the employees' potential assignment to multiple programs or activities may not be within the authority of the supervisor responsible for certifying time and attendance. Because the person responsible for certifying time and attendance within DCDS also has the authority, function, and purview to assign employees to multiple

programs or activities, DCDS cannot be used to meet the semiannual certification requirements.

- (2) HAL's personnel activity reports did not adequately support its distribution of the payroll costs for three employees who worked on multiple State and federal programs during fiscal years 2005-06 and 2004-05. Charges to the Historic Preservation Fund Grants-In-Aid Program for these three employees were based on a predetermined rate and totaled \$219,634 during the two-year audit period.

The employees' biweekly time sheets recorded only the total hours worked. HAL charged its federal grants based on a predetermined rate rather than on actual time. Because HAL did not document the actual hours worked on the federal programs, it could not verify whether the predetermined rate was an accurate reflection of actual federal payroll costs.

OMB Circular A-87 requires employees charged to multiple activities or cost objectives to document and maintain personnel activity reports or equivalent documentation that support the distribution of their salaries or wages. Personnel activity reports or equivalent documentation must reflect an after-the-fact distribution of the actual activity of each employee, must account for total activity for which the employee is compensated, must be prepared at least monthly, and must be signed by the employee.

b. Matching, Level of Effort, and Earmarking

HAL had not established a process to ensure that it limited administrative costs for federal earmarking requirements under the Historic Preservation Fund Grants-In-Aid Program to 25% of the total grant award.

The National Historic Preservation Act requires that the administrative costs charged to the Historic Preservation Fund Grants-In-Aid Program by the State Historic Preservation Office may not exceed 25% of the total grant award. Administrative costs are generally defined as those costs associated with managing the program, other than costs that can be assigned and identified with a specific project or grant activity. HAL awarded grants totaling \$2,636,524; therefore, the Act limited administrative costs to \$659,131.

Total salaries and wages charged to the Historic Preservation Fund Grants-In-Aid Program were approximately \$1.4 million during the two-year audit period. However, HAL did not document the administrative portion associated with these salaries and wages.

c. Reporting

HAL did not submit 2 (50%) of 4 final project reports to the National Park Service on a timely basis. One of the reports was 83 days late, and the other was 114 days late.

The Historic Preservation Fund annual grant agreements require that HAL submit final project reports involving subgrants of \$25,000 or more to the National Park Service within 90 calendar days of the completion of the project.

RECOMMENDATION

We recommend that HAL establish internal control over the Historic Preservation Fund Grants-In-Aid Program to ensure compliance with federal laws and regulations regarding allowable costs/cost principles; matching, level of effort, and earmarking; and reporting.

The status of the findings related to federal awards that were reported in prior Single Audits is disclosed in the summary schedule of prior audit findings.

OTHER SCHEDULES

DEPARTMENT OF HISTORY, ARTS AND LIBRARIES
Summary Schedule of Prior Audit Findings
As of April 17, 2007

PRIOR AUDIT FINDINGS RELATED TO THE FINANCIAL SCHEDULES

Audit Findings That Have Been Fully Corrected:

Audit Period: October 1, 2002 through September 30, 2004

Finding Number: 250503

Finding Title: Internal Auditors' Independence

Finding: The Department of History, Arts and Libraries' (HAL's) internal audit staff were not organizationally independent.

Comments: HAL was reorganized so that the internal auditor and staff assisting her report directly to, and are under the general supervision of, the HAL director for all activities.

Audit Findings Not Corrected or Partially Corrected:

Audit Period: October 1, 2002 through September 30, 2004

Finding Number: 250501

Finding Title: Internal Control Over Financial Reporting

Finding: HAL's internal control over financial reporting did not ensure that transactions were accurately recorded and that identified errors were corrected.

Comments: HAL requested and received a waiver from the Office of Financial Management (OFM), Department of Management and Budget, granting permission for HAL's financial schedules to differ from the *State of Michigan Comprehensive Annual Financial Report (SOMCAFR)*. HAL is now aware of the accounting events that occur when using different transaction codes to establish work

projects and their effects on year-end closing. HAL is also aware that the measure of materiality for HAL is different from that used by OFM for the *SOMCAFR*. HAL will continue to evaluate its processes in efforts for continuous improvement to internal control over financial reporting.

Audit Period: October 1, 2002 through September 30, 2004

Finding Number: 250502

Finding Title: Indirect Costs

Finding: HAL did not establish an indirect cost rate and charge indirect costs to awards, contracts, and grants, including those received from the federal government.

Comments: HAL will more aggressively pursue, within federal regulatory limits, the direct charging of administrative costs to each federal grant. HAL will reassess its indirect cost rate in light of the impact of this strategy on available grant funds. If federal funds are available and it does not cost more to revise and maintain an indirect cost rate than would be recovered from applying such a rate, HAL will establish and apply a revised indirect cost rate to its awards, contracts and grants.

PRIOR AUDIT FINDINGS RELATED TO FEDERAL AWARDS

Audit Findings That Have Been Fully Corrected:

Audit Period: October 1, 2002 through September 30, 2004

Finding Number: 250504

Finding Title: Unemployment Insurance (Reed Act Distribution), *CFDA* 17.225

Finding: HAL's internal control over the Unemployment Insurance (Reed Act Distribution) program did not ensure compliance with federal laws and regulations regarding allowable costs/cost principles.

Comments: HAL no longer administers Reed Act funding under the Unemployment Insurance program.

Audit Period: October 1, 2002 through September 30, 2004

Finding Number: 250505

Finding Title: State Library Program, *CFDA* 45.310

Finding: HAL's internal control over the State Library Program did not ensure compliance with federal laws and regulations regarding matching, level of effort, and earmarking; reporting; and subrecipient* monitoring.

Comments: HAL has instituted improved management oversight to see that all procedures are being followed. To ensure that the equipment monitoring records are current, inventories were sent by June 30, 2005 to libraries that had purchased equipment with Library Services and Technology Act (LSTA) funds with a last reported fair market value of \$5,000 or more. Equipment inventory confirmations will be sent every two years, until the fair market value of equipment purchased with LSTA funds is recorded as less than \$5,000. Site visits will include the monitoring of subrecipients' compliance with federal requirements.

* See glossary at end of report for definition.

DEPARTMENT OF HISTORY, ARTS AND LIBRARIES

Corrective Action Plan

As of June 26, 2007

FINDINGS RELATED TO THE FINANCIAL SCHEDULES

Finding Number: 2510701

Finding Title: Internal Control Over Financial Reporting

Management Views: The Department of History, Arts and Libraries (HAL) agrees with the finding.

Corrective Action: HAL strengthened the internal control in fiscal year 2005-06 and reported all financial transactions accurately.

Anticipated Completion Date: Completed

Responsible Individual: Janet Laverty, Chief Financial Officer

Finding Number: 2510702

Finding Title: Use of State General Fund/General Purpose Appropriations

Management Views: HAL agrees with part b. and does not agree with part a. of the finding.

- a. In the most recent Single Audit, the Office of the Auditor General recommended that HAL establish an indirect cost rate and charge indirect costs to awards, contracts, and grants, including those received from the federal government. HAL responded that it would more aggressively pursue, within federal regulatory limits, the direct charging of administrative costs to each federal grant and that HAL would reassess its indirect cost rate in light of the impact of this strategy on

available grant funds. If federal funds are available and it does not cost more to revise and maintain an indirect cost rate than would be recovered from applying such a rate, HAL would establish and apply a revised indirect cost rate to its awards, contracts, and grants.

The corrective action plan was prepared after meeting with the Office of the State Budget and was accepted by the Office of Financial Management, Department of Management and Budget, and shared with the Governor, Senate and House Appropriations Committee chairs, and fiscal agencies, as required by statute. At that meeting, it was agreed that HAL would pursue the recovery of indirect costs as a two-step process: first, collect direct costs to help survive the fiscal year 2005-06 budget and, second, establish an indirect rate and collect from that.

HAL has implemented the accepted plan. For example, in 2006, HAL recovered all eligible administrative costs under the Library Services and Technology Act (LSTA) grant award (now known as Grants to States) by charging the maximum allowable administrative costs to its 2005 LSTA grant. The Institute of Museum and Library Services (IMLS) is the federal funding agency for the LSTA program. IMLS posted a document entitled "FAQ: 4% Administrative Costs" to clarify administrative costs allowed under LSTA. It reads:

The statute is quite specific in its language with respect to this issue: No more than 4% of the total amount of funds received under this subchapter for any fiscal year by a State may be used for administrative costs (20 U.S.C.

Section 9132(a)). IMLS and its predecessor funding agency have long defined administrative costs to include expenses normally classified as indirect costs. In general, administrative costs are those necessary to carry out the management of a state's LSTA program in an efficient manner so that it can meet its program goals and objectives. It includes the area of management concerned with the interpretation of policy and translation of it into effective executive action. As distinguished from program activities, such as statewide services and other specific projects, it is that phase of overall program management which plans, organizes, and controls the activities for the accomplishment of the objectives in the long run.

The FAQ provided several examples of typical administrative costs that must come out of the 4% administrative funds. They include:

- Personnel who make management decisions involved in carrying out the LSTA program.
 - Financial management costs, including audit costs.
 - Indirect costs.
- b. HAL agrees with the recommendation and will use all available grant funds before using State General Fund/general purpose funds.

Corrective Action:

HAL will more aggressively pursue, within federal regulatory limits, the direct charging of administrative costs to each federal grant and will reassess the indirect cost rate in light of the impact of this strategy

on available grant funds. If federal funds are available and it does not cost more to revise and maintain an indirect cost rate than would be recovered from applying such a rate, HAL will establish and apply a revised indirect cost rate to its awards, contracts, and grants.

Anticipated Completion Date: September 30, 2007

Responsible Individual: Mark Hoffman, Deputy Department Director

Finding Number: 2510703

Finding Title: State Aid to Libraries

Management Views: HAL does not agree with the finding.

HAL obtained an advisory memorandum from the Department of Attorney General on whether State aid payments to public libraries were distributed in accordance with State law. The memorandum states:

HAL's authority to distribute State aid to public libraries is derived from each year's appropriations act, and subsection 16(2) does not limit how HAL may distribute the State aid to public libraries. . . .

The Auditor General's reading of subsection 16(2) . . . does not take into account the dual nature of the subsection as both a substantive act and an appropriations act. Appropriations are only valid for the current and next ensuing fiscal year. After that time, the appropriation is not invalid, but only expresses an intent to appropriate. When the Legislature enacted subsection 16(2), it limited the appropriation contained in that subsection to fiscal year 1978-79. But the Legislature did not and could not limit future Legislatures from appropriating the same amount of State aid to public libraries under the same standards

set forth in subsection 16(2). One Legislature cannot bind the power of its successor.

The Legislature appropriates funds to HAL under an appropriations act and not under the State Aid to Public Libraries Act. HAL uses the State Aid Guidelines for Michigan Public Libraries to determine how to distribute the State aid to public libraries. The guidelines use the funding levels established in sections 13 and 16 of the Act when it establishes standards for staffing and local funding for libraries to meet to qualify for the State aid. But the fact that the guidelines refer to eligibility for State aid under subsection 16(2) and that subsection 16(2) allocates funds during the fiscal year 1978-79 does not mean that HAL lacks authority to distribute State aid under the same standards set forth in subsection 16(2).

The appropriations acts for fiscal years 2004-2005 and 2005-2006 provide line-item state aid to public libraries, and the acts do not restrict how HAL may distribute the State aid to public libraries.

Corrective Action: None

Anticipated Completion Date: None

Responsible Individual: Mark Hoffman, Deputy Department Director

FINDINGS RELATED TO FEDERAL AWARDS

Finding Number: 2510704

Finding Title: Historic Preservation Fund Grants-In-Aid,
CFDA 15.904

Management Views:

HAL agrees with part c. and does not agree with parts a. and b. of the finding.

HAL does not agree with the introductory statement in the finding. The statement is not supported by the findings and is in direct contradiction to the National Park Service's (NPS's) approval of annual end-of-year reports that certify and document matching, level of effort, earmarking, and reporting for each year during the audit period.

a. Allowable Costs/Cost Principles

NPS, the grantor agency for the Historic Preservation Fund Grants-In-Aid Program, supports HAL's opinion that Michigan's State Historic Preservation Office (SHPO) procedures for timekeeping are in full compliance with U.S. Office of Management and Budget (OMB) Circular A-87.

OMB Circular A-87, Attachment B, Section 8.h., Support of salaries and wages, subsection (3) requires that for employees who work solely on a single federal award, charges for their salaries and wages should be supported by periodic certifications that the employees worked solely on that program for the period covered by the certification. The Circular further requires that the periodic certifications should be prepared at least semiannually and signed by the employee or supervisory official having firsthand knowledge of the work performed by the employee. Subsection (4) requires that for employees who work on multiple activities or cost objectives, a distribution of their salaries or wages should be supported by personnel activity reports or equivalent documentation that meets the

standards in subsection (5) unless a statistical sampling system or other substitute system has been approved by the cognizant federal agency.

At the end of each biweekly period, the SHPO staff and supervisors certify their time and attendance using the Data Collection and Distribution System (DCDS), the State's electronic payroll system. The time and attendance is directly coded to index codes for the federal Historic Preservation Fund grant, nonfederal matching share, or other unrelated activities.

Electronic certification of time and attendance records meets all requirements of NPS for maintaining time and attendance and certification records. The semiannual requirement of OMB Circular A-87, Attachment B, Section 8.h., subsection (3), as well as the monthly documentation required by both subsections (4) and (5) and Part 3.4, question 3-19 of the Implementation Guide for OMB Circular A-87 are clearly met with the biweekly reports that SHPO submits.

HAL understands that the same issue has been an audit finding in other departments. HAL recommends that there be a centralized review of the appropriate use of DCDS as an electronic system for payroll activity reporting.

b. Matching, Level of Effort, and Earmarking

While HAL agrees with the theory of the finding and has instituted procedures to ensure that it met the 25% limit on administrative costs for federal earmarking requirements under the Historic Preservation Fund Grants-In-Aid

Program, HAL did not exceed the 25% maximum in either of the audit periods. Only two persons that were charged to the Historic Preservation Fund Grants-In-Aid Program performed activities that fall under the category "administrative" as defined in the Historic Preservation Fund Grants-In-Aid regulations. Even if these two persons spent 100% of their time on administrative activities, their salaries and benefits were well below the 25% limit. Based on this, HAL met the federal requirement though it did not keep specific documentation of administrative time as noted by the auditors.

c. Reporting

HAL agrees with the finding. Given that the two final project reports in question came in at the close of the fiscal year, HAL submitted them to NPS together with the required end-of-year reports. While an extension for the end-of-year reports was granted by NPS, the extension did not specifically include mention of these two reports. However, NPS accepted and approved the reports without question.

Corrective Action:

- a. While HAL disagrees with the finding, the SHPO staff have instituted additional procedures to ensure full compliance with the reporting requirements of OMB Circular A-87 until a centralized review of the use of DCDS payroll activity reports for timekeeping and certifications has been conducted.
- b. HAL has instituted procedures to ensure that it meets the 25% limit on administrative costs for federal earmarking requirements under the

Historic Preservation Fund Grants-In-Aid Program.

- c. HAL has changed its procedures to submit final project reports to NPS immediately upon closing out the project, ensuring that the reports are submitted to NPS within the specified time period.

Anticipated Completion Date: Completed

Responsible Individual: Brian Conway, State Historic Preservation Officer

GLOSSARY

Glossary of Acronyms and Terms

adverse opinion	<p>An auditor's opinion in which the auditor states that:</p> <ol style="list-style-type: none">a. The financial schedules and/or financial statements presenting the basic financial information of the audited agency are not fairly presented in conformity with the disclosed basis of accounting;b. The financial schedules and/or financial statements presenting supplemental financial information are not fairly stated in relation to the basic financial schedules and/or financial statements. In issuing an "in relation to" opinion, the auditor has applied auditing procedures to the supplemental financial schedules and/or financial statements to the extent necessary to form an opinion on the basic financial schedules and/or financial statements, but did not apply auditing procedures to the extent that would be necessary to express an opinion on the supplemental financial schedules and/or financial statements taken by themselves; orc. The audited agency did not comply, in all material respects, with the cited requirements that are applicable to each major federal program.
<i>CFDA</i>	<i>Catalog of Federal Domestic Assistance.</i>
DCDS	Data Collection and Distribution System.
financial audit	An audit that is designed to provide reasonable assurance about whether the financial schedules and/or financial statements of an audited entity are fairly presented in conformity with the disclosed basis of accounting.
HAL	Department of History, Arts and Libraries.

IMLS	Institute of Museum and Library Services.
internal control	A process, effected by management, designed to provide reasonable assurance regarding the reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations.
low-risk auditee	As provided for in OMB Circular A-133, an auditee that may qualify for reduced federal audit coverage if it receives an annual Single Audit and it meets other criteria related to prior audit results. In accordance with State statute, this Single Audit was conducted on a biennial basis; consequently, this auditee is not considered a low-risk auditee.
LSTA	Library Services and Technology Act.
material misstatement	A misstatement in the financial schedules and/or financial statements that causes the schedules and/or statements to not present fairly the financial position or the changes in financial position or cash flows in conformity with the disclosed basis of accounting.
material noncompliance	Violations of laws and regulations that could have a direct and material effect on major federal programs or on financial schedule and/or financial statement amounts.
material weakness	A reportable condition related to the design or operation of internal control that does not reduce to a relatively low level the risk that either misstatements caused by error or fraud in amounts that would be material in relation to the financial schedules and/or financial statements or noncompliance with applicable requirements of laws, regulations, contracts, and grants that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

MISPC	Mackinac Island State Park Commission.
NPS	National Park Service.
OFM	Office of Financial Management.
OMB	U.S. Office of Management and Budget.
OMB Circular A-87	Guidance regarding "Cost Principles for State, Local, and Indian Tribal Governments," which has been incorporated into the <i>Code of Federal Regulations</i> as Title 2, Part 225 (i.e., federal regulation 2 <i>CFR</i> 225).
questioned cost	A cost that is questioned by the auditor because of an audit finding: (1) which resulted from a violation or possible violation of a provision of a law, regulation, contract, grant, cooperative agreement, or other agreement or document governing the use of federal funds, including funds used to match federal funds; (2) where the costs, at the time of the audit, are not supported by adequate documentation; or (3) where the costs incurred appear unreasonable and do not reflect the actions a prudent person would take in the circumstances.
reportable condition	A matter coming to the auditor's attention relating to a significant deficiency in the design or operation of internal control that, in the auditor's judgment, could adversely affect the entity's ability to (1) initiate, record, process, and report financial data consistent with the assertions of management in the financial schedules and/or financial statements or (2) administer a major federal program in accordance with the applicable requirements of laws, regulations, contracts, and grants. Violations of State laws, regulations, contracts, and grant agreements that should be communicated to management but are not material to the financial schedules and/or financial statements may also be reported.

SHPO	State Historic Preservation Office.
Single Audit	A financial audit, performed in accordance with the Single Audit Act Amendments of 1996, that is designed to meet the needs of all federal grantor agencies and other financial report users. In addition to performing the audit in accordance with the requirements of auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in <i>Government Auditing Standards</i> issued by the Comptroller General of the United States, a Single Audit requires the assessment of compliance with requirements that could have a direct and material effect on a major federal program and the consideration of internal control over compliance with OMB Circular A-133.
<i>SOMCAFR</i>	<i>State of Michigan Comprehensive Annual Financial Report.</i>
subrecipient	A nonfederal entity that expends federal awards received from another nonfederal entity to carry out a federal program.
unqualified opinion	An auditor's opinion in which the auditor states that: <ul style="list-style-type: none"> a. The financial schedules and/or financial statements presenting the basic financial information of the audited agency are fairly presented in conformity with the disclosed basis of accounting; or b. The financial schedules and/or financial statements presenting supplemental financial information are fairly stated in relation to the basic financial schedules and/or financial statements. In issuing an "in relation to" opinion, the auditor has applied auditing procedures to the supplemental financial schedules and/or financial statements to the extent necessary to form an opinion on the basic financial schedules and/or financial

statements, but did not apply auditing procedures to the extent that would be necessary to express an opinion on the supplemental financial schedules and/or financial statements taken by themselves; or

- c. The audited agency complied, in all material respects, with the cited requirements that are applicable to each major federal program.

